**QUARTERLY MEETING OF THE STATE BOARD OF ADMINISTRATION**

**GOVERNOR SCOTT AS CHAIRMAN**
**CHIEF FINANCIAL OFFICER ATWATER AS TREASURER**
**ATTORNEY GENERAL BONDI AS SECRETARY**

**MARCH 20, 2012**

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**www.sbafla.com**

**AMENDED AGENDA**

**ITEM 1.** **REQUEST APPROVAL OF THE MINUTES OF THE JANUARY 18, 2012, AND FEBRUARY 9, 2012, MEETINGS.**

**(See Attachments 1A and 1B)**

**ACTION REQUIRED**

**ITEM 2.** **REQUEST APPROVAL OF A FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $310,000,000 STATE OF FLORIDA, FULL FAITH AND CREDIT, DEPARTMENT OF TRANSPORTATION RIGHT-OF-WAY ACQUISITION AND BRIDGE CONSTRUCTION REFUNDING BONDS, SERIES (TO BE DETERMINED).**

**(See Attachment 2)**

**ACTION REQUIRED**

**ITEM 3.** **REQUEST APPROVAL OF A FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $47,500,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE BONDS, SERIES 2012A AND REQUEST APPROVAL OF A FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $7,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE REFUNDING BONDS, SERIES (TO BE DETERMINED).**

**(See Attachments 3A and 3B)**

**ACTION REQUIRED**

**ITEM 4.** **REQUEST APPROVAL OF A FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $31,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, UNIVERSITY OF FLORIDA DORMITORY REVENUE BONDS, SERIES 2012A.**

**(See Attachment 4)**

**ACTION REQUIRED**

**ITEM 5. REQUEST APPROVAL OF SBA QUARTERLY REPORT REQUIRED BY THE PROTECTING FLORIDA'S INVESTMENTS ACT (PFIA).**

Pursuant to Sections 215.473 and 215.442, F.S., the SBA is required to submit a quarterly report that includes lists of "Scrutinized Companies" with activities in Sudan and Iran. The PFIA prohibits the SBA, acting on behalf of the Florida Retirement System Trust Fund, from investing in, and requires divestment from, companies involved in certain types of business activities in or with Sudan or Iran, (i.e., the "Scrutinized Companies").

**(See Attachment 5)**

**ACTION REQUIRED**

**ITEM 6. REQUEST APPROVAL OF A DRAFT LETTER CERTIFYING THE TRUSTEES HAVE REVIEWED THE AUDITOR GENERAL'S ANNUAL FINANCIAL AUDIT (REPORT NO. 2012-066) OF THE LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (NOW KNOWN AS "FLORIDA PRIME") AND THERE WAS NO CORRECTIVE ACTION REQUIRED BY THE AUDIT.**

Pursuant to Section 218.409(9), F.S., the Auditor General shall conduct an annual financial audit of the trust fund, which shall include testing for compliance with the investment policy. The trustees shall report to the Joint Legislative Auditing Committee that the trustees have reviewed the audit of the trust fund and shall certify that any necessary items are being addressed by a corrective action plan that includes target completion dates.

**(See Attachments 6A and 6B)**

**ACTION REQUIRED**

**ITEM 7. REQUEST APPROVAL OF, AND AUTHORITY TO FILE, A NOTICE OF PROPOSED RULE FOR RULES 19-8.029, F.A.C., INSURER REPORTING REQUIREMENTS AND 19-8.030, F.A.C., INSURER RESPONSIBILITIES, AND TO FILE THESE RULES, ALONG WITH THE INCORPORATED FORMS, FOR ADOPTION IF NO MEMBER OF THE PUBLIC TIMELY REQUESTS A RULE HEARING.**

**(See Attachments 7A – 7K)**

**ACTION REQUIRED**

**ITEM 8. REQUEST APPROVAL OF THE APPOINTMENT OF CHARLES E. COBB TO THE INVESTMENT ADVISORY COUNCIL.**

**(See Attachments 8A and 8B)**

**ACTION REQUIRED**

**ITEM 9. QUARTERLY REPORTS PURSUANT TO 215.44 (2)(e), FLORIDA STATUTES**

- Executive Director/CIO Introductory Remarks – *Ash Williams*
- Major Mandates Investment Performance Review as of December 31, 2011
  *Mike Sebastian & Kristen Doyle – Hewitt EnnisKnupp*

- Standing Reports
  - Investment Advisory Council
  - Participant Local Government Advisory Council
  - Audit Committee
  - Executive Director/CIO

**(See Attachments 9A – 9G)**

**INFORMATION/DISCUSSION ITEMS**

**ITEM 10. FLORIDA RETIREMENT SYSTEM PENSION PLAN (DB) ACTUARIAL VALUATION**

*Sarabeth Snuggs, Division of Retirement*
*Robert Dezube, Milliman & Associates*

**(See Attachment 10)**

**INFORMATION/DISCUSSION ITEM**

**ITEM 11. FLORIDA RETIREMENT SYSTEM PLAN (DB) ASSET LIABILITY AND ASSET ALLOCATION REVIEW**

*Rowland Davis & Mike Sebastian, Hewitt EnnisKnupp*

**(See Attachment 11)**

**INFORMATION/DISCUSSION ITEM**

**ITEM 12. REQUEST APPROVAL OF THE 2012 CORPORATE GOVERNANCE PRINCIPLES AND PROXY VOTING GUIDELINES.**

The SBA's Corporate Governance Principles & Proxy Voting Guidelines are reviewed annually and updated, as needed, to reflect the most current policy application and regulatory requirements. The attached Guidelines document incorporates recent updates including general edits, research citations, and expanded narrative, as well as the addition of one amended voting guideline and one new voting guideline.

**(See Attachments 12A – 12C)**

**ACTION REQUIRED**

**ITEM 13. REQUEST APPROVAL OF THREE REAPPOINTMENTS TO THE INVESTMENT ADVISORY COUNCIL (IAC), LES DANIELS, MICHAEL PRICE, AND GARY WENDT, (S. 215.444, F.S.) AND ONE REAPPOINTMENT TO THE PARTICIPANT LOCAL GOVERNMENT ADVISORY COUNCIL (PLGAC), BARBARA SCOTT, (S.218.409(10)(A), F.S.).**

Les Daniels, Michael Price, and Gary Wendt were previously appointed and approved by the Board of Trustees to serve on the Investment Advisory Council. Barbara Scott was appointed and approved by the Board of Trustees to serve on the Participant Local Government Advisory Council. Pursuant to Section 114.05(1)(e), F.S., they are submitted for reappointment.

**ACTION REQUIRED**

# T H E  C A B I N E T

# S T A T E  O F  F L O R I D A

---

Representing:

FLORIDA PAROLE COMMISSION
CITIZENS PROPERTY INSURANCE CORPORATION
LAW ENFORCEMENT CONSOLIDATION TASK FORCE
DIVISION OF BOND FINANCE
STATE BOARD OF ADMINISTRATION
ADMINISTRATION COMMISSION

The above agencies came to be heard before THE FLORIDA CABINET, the Honorable Governor Scott presiding, in the Cabinet Meeting Room, LL-03, The Capitol, Tallahassee, Florida, on Tuesday, January 18, 2012, commencing at approximately 9:13 a.m.

Reported by:

MARY ALLEN NEEL
Registered Professional Reporter
Florida Professional Reporter
Notary Public

ACCURATE STENOTYPE REPORTERS, INC.
2894 REMINGTON GREEN LANE
TALLAHASSEE, FLORIDA 32308
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APPEARANCES:

REPRESENTING THE FLORIDA CABINET:

RICK SCOTT
Governor

PAM BONDI
Attorney General

JEFF ATWATER
Chief Financial Officer

ADAM PUTNAM
Commissioner of Agriculture

* * *

I N D E X

FLORIDA PAROLE COMMISSION APPOINTMENT


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|---|---|---|
| 1 | Approved | 5 |


CITIZENS PROPERTY INSURANCE CORPORATION
(Presented by SCOTT WALLACE)


| ITEM | ACTION | PAGE |
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LAW ENFORCEMENT CONSOLIDATION TASK FORCE
(Presented by JULIE JONES)


| ITEM | ACTION | PAGE |
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DIVISION OF BOND FINANCE
(Presented by BEN WATKINS)


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STATE BOARD OF ADMINISTRATION
(Presented by ASH WILLIAMS)


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ADMINISTRATION COMMISSION
(Presented by PHILLIP MILLER)


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1 GOVERNOR SCOTT: All right. Now I would like
2 to recognize Ash Williams with the State Board of
3 Administration. Good morning, Ash.
4 MR. WILLIAMS: Good morning, Governor and
5 Trustees. A general update, as usual, to start off
6 today. Through the close on the 16th of fiscal
7 year-to-date, we're down 4.32 percent. That's 38
8 basis points behind target. The balance in the
9 Florida Retirement System Trust Fund is
10 $119.9 billion.
11 To put in perspective for you how miserable
12 the latter half of calendar 2011 was, one of the
13 worst periods on record, when we go back to fiscal
14 year-end, we were at 128.5 billion as of 30 June
15 2011.
16 GOVERNOR SCOTT: Okay. So we were at 128 last
17 June?
18 MR. WILLIAMS: Correct, June 30. So --
19 GOVERNOR SCOTT: And that year we had really
20 good returns; right?
21 MR. WILLIAMS: Yes. So we're down
22 $8.4 billion since that time in fund balance.
23 Now, the other thing to recall is that we're
24 also paying out on net somewhere between 300 and
25 600 million a month cash in benefits, so that's not

1 all investment performance. Some of that is
2 outgoing cash, but the balance is what the balance
3 is. So I wanted to share that with you.
4 Absent any questions, I'll be happy to move
5 ahead with the agenda.
6 GOVERNOR SCOTT: So, Ash, do you -- all right.
7 We had a great year ending June 30, and then we
8 lost; right?
9 MR. WILLIAMS: Yes.
10 GOVERNOR SCOTT: And the average the last two
11 years was a little over 5; right?
12 MR. WILLIAMS: Yes. And, of course, what
13 you're seeing is, you have -- anytime you have a
14 very big move in any one year, whether it's up or
15 down, it will skew the time series for a period of
16 time away from that. So if you look at the 30-year
17 number, it's still quite strong north of 10. As
18 you get into time periods of narrower width that
19 include the drawdown of the '08-'09 crisis, that's
20 where you'll see it.
21 GOVERNOR SCOTT: And '08 was the tough year;
22 right? Was it '08, our worst year?
23 MR. WILLIAMS: Yes. Well, looking at fiscal
24 year.
25 GOVERNOR SCOTT: And '11 was our best in that

1 time frame?
2 MR. WILLIAMS: Yes. Actually, the last two
3 years were quite good, and the one prior was quite
4 bad. So we have to say, "Well, okay. Which one is
5 the predictor?" And we're doing a lot work on the
6 longer term view and whether the debt cycle that
7 we're coming out of is a self-reinforcing negative
8 that goes for a very, very long period of time. If
9 that's true, it's not good. But that's where we
10 are.
11 GOVERNOR SCOTT: How much does the -- the
12 issues with the Euro have an impact on us?
13 MR. WILLIAMS: I think the Euro -- we had an
14 interesting meeting on that yesterday, and the Euro
15 issue is being treated like it's primarily a
16 liquidity issue. It may be worse than that from
17 the standpoint that it may be a fundamental issue
18 when you consider that simply the revenues, the
19 GDPs of the debtor counties that have become so
20 highly levered may not be sufficient to meet P&I to
21 maturity on some of these credits absent some sort
22 of inflation to cheapen the repayment of the debt.
23 That's a much more serious issue than a liquidity
24 issue, and it carries far more significant
25 ramifications with it.

1 And a similar question can be raised about the
2 U.S. We reached a point recently where every
3 single member of the workforce in the United
4 States, both employed and unemployed, can now have
5 attributed to them roughly $100,000 of federal
6 deficit. That's a pretty significant amount. And
7 if you look at only employed workers, that number
8 goes up to 108,000.
9 So arguably, the debt cycle has to correct
10 globally. And when you consider the ramifications
11 of that in terms of credit availability, in terms
12 of spending, in terms of asset values, in terms of
13 incomes that in turn result from spending, general
14 economic activity, the same self-perpetuating cycle
15 that went from the '60s through 2008 could go the
16 other way.
17 GOVERNOR SCOTT: So what you took is just the
18 federal deficit -- or debt divided by the number of
19 people?
20 MR. WILLIAMS: Workforce.
21 GOVERNOR SCOTT: So if it's 100,000 and
22 average interest rates are 5 percent, then every
23 year, just to pay the interest, it's 5,000 per --
24 $5,000 per person. Is that a good way of looking
25 at it?

1 MR. WILLIAMS: Depending on how you want to
2 set the interest rate, yes.
3 GOVERNOR SCOTT: Yeah. And then if you would
4 say -- if the interest rates are like we're getting
5 at the bank, they would be pretty cheap. But if
6 you worry about hyperinflation, then it gets pretty
7 expensive.
8 MR. WILLIAMS: Right. One of the other
9 ramifications of this potential long down cycle --
10 and I think we're in the early days on the work on
11 this, but we just heard Mr. Watkins talking about
12 the refunding environment and the record low rates,
13 et cetera. One of the things that's a byproduct of
14 this kind of a cycle, if this is what's really
15 going on, is that those rates can stay like that
16 for a long time, because regardless of how low the
17 rates are, the economic activity isn't there to
18 drive --
19 GOVERNOR SCOTT: Yeah. Where are you going to
20 put the money.
21 MR. WILLIAMS: Right, exactly.
22 GOVERNOR SCOTT: And that doesn't include the
23 debt for Medicare, Social Security, or other --
24 federal retirement.
25 MR. WILLIAMS: Correct.

1 GOVERNOR SCOTT: It adds up.
2 Okay. Does anybody have any questions?
3 MR. WILLIAMS: Item 1, request approval of the
4 minutes of the October 8, November 5, November 15,
5 and December 6 meetings.
6 GOVERNOR SCOTT: Is there a motion to approve
7 Item 1?
8 ATTORNEY GENERAL BONDI: So moved.
9 CFO ATWATER: Second.
10 GOVERNOR SCOTT: Moved and seconded. Item 1
11 is approved without objection.
12 MR. WILLIAMS: Thank you. Items 2 through 5
13 will mirror items that you just heard and approved
14 on the Division of Bond Finance agenda.
15 Item 2, request a fiscal sufficiency in an
16 amount not exceeding $580 million, State of Florida
17 full faith and credit, Board of Education Public
18 Education Capital Outlay refunding bonds.
19 GOVERNOR SCOTT: So we'll just do -- we'll do
20 2 through 5. Is there a motion? Is there a motion
21 to approve Items 2 through 5?
22 CFO ATWATER: So moved.
23 GOVERNOR SCOTT: Is there a second?
24 ATTORNEY GENERAL BONDI: Second.
25 GOVERNOR SCOTT: All in favor? Moved and

1 seconded. Items 2 through 5 are approved without
2 objection.
3 MR. WILLIAMS: Thank you. Item 6, the staff
4 of the State Board of Administration requests
5 approval for filing of a Notice of Proposed Rule to
6 repeal Rule 19-7. This is relating to the Local
7 Government Surplus Funds Trust Fund and is at this
8 point a redundant rule.
9 GOVERNOR SCOTT: Okay. Is there a motion to
10 approve Item 6?
11 ATTORNEY GENERAL BONDI: So moved.
12 GOVERNOR SCOTT: Is there a second?
13 CFO ATWATER: Second.
14 GOVERNOR SCOTT: Moved and seconded. Item 6
15 is approved without objection.
16 MR. WILLIAMS: Thank you. Item 7, the staff
17 of the State Board requests that the Trustees
18 approve filing of a Notice of Proposed Rule to
19 amend Rule 19-7.002. This is the Investment Policy
20 Statement for the local pool and Pool B. These are
21 investment policies previously reviewed and
22 approved by both the IAC and the Trustees. We're
23 just putting them into rule.
24 GOVERNOR SCOTT: Is there a motion to approve
25 Item 7?

1 CFO ATWATER: So moved.
2 GOVERNOR SCOTT: Is there a second?
3 ATTORNEY GENERAL BONDI: Second.
4 GOVERNOR SCOTT: Moved and seconded. Item 7
5 is approved without objection.
6 MR. WILLIAMS: Thank you. Item 8, request
7 approval of the appointment of Dr. Kurt Gurley as
8 the engineer member of the Advisory Council for the
9 Florida Hurricane Catastrophe Fund. Dr. Gurley is
10 a distinguished associate professor at the
11 University of Florida, and if you read his bio in
12 here and his vita of publications, it's quite
13 impressive. Request approval.
14 GOVERNOR SCOTT: All right. Is there a motion
15 to approve Item 8?
16 ATTORNEY GENERAL BONDI: So moved.
17 GOVERNOR SCOTT: Is there a second?
18 CFO ATWATER: Second.
19 GOVERNOR SCOTT: Moved and seconded. Item 8
20 is approved without objection.
21 ATTORNEY GENERAL BONDI: And if we could just
22 say, I met with Dr. Gurley and was extremely
23 impressed by his qualification.
24 GOVERNOR SCOTT: That's great. All right.
25 MR. WILLIAMS: Thank you. Item 9, I would

1 like to provide an update on two items. The first
2 of these is the Crowe Horwath review
3 recommendations.
4 You will recall at the December SBA-Trustees
5 quarterly meeting, there was a presentation from
6 the IAC, and there was discussion among the
7 Trustees. And while the vast majority of
8 observations in the Crowe report were accepted and
9 are being handled by SBA staff, there were a small
10 minority of their recommendations that really went
11 beyond SBA staff authority and came into the area
12 of governance and really more the territory of the
13 IAC and the Audit Committee.
14 The Trustees asked that IAC Chair Gidel, CFO
15 Atwater, and myself work on these issues and report
16 back subsequently. In addition, we took it upon
17 ourselves to add Rolf Engmann as a representative
18 of the Audit Committee to our little working group,
19 and we had a series of one-off conversations over
20 the holidays and came up with recommendations on
21 two levels to make absolutely crystal clear that
22 there is no conflict issue in the governance
23 structure of the SBA as it relates to the chief
24 risk and compliance officer's reporting to the
25 executive director and chief investment officer.

1 So really, Crowe considered a couple of
2 options there if you want to cure that potential
3 issue, and I would underscore the word "potential."
4 GOVERNOR SCOTT: Right.
5 MR. WILLIAMS: But one would be to separate
6 the duties of the executive director and the CIO.
7 The other would be to modify the reporting
8 relationship in some way so that you cure any
9 potential perception of conflict. The conclusion
10 was that the latter route was the more productive,
11 so we're approaching that -- recommending
12 approaching that on two levels.
13 The first would be to codify in the investment
14 policies for the various primary entities of the
15 State Board the current practice of having the CRCO
16 report no less than quarterly to the IAC, the
17 Trustees, and the Audit Committee, and further, to
18 make clear that the CRCO has access to those bodies
19 at any time for any reason to ensure that that
20 individual's function can be executed in a
21 completely independent and effective manner.
22 The second thing would be to have the
23 individual in the CRCO role subject to an
24 affirmation of their selection, compensation, and
25 retention by the Trustees. The normal day-to-day

1 executive and administrative relationship would
2 continue to reside with the executive director,
3 which addresses the issue of the ability to provide
4 timely response to any issues that should surface.
5 That's very important. But it provides that extra
6 layer of insulation, if you will, or independence
7 just to ensure that nobody can draw a wrong
8 inference about the independence of that role. So
9 those are the recommendations there.
10 The investment policy changes by law must
11 first be approved by the Investment Advisory
12 Council. We have a telephonic meeting of the
13 Council scheduled for 9 a.m. this Friday morning.
14 So presuming the IAC concurs with this direction,
15 then the Trustees would be clear anytime subsequent
16 to Friday's meeting to move forward with those
17 policy changes, and we would bring them to you on
18 an agenda just as we just did with the local
19 government pool policy a moment ago.
20 So unless there are questions on that area, I
21 would like to give you an update on where we are on
22 the inspector general process.
23 GOVERNOR SCOTT: Does anybody have anything?
24 CFO ATWATER: No.
25 MR. WILLIAMS: All right. Very good. Thank

1 you.
2 On the inspector general search, we conducted
3 a national effort there. Florida's chief inspector
4 general, Melinda Miguel, was extremely helpful and
5 made available to us the website of the National
6 Organization of Inspectors General. We advertised
7 the position there, had a number of responses,
8 narrowed that down to a select group, conducted a
9 series of interviews over the past couple of weeks,
10 and basically have focused our selection and are
11 doing some final reference checks now, but we've
12 basically got that one tied out. And presuming
13 that the reference checks are good, we'll be done
14 within the next few days, I think, on that one,
15 assuming we can come to terms.
16 So net, I think we're covered on both those
17 items.
18 Any questions?
19 GOVERNOR SCOTT: Thank you.
20 MR. WILLIAMS: Thank you.
21 Item 9, reaffirmation of the executive
22 director. Item 10. I'm sorry.
23 GOVERNOR SCOTT: All right. So you want me to
24 do this part?
25 MR. WILLIAMS: I recommend adoption.

1 (Laughter.)
2 GOVERNOR SCOTT: Who is that?
3 MR. WILLIAMS: Completely objective.
4 GOVERNOR SCOTT: So this is the reaffirmation
5 of Ash Williams as the executive director.
6 You turned really red, by the way. I hope
7 there's a doctor in the room.
8 MR. WILLIAMS: Right.
9 GOVERNOR SCOTT: So is there a motion to
10 approve Item 10?
11 ATTORNEY GENERAL BONDI: So moved.
12 GOVERNOR SCOTT: Is there a second?
13 CFO ATWATER: Second.
14 GOVERNOR SCOTT: Moved and seconded. Item 10
15 is approved without objection. Congratulations.
16 MR. WILLIAMS: Thank you very much.
17 GOVERNOR SCOTT: All right. Thank you very
18 much.
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End of Section

# T H E  C A B I N E T

## S T A T E  O F  F L O R I D A

**REPRESENTING:**

DEPARTMENT OF HIGHWAY SAFETY AND MOTOR VEHICLE

STATE BOARD OF ADMINISTRATION

BOARD OF TRUSTEES, INTERNAL IMPROVEMENT TRUST FUND

The above agencies came to be heard before the THE FLORIDA CABINET, Honorable Governor Scott presiding, in the Robert Thomas Equestrian Center at the Florida State Fairgrounds, 4800 U.S. Highway 301 North, Tampa, Florida, on Thursday, February 9, 2012, commencing at 9:07 a.m.

REPORTED BY:
Selina Glisson
Digital Court Reporter
Notary Public

*Record Transcripts Incorporated*
*501 East Kennedy Boulevard, Suite 170*
*Tampa, Florida 33602*
*(813) 514-5100*

1 **A P P E A R A N C E S**

2

REPRESENTING THE FLORIDA CABINET

3

RICK SCOTT
4 Governor

5 ADAM H. PUTNAM
Commissioner of Agriculture

6

PAM BONDI,
7 Attorney General

8 JEFF ATWATER
Chief Financial Officer

9

10

SPEAKERS:

11

Julie Jones, Highway Safety and Motor Vehicle
12 Ash Williams, State Board of Administration
Herschel Vinyard, Board of Trustees

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# I N D E X

## HIGHWAY SAFETY AND MOTOR VEHICLE
Presented by Julie Jones


| ITEM | | ACTION | PAGE |
|---|---|---|---|
| 1 | Minutes | Approved | 5 |
| 2 | Quarterly Reports | Approved | 10 |


## STATE BOARD OF ADMINISTRATION
Presented by Ash Williams


| ITEM | | ACTION | PAGE |
|---|---|---|---|
| 1 | Pension Plan: Investment policy statement amendment | Approved | 13 |
| 2 | Investment Plan: Investment policy statement amendment | Approved | 13 |
| 3 | Lawton Chiles Endowment: Investment policy statement amendment | Approved | 13 |
| 4 | Joint Legislative Auditing Committee: Approval of draft letter | Approved | 14 |
| 5 | Investment Advisory Council Appointment of William H. Harrell, Jr | Approved | 15 |


## BOARD OF TRUSTEE
Presented by Herchel Vinyard


| ITEM | | ACTION | PAGE |
|---|---|---|---|
| 1 | Minutes | Approved | 16 |
| 2 | Rule Repeals | Approved | 17 |
| 3 | Nativity Lutheran Church Land Exchange | Approved | 19 |
| 4 | Oldcastle Limerock Mining Lease | Approved | 20 |

CERTIFICATE OF COURT REPORTER 21

motion to approve Item Two?

ATTORNEY GENERAL BONDI: So moved.

CHIEF FINANCIAL OFFICER ATWATER: So moved.

GOVERNOR SCOTT: Is there a second? Moved and seconded. Item Two is approved without objection.

Thank you very much, Julie.

MS. JONES: Thank you all. I appreciate your support.

GOVERNOR SCOTT: Enjoy the fair.

(Applause.)

(The following excerpt of the meeting commencing at 10:04 a.m. is as follows:)

GOVERNOR SCOTT: Next, I'd like to recognize Ash Williams with the State Board of Administration. Good morning, Ash. You can't have -- you cannot wear a bow tie at the fair.

(Laughter.)

MR. WILLIAMS: Well, I thought I might apply for a job as a barker.

GOVERNOR SCOTT: Oh.

MR. WILLIAMS: Get a cane and a hat perhaps.

GOVERNOR SCOTT: I don't think you'll sell as much of this with the bow tie.

CHIEF FINANCIAL OFFICER ATWATER: If I can add, though, Ash was watching the agenda and when Julie was sitting down you said, "I'd next like to introduce," and he stood up, "a

very nice young man," and he just sat right back down.

MR. WILLIAMS: Yeah.

(Laughter)

MR. WILLIAMS: Exactly right. So with that humble beginning, fiscal year to date, the Florida Retirement System Trust Fund is up 15 basis points, that's 43 basis points behind target. The balance currently stands at 124.9 billion, which is up from where we were at our last meeting. To put that in perspective, at fiscal year end June 30, 2011, we were 128.5 billion. We have since had net distributions of 3.6 billion, which coincidentally exactly matches the difference between those two numbers. To put it in perspective for calendar year end, we're at 118.2 billion at calendar year end. So unless there are questions on that information we will press on.

GOVERNOR SCOTT: That's great. My biggest concern, I think everyone's concern is, that is there -- our biggest concern is that we have a pension plan right now that's under-funded --

MR. WILLIAMS: Correct.

GOVERNOR SCOTT: -- and for the last 10 years, at least, we've not been able to get the returns that the pension -- not your expectations, but the pension plan expectations is 7.75 percent return and with -- you worked very hard, but it's -- we've not been able to do that and so

we're getting further and further behind, so -- but I know you're working hard at it.

MR. WILLIAMS: The other key variable, of course, is funding and benefit cost. And there have been reforms made, at least in the benefit cost area, and hopefully as the state's economy comes back the funding can progress a bit as well. Items One, Two, and Three on today's agenda are all related and these are the investment policy changes that are following onto the conversation at the January 18 trustees meeting regarding enhanced independence for the Chief Risk and Compliance Officer function. So we have basically conducted a meeting of the Investment Advisory Council, which took place on January 20. These policy recommendations were unanimously approved by the IAC in that meeting and so we have today, before you, the final policies to be adopted.

So Items One, Two, and Three are the Florida Retirement System Pension Plan, the Investment Plan, and a Lawton Chiles Endowment, respectively, and would request approval.

GOVERNOR SCOTT: All right. Is there a motion to approve Items One, Two, and Three?

ATTORNEY GENERAL BONDI: So moved.

GOVERNOR SCOTT: Is there a second?

CHIEF FINANCIAL OFFICER ATWATER: Second.

GOVERNOR SCOTT: Did you want to add anything?

CHIEF FINANCIAL OFFICER ATWATER: I just need to --

GOVERNOR SCOTT: Do you want to add something?

CHIEF FINANCIAL OFFICER ATWATER: If I might, yeah; and I really appreciate this, but I -- if you could state this because we've talked about this, Ash, that the decisions that we've just made now and what the IAC brought to us and we're affirming is it meets the concern that Crowe Horwath could addressed, so they were satisfied with the decisions --

MR. WILLIAMS: Yes, they were.

CHIEF FINANCIAL OFFICER ATWATER: -- that have been made to address the design, the structure design.

MR. WILLIAMS: Yes, they were and they certified as much in writing.

CHIEF FINANCIAL OFFICER ATWATER: Very good, thank you.

MR. WILLIAMS: Thank you.

GOVERNOR SCOTT: Okay. Moved and seconded. Items One, Two, and Three are approved without objection.

MR. WILLIAMS: Thank you. Item Four: Request approval of a draft letter to the Joint Legislative Auditing Committee affirming that the SBA trustees have reviewed and approved the monthly Florida Prime and Fund B management reports and actions taken, if any, to address any material impacts. The reports are here there are no material impacts and we have continued to progress on Fund B distributions as

well.

GOVERNOR SCOTT: Great. Is there a motion to approve Item Four?

CHIEF FINANCIAL OFFICER ATWATER: So moved.

GOVERNOR SCOTT: Is there a second?

ATTORNEY GENERAL BONDI: Second.

GOVERNOR SCOTT: Moved and seconded, Item Four is approved without objection.

MR. WILLIAMS: Thank you. Item Five: Request approval of the appointment of William H. Harrell, Jr. to the Investment Advisory Council. Mr. Harrell is here today. He will join us as a distinguished private equity investor and has things in common with other people who have appeared today, notably connections in Gainesville.

GOVERNOR SCOTT: Where does he live?

MR. WILLIAMS: Where does he live? Let's see -- nearby.

GOVERNOR SCOTT: That's what I figured.

ATTORNEY GENERAL BONDI: Find out who nominated him?

GOVERNOR SCOTT: Yeah. I wonder where he lives. Oh, Tampa, probably.

(Laughter)

MR. HARRELL: Well, I am very appreciative of the honor that you all are doing for me here today. I'm very conscious of the trust and confidence that you're proposing

in me. I'm very impressed what I've learned so far with the quality of the organization, the others members of the IAC. I'm very much looking forward to working with them. So thank you very much.

GOVERNOR SCOTT: Well, thank you very much for your service.

ATTORNEY GENERAL BONDI: And, Governor, if I may? Will is my nominee, of course, and he is so extremely qualified for this position. And he has a family and we know how much time this takes and so thank you for your willingness to serve the state of Florida in this capacity.

MR. HARRELL: Thank you.

ATTORNEY GENERAL BONDI: Thank you so much.

MR. HARRELL: Yeah.

(Applause)

GOVERNOR SCOTT: So is there a motion to approve Item Five?

ATTORNEY GENERAL BONDI: So moved.

CHIEF FINANCIAL OFFICER ATWATER: Is that -- can I use that.

ATTORNEY GENERAL BONDI: So moved.

GOVERNOR SCOTT: Is there a second?

CHIEF FINANCIAL OFFICER ATWATER: Second.

GOVERNOR SCOTT: All right. Moved and seconded. Item Five is approved without objection.

GOVERNOR SCOTT: Congratulations and we look forward to your service. And thank you very much, Ash.

MR. WILLIAMS: Thank you.

MR. HARRELL: Thank you.

((The following excerpt of the meeting commencing at 10:17 a.m. is as follows:)

GOVERNOR SCOTT: I'd like to now recognize Herschel Vinyard with the Board of Trustees. And Herschel is the Secretary of the Department of Environmental Protection and has built a -- he has been doing this job for a little less than a year -- right, about a year, and has done a great job of making sure that, one, the federal government allows us to make our own decisions with regard to our environment --

ATTORNEY GENERAL BONDI: That's right.

GOVERNOR SCOTT: -- and two -- which we clearly all care about -- and, two, making sure there's certainty with regard to our environmental regulation in the state, which has had a positive impact on jobs in our state.

MR. VINYARD: Thank you, Governor, Members of Cabinet. I'm happy not to wear a bow tie today. There are four items on our agenda today for the Board of Trustees. The first one is request approval of the board minutes for November 1, November 15, and December 6.

COMMISSIONER PUTNAM: So moved.

GOVERNOR SCOTT: Is there a second?

End of Section

**STATE BOARD OF ADMINISTRATION**
**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**

---

**TO:** Ash Williams
**FROM:** Robert Copeland
**SUBJECT:** Fiscal Sufficiency
**DATE:** March 7, 2012

---

**APPROVAL OF FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $310,000,000 STATE OF FLORIDA, FULL FAITH AND CREDIT, DEPARTMENT OF TRANSPORTATION RIGHT-OF-WAY ACQUISITION AND BRIDGE CONSTRUCTION REFUNDING BONDS, SERIES (TO BE DETERMINED)**

The Division of Bond Finance of the State Board of Administration (the "Division") has submitted for approval as to fiscal sufficiency a proposal to issue an amount not exceeding $310,000,000 State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Refunding Bonds, Series (to be determined) (the "Bonds"), in one or more series, for the purpose of refunding all or a portion of the outstanding callable Series 2002A and 2003A Bonds and to pay costs associated with the issuance and sale of the Bonds. The Bonds will be issued pursuant to an authorizing resolution adopted by the Governor and Cabinet on February 28, 1989, as amended and supplemented by various resolutions and an authorizing and sale resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012.

The Bonds to be issued pursuant to Section 17 of Article VII of the State Constitution and Chapter 88-247, Laws of Florida, are to be secured by a pledge of and shall be payable primarily from motor fuel and special fuel taxes, except those defined in Section 9(c) of Article XII of the State Constitution, as provided by law (the "Pledged Gas Taxes"), and shall additionally be secured by the full faith and credit of the State. The Division has heretofore issued State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Bonds and Refunding Bonds, Series 2002 through 2011B (the "Outstanding Bonds"). The Bonds will be issued on a parity as to lien and security for payment from the Pledged Gas Taxes with the Outstanding Bonds.

A study of this proposal and the estimates of revenue expected to accrue from the Pledged Gas Taxes, indicate that the proposed Bonds are fiscally sufficient and that the proposal will be executed pursuant to the applicable provisions of law.

**RECOMMENDATION:** It is recommended that the Board approve the fiscal the proposal outlined above.

cc: Janie Knight

**A RESOLUTION OF THE STATE BOARD OF ADMINISTRATION APPROVING THE FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $310,000,000 STATE OF FLORIDA, FULL FAITH AND CREDIT, DEPARTMENT OF TRANSPORTATION RIGHT-OF-WAY ACQUISITION AND BRIDGE CONSTRUCTION REFUNDING BONDS, SERIES (TO BE DETERMINED)**

**WHEREAS,** the Division of Bond Finance of the State Board of Administration (the "Division") proposes to issue an amount not exceeding $310,000,000 State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Refunding Bonds, Series (to be determined) (the "Bonds"), in one or more series, for the purpose of refunding all or a portion of the outstanding callable Series 2002A and 2003A Bonds and to pay costs associated with the issuance and sale of the Bonds; and,

**WHEREAS,** during the 1988 Legislative Session, the Florida Legislature passed and submitted to the electors of the State for approval or rejection at the general election held on November 8, 1988, Senate Joint Resolution 391, which created Section 17 of Article VII of the State Constitution, providing for the issuance of bonds pledging the full faith and credit of the State, without a vote of the electors, to finance or refinance the cost of acquiring real property or the rights to real property for State roads as defined by law, or to finance or refinance the cost of State bridge construction, and purposes incidental to such property acquisition or State bridge construction; and,

**WHEREAS,** the majority of the electors of the State approved the creation of Section 17 of Article VII of the State Constitution at the general election held on November 8, 1988; and,

**WHEREAS,** the Florida Legislature also enacted Chapter 88-247, Laws of Florida, which implements the provisions of Section 17 of Article VII of the State Constitution, providing for the issuance of the Bonds by the Division on behalf of the Department of Transportation; and,

**WHEREAS,** the Bonds to be issued pursuant to Section 17 of Article VII of the State Constitution and Chapter 88-247, Laws of Florida, are to be secured by a pledge of and shall be payable primarily from motor fuel and special fuel taxes, except those defined in Section 9(c) of Article XII of the State Constitution, as provided by law (the "Pledged Gas Taxes"), and shall additionally be secured by the full faith and credit of the State; and,

**WHEREAS,** the Bonds will be issued pursuant to an authorizing resolution adopted by the Governor and Cabinet on February 28, 1989, as amended and supplemented by various resolutions and an authorizing and sale resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012; and,

**WHEREAS,** the Division has heretofore issued State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Bonds and Refunding Bonds, Series 2002 through 2011B (the "Outstanding Bonds"); and,

**WHEREAS,** the State Board of Administration has approved the fiscal sufficiency of an amount not exceeding $310,000,000 Right-of-Way Acquisition and Bridge Construction Refunding Bonds, Series (to be determined) (the "Series 2011 Refunding Bonds") at its November 9, 2010, meeting, of which $51,715,000 remains unissued; and,

**WHEREAS,** the Division of Bond Finance of the State Board of Administration has requested, and it is anticipated that the State Board of Administration will rescind its approval of fiscal sufficiency with respect to the unissued portion of the Series 2011 Refunding Bonds; and,

**WHEREAS,** the Bonds will be issued on a parity as to lien and security for payment from the Pledged Gas Taxes with the Outstanding Bonds; and,

**WHEREAS,** the Pledged Gas Taxes are not pledged, encumbered or committed in any manner, except for the payment of the Outstanding Bonds, and, if and when issued, the proposed Bonds mentioned above; and,

**WHEREAS,** it appears and the Board so finds that this financing will be executed pursuant to the applicable provisions of law, and that the revenue to be used in servicing and liquidating the indebtedness to be created thereby may be reasonably expected to accrue in amounts sufficient to accomplish this purpose; and,

**WHEREAS,** in no State fiscal year will the annual debt service exceed ninety percent (90%) of the Pledged Gas Taxes available for payment of the annual debt service; and,

**WHEREAS,** the Division has furnished sufficient information to enable the State Board of Administration to fulfill its duties pursuant to Section 215.73, Florida Statutes; and,

**WHEREAS,** the State Board of Administration has relied upon information from others but has not independently verified the accuracy or completeness of such information; and,

**WHEREAS,** the State Board of Administration does not approve or disapprove the Bonds as an investment and has not passed upon the accuracy or adequacy of the Official Statement; **Now, Therefore,**

**BE IT RESOLVED,** by the State Board of Administration of Florida, a constitutional body created by Section 4 of Article IV of the Constitution of the State of Florida, as revised in 1968 and subsequently amended, that pursuant to the requirements of Section 215.73, Florida Statutes, the proposal of the Division of Bond Finance of the State Board of Administration of Florida to issue an amount not exceeding $310,000,000 State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Refunding Bonds, Series (to be determined), is hereby approved as to fiscal sufficiency.

**ADOPTED** March 20, 2012

STATE OF FLORIDA

**DIVISION OF BOND FINANCE**
OF THE STATE BOARD OF ADMINISTRATION

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GOVERNOR
AS CHAIRMAN

PAM BONDI
ATTORNEY GENERAL
AS SECRETARY

JEFF ATWATER
CHIEF FINANCIAL OFFICER
AS TREASURER

ADAM H. PUTNAM
COMMISSIONER OF AGRICULTURE

March 2, 2012

Mr. Ashbel C. Williams
Executive Director
State Board of Administration
Post Office Box 13300
Tallahassee, Florida 32317-3300

RE: Not Exceeding $310,000,000 State of Florida, Full Faith and Credit, Department of Transportation Right-of-Way Acquisition and Bridge Construction Refunding Bonds, Series (to be determined)

Dear Mr. Williams:

In compliance with Section 215.73, Florida Statutes, the Division of Bond Finance requests State Board of Administration approval as to fiscal sufficiency for the above referenced bond issue. We request such approval at your board meeting of March 20, 2012.

These bonds will be payable from pledged gas taxes, consisting of certain motor fuel and diesel fuel taxes, and are additionally secured by the full faith and credit of the State of Florida. The bonds will be issued on a parity with the previously issued State of Florida Department of Transportation Right-of-Way Acquisition and Bridge Construction Bonds. The fiscal sufficiency for the remaining $51,715,000 Series (to be determined) refunding bonds approved for fiscal sufficiency on November 9, 2010 should be rescinded

The proposed bonds are being issued to refund all or a portion of the outstanding Series 2002A and Series 2003A Right-of-Way Acquisition and Bridge Construction Bonds and to pay costs associated with the issuance and sale of the proposed bonds. The bonds will only be issued if there is a savings.

The following documents are enclosed for your consideration:

Enclosure 1: A coverage table based on the estimated pledged revenues available for debt service without considering the potential savings from the proposed $310,000,000 refunding bonds;

Enclosure 2: Estimated debt service and savings schedule for the proposed bonds; and

Enclosure 3: A schedule showing the estimated Highway Fuel Sales Tax collections (the motor and diesel fuel taxes pledged) as projected by the Florida Consensus Estimating Conference at its January 2012 meeting.

The bonds will be issued in one or more series and are being issued pursuant to an authorizing resolution adopted by the Governor and Cabinet on February 28, 1989, as amended and supplemented by various resolutions and an authorizing and sale resolution which is anticipated to be adopted on March 20, 2012. Copies of the February 28, 1989 authorizing resolution and its subsequent supplemental resolutions have previously been provided to you, and a draft of the sale resolution will be provided as soon as it is available.

A draft of the fiscal sufficiency resolution should be sent to Ray Petty and Charlie Yadon of this office for review. Should you have any questions, please contact either myself or Charlie Yadon at 488-4782. Your consideration in this matter is appreciated.

Very truly yours,

J. Ben Watkins III
Director

JBW\cy

Enclosures

cc: Robert Copeland
Janie Knight
Anthony Doheny

**Enclosure 1**

# STATE OF FLORIDA FULL FAITH AND CREDIT
# RIGHT-OF-WAY ACQUISITION AND BRIDGE CONSTRUCTION BONDS
# ESTIMATED SCHEDULE OF COVERAGE ON OUTSTANDING BONDS

| Fiscal Year Ended June 30 | Projected Motor & Diesel Fuel Sales Tax Available for Debt Service (1) | Outstanding Debt Service | Debt Service Coverage (2) | Maximum Allowable Debt Service (3) | Pro Forma Debt Service Coverage (4) |
|---|---|---|---|---|---|
| 2012 | $1,094,200,000 | $143,624,226 | 7.62x | $188,762,000 | 5.80x |
| 2013 | 1,139,300,000 | 146,313,040 | 7.79x | 194,593,000 | 5.85x |
| 2014 | 1,184,600,000 | 146,288,228 | 8.10x | 209,923,000 | 5.64x |
| 2015 | 1,239,500,000 | 146,349,246 | 8.47x | 219,163,000 | 5.66x |
| 2016 | 1,301,300,000 | 146,344,290 | 8.89x | 229,901,000 | 5.66x |
| 2017 | 1,358,900,000 | 146,393,040 | 9.28x | 240,289,000 | 5.66x |
| 2018 | 1,411,700,000 | 146,448,565 | 9.64x | 249,620,000 | 5.66x |
| 2019 | 1,468,300,000 | 146,372,003 | 10.03x | 259,238,000 | 5.66x |
| 2020 | 1,521,600,000 | 146,468,271 | 10.39x | 268,359,000 | 5.67x |
| 2021 | 1,579,400,000 | 146,472,540 | 10.78x | 275,000,000 | 5.74x |
| 2022 | 1,579,400,000 | 143,132,753 | 11.03x | 275,000,000 | 5.74x |
| 2023 | 1,579,400,000 | 142,219,248 | 11.11x | 275,000,000 | 5.74x |
| 2024 | 1,579,400,000 | 138,591,070 | 11.40x | 275,000,000 | 5.74x |
| 2025 | 1,579,400,000 | 128,195,683 | 12.32x | 275,000,000 | 5.74x |
| 2026 | 1,579,400,000 | 128,234,350 | 12.32x | 275,000,000 | 5.74x |
| 2027 | 1,579,400,000 | 118,590,906 | 13.32x | 275,000,000 | 5.74x |
| 2028 | 1,579,400,000 | 96,742,194 | 16.33x | 275,000,000 | 5.74x |
| 2029 | 1,579,400,000 | 88,218,125 | 17.90x | 275,000,000 | 5.74x |
| 2030 | 1,579,400,000 | 88,187,463 | 17.91x | 275,000,000 | 5.74x |
| 2031 | 1,579,400,000 | 88,141,350 | 17.92x | 275,000,000 | 5.74x |
| 2032 | 1,579,400,000 | 79,657,563 | 19.83x | 275,000,000 | 5.74x |
| 2033 | 1,579,400,000 | 68,037,275 | 23.21x | 275,000,000 | 5.74x |
| 2034 | 1,579,400,000 | 48,558,650 | 32.53x | 275,000,000 | 5.74x |
| 2035 | 1,579,400,000 | 28,931,988 | 54.59x | 275,000,000 | 5.74x |
| 2036 | 1,579,400,000 | 28,886,350 | 54.68x | 275,000,000 | 5.74x |
| 2037 | 1,579,400,000 | 28,846,688 | 54.75x | 275,000,000 | 5.74x |
| 2038 | 1,579,400,000 | 18,895,100 | 83.59x | 275,000,000 | 5.74x |
| 2039 | 1,579,400,000 | 18,894,100 | 83.59x | 275,000,000 | 5.74x |
| 2040 | 1,579,400,000 | 5,905,600 | 267.44x | 275,000,000 | 5.74x |
| 2041 | 1,579,400,000 | 5,907,200 | 267.37x | 275,000,000 | 5.74x |
| | | $ 2,953,847,101 | | $7,834,848,000 | |

(1) The bonds are payable from the motor fuel and diesel fuel taxes pursuant to Sections 206.41(g) and 206.87(1)(e), Florida Statutes. The projected motor and diesel fuel tax collections are as adopted by the Florida Consensus Estimating Conference on Transportation Revenues, October 2011, and are rounded to the nearest thousand dollars. The projections are held constant in Fiscal Year 2020-2021 for future years. **The projections are based on the best information available when the estimates are made, which is believed to be accurate. Projections are statements of opinion and are subject to future events which may cause the actual results to differ materially from those set forth herein. Undue reliance should not be placed on these projections.**

(2) Coverage has been calculated by dividing the amount of Projected Motor and Diesel Fuel Sales Tax Available for Debt Service by the Outstanding Total Debt Service

(3) Pursuant to Section 206.46(2), Florida Statutes, debt service cannot exceed the lesser of 7% of state revenues transferred to the STTF or $275 million.

(4) Coverage has been calculated by dividing the amount of Projected Motor and Diesel Fuel Sales Tax Available for Debt Service by the Maximum Allowable Debt Service.

End of Section

**STATE BOARD OF ADMINISTRATION**
**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**

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**TO:** Ash Williams
**FROM:** Robert Copeland
**SUBJECT:** Fiscal Sufficiency
**DATE:** March 7, 2012

---

**APPROVAL OF FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $47,500,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE BONDS, SERIES 2012A:**

The Division of Bond Finance of the State Board of Administration (the "Division") has submitted for approval as to fiscal sufficiency a proposal to issue an amount not exceeding $47,500,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Bonds, Series 2012A (the "Bonds"), to finance the construction of a student housing facility on the main campus of Florida International University; fund a debt service reserve, if necessary; fund capitalized interest, if any; and pay costs associated with the issuance and sale of the Bonds.

The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, by a resolution adopted September 23, 1998, and as amended by the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively, and the Fifth Supplemental Resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012 (collectively referred to herein as the "Resolution"). The Division has heretofore issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A (collectively, the "Outstanding Bonds"). The Division has submitted for approval as to fiscal sufficiency a proposal to issue not exceeding $7,000,000 Florida International University Dormitory Revenue Refunding Bonds, Series (the "2012 Refunding Bonds") for approval at the March 20, 2012, meeting of the State Board of Administration. The Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues as defined in the Resolution, with the Outstanding Bonds, and the 2012 Refunding Bonds when and if approved and issued.

A study of this proposal and the estimates of revenue expected to accrue indicate that the proposed Bonds are fiscally sufficient and that the proposal will be executed pursuant to the applicable provisions of law.

**RECOMMENDATION:** It is recommended that the Board approve the proposal outlined above.

cc: Janie Knight

**A RESOLUTION OF THE STATE BOARD OF ADMINISTRATION APPROVING THE FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $47,500,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE BONDS, SERIES 2012A**

**WHEREAS,** the Division of Bond Finance of the State Board of Administration (the "Division") proposes to issue an amount not exceeding $47,500,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Bonds, Series 2012A (the "Bonds"), to finance the construction of a student housing facility on the main campus of Florida International University; fund a debt service reserve, if necessary; fund capitalized interest, if any; and pay costs associated with the issuance and sale of the Bonds; and,

**WHEREAS,** the Division has requested the State Board of Administration to approve the fiscal sufficiency of the proposed issue as required by Section 215.73, Florida Statutes; and,

**WHEREAS,** The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, as amended by a resolution adopted September 23, 1998, and by a resolution adopted September 23, 1998, and by the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively, and the Fifth Supplemental Resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012 (collectively referred to herein as the "Resolution"); and,

**WHEREAS,** the Division has heretofore issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A (collectively, the "Outstanding Bonds"); and,

**WHEREAS,** the Division has submitted for approval as to fiscal sufficiency a proposal to issue not exceeding $7,000,000 Florida International University Dormitory Revenue Refunding Bonds, Series (to be determined) (the "2012 Refunding Bonds") for approval at the March 20, 2012, meeting of the State Board of Administration; and,

**WHEREAS,** the Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues as described in the Resolution, and in all other respects, with the Outstanding Bonds, and the 2012 Refunding Bonds when and if approved and issued; and,

**WHEREAS,** the principal of and interest due on the Bonds shall be paid solely out of revenues and other amounts pledged therefor, as described in the Resolution; and,

**WHEREAS,** the Bonds do not constitute an obligation, either general or special, of the State of Florida or any of its units of local government and shall not be a debt of the State or of any unit of local government, and neither the State nor any unit of local government shall be liable thereon; and,

**WHEREAS,** Florida International University shall not have the power to pledge the credit, the revenues, or the taxing power of the State or of any unit of local government, and neither the credit, the revenues, nor the taxing power of the State or of any unit of local government shall be deemed to be pledged to the payment of the Bonds; and,

**WHEREAS,** the proceeds of the Bonds shall be and constitute trust funds and shall be used and applied solely in the manner and for the purposes provided in the Resolution; and,

**WHEREAS,** the estimate of funds pledged to the issue indicates that in no State fiscal year will the debt service requirements of the Bonds and all other issues secured by the same pledged revenues exceed the Pledged Revenues available for payment of such debt service requirements and that in no State fiscal year will the moneys pledged for the debt service requirements be less than the required coverage amount; and,

**WHEREAS,** the Division, has furnished sufficient information to enable the State Board of Administration to fulfill its duties pursuant to Section 215.73, Florida Statutes; and,

**WHEREAS,** the State Board of Administration has relied upon information from others but has not independently verified the accuracy or completeness of such information; and,

**WHEREAS,** the State Board of Administration does not approve or disapprove the Bonds as an investment and has not passed upon the accuracy or adequacy of the Official Statement; **Now, Therefore,**

**BE IT RESOLVED,** by the State Board of Administration of Florida, a constitutional body created by Section 4 of Article IV of the Constitution of the State of Florida, as revised in 1968 and subsequently amended, that pursuant to the requirements of Section 215.73, Florida Statutes, the proposal of the Division of Bond Finance of the State Board of Administration to issue an amount not exceeding $47,500,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Bonds, Series 2012A for the uses and purposes hereinabove set forth, is hereby approved as to fiscal sufficiency.

**ADOPTED** March 20, 2012

STATE OF FLORIDA

**DIVISION OF BOND FINANCE**
OF THE STATE BOARD OF ADMINISTRATION

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GOVERNOR
AS CHAIRMAN

PAM BONDI
ATTORNEY GENERAL

JEFF ATWATER
CHIEF FINANCIAL OFFICER

ADAM H. PUTNAM
COMMISSIONER OF AGRICULTURE

March 2, 2012

Mr. Ashbel C. Williams
Executive Director & CIO
State Board of Administration
Post Office Box 13300
Tallahassee, Florida 32317-3300

RE: Not Exceeding $47,500,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Bonds, Series 2012A

Dear Mr. Williams:

In compliance with Section 215.73, Florida Statutes, the Division of Bond Finance requests State Board of Administration approval as to fiscal sufficiency for the above referenced bond issue. We request such approval at your board meeting of March 20, 2012.

The proposed bonds will be secured by the revenues of the housing system after deducting operating expenses. Housing system revenues are derived primarily from student housing rental income. The proposed bonds will be payable on a parity with the previously issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A remaining outstanding after issuance of the proposed $7,000,000 refunding bonds expected to be approved for fiscal sufficiency on March 20, 2012.

The bonds are being issued to finance the construction of a 620-bed student housing facility on the main campus of the University; fund a debt service reserve, if necessary; fund capitalized interest, if any; and pay the costs associated with the sale of the proposed bonds.

Enclosed for your review are the following:

Enclosure 1: an estimated coverage table for the program including the proposed $47,500,000 dormitory revenue bonds, without considering the potential savings from the proposed $7,000,000 refunding bonds; and

Enclosure 2: an estimated debt service schedule from a recent sizing of the proposed bonds.

The bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, as amended by a resolution adopted September 23, 1998, and the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively. On March 20, 2012, the Governing Board of the Division of Bond Finance is expected to adopt the Fifth Supplemental Resolution authorizing the issuance and sale of the $47,500,000 dormitory revenue bonds. Also on March 20, 2012, the Governing Board of the Division of Bond Finance is expected to adopt the Sixth Supplemental Resolution, which will authorize the issuance of the $7,000,000 refunding bonds. The Original Resolution and the Second and Fourth Supplemental Resolutions were previously provided; the Fifth and Sixth Supplemental Resolutions will be provided as soon as they are available.

A draft of the fiscal sufficiency resolution should be sent to Donna Biggins and Nora Wittstruck of this office for review. Should you have any questions, please contact either myself, Donna Biggins or Nora Wittstruck at 488-4782. Your consideration of this matter is appreciated.

Sincerely,

J. Ben Watkins III
Director

JBW:nw

Enclosures

cc: Anthoney Doheny
Robert Copeland

# STATE OF FLORIDA, BOARD OF GOVERNORS
# FLORIDA INTERNATIONAL UNIVERSITY
# DORMITORY REVENUE BONDS, SERIES 2012A
# FISCAL SUFFICIENCY REQUEST FOR NOT EXCEEDING $47,500,000

## ESTIMATED DEBT SERVICE COVERAGE

| Fiscal Year Ended June 30 | Gross Revenues | O & M Expenses | Pledged Revenue | Outstanding Debt Service | Estimated Debt Service: Principal | Estimated Debt Service: Interest | Estimated Debt Service: Capitalized Interest | Estimated Debt Service: Total | Total Debt Service | Coverage |
|---|---|---|---|---|---|---|---|---|---|---|
| | (1) | (1) | | | | (2) | (3) | | | (4) |
| **Historical** | | | | | | | | | | |
| 2007 | $19,892,301 | $10,190,840 | $ 9,701,461 | $ 7,124,989 | | | | | $ 7,124,989 | 1.36x |
| 2008 | 21,396,866 | 10,565,212 | 10,831,654 | 7,131,329 | | | | | 7,131,329 | 1.52x |
| 2009 | 22,940,987 | 12,243,140 | 10,697,847 | 7,129,249 | | | | | 7,129,249 | 1.50x |
| 2010 | 23,204,205 | 12,418,545 | 10,785,660 | 7,124,129 | | | | | 7,124,129 | 1.51x |
| 2011 | 26,003,389 | 13,951,606 | 12,051,783 | 7,129,454 | | | | | 7,129,454 | 1.69x |
| **Projected** | | | | | | | | | | |
| 2012 | $25,161,878 | $14,975,162 | $10,186,716 | $ 6,961,829 | $ - | $ - | $ - | $ - | $ 6,961,829 | 1.46x |
| 2013 | 24,705,258 | 14,847,834 | 9,857,424 | 6,846,569 | - | 3,307,847 | 3,307,847 | - | 6,846,569 | 1.44x |
| 2014 | 30,230,729 | 16,735,035 | 13,495,694 | 6,846,219 | 720,000 | 2,731,250 | - | 3,451,250 | 10,297,469 | 1.31x |
| 2015 | 30,955,627 | 17,204,901 | 13,750,726 | 6,853,269 | 765,000 | 2,689,850 | - | 3,454,850 | 10,308,119 | 1.33x |
| 2016 | 31,841,419 | 17,412,012 | 14,429,407 | 6,846,869 | 805,000 | 2,645,863 | - | 3,450,863 | 10,297,732 | 1.40x |
| 2017 | 32,815,584 | 17,760,252 | 15,055,331 | 4,776,269 | 855,000 | 2,599,575 | - | 3,454,575 | 8,230,844 | 1.83x |
| 2018 | 32,815,584 | 17,760,252 | 15,055,331 | 4,773,319 | 905,000 | 2,550,413 | - | 3,455,413 | 8,228,732 | 1.83x |
| 2019 | 32,815,584 | 17,760,252 | 15,055,331 | 4,774,819 | 955,000 | 2,498,375 | - | 3,453,375 | 8,228,194 | 1.83x |
| 2020 | 32,815,584 | 17,760,252 | 15,055,331 | 4,770,219 | 1,010,000 | 2,443,463 | - | 3,453,463 | 8,223,682 | 1.83x |
| 2021 | 32,815,584 | 17,760,252 | 15,055,331 | 4,774,569 | 1,065,000 | 2,385,388 | - | 3,450,388 | 8,224,957 | 1.83x |
| 2022 | 32,815,584 | 17,760,252 | 15,055,331 | 4,773,744 | 1,130,000 | 2,324,150 | - | 3,454,150 | 8,227,894 | 1.83x |
| 2023 | 32,815,584 | 17,760,252 | 15,055,331 | 4,768,994 | 1,195,000 | 2,259,175 | - | 3,454,175 | 8,223,169 | 1.83x |
| 2024 | 32,815,584 | 17,760,252 | 15,055,331 | 4,771,056 | 1,260,000 | 2,190,463 | - | 3,450,463 | 8,221,519 | 1.83x |
| 2025 | 32,815,584 | 17,760,252 | 15,055,331 | 4,923,050 | 1,335,000 | 2,118,013 | - | 3,453,013 | 8,376,063 | 1.80x |
| 2026 | 32,815,584 | 17,760,252 | 15,055,331 | 3,955,500 | 1,410,000 | 2,041,250 | - | 3,451,250 | 7,406,750 | 2.03x |
| 2027 | 32,815,584 | 17,760,252 | 15,055,331 | 3,949,825 | 1,495,000 | 1,960,175 | - | 3,455,175 | 7,405,000 | 2.03x |
| 2028 | 32,815,584 | 17,760,252 | 15,055,331 | 3,953,300 | 1,580,000 | 1,874,213 | - | 3,454,213 | 7,407,513 | 2.03x |
| 2029 | 32,815,584 | 17,760,252 | 15,055,331 | 2,220,250 | 1,670,000 | 1,783,363 | - | 3,453,363 | 5,673,613 | 2.65x |
| 2030 | 32,815,584 | 17,760,252 | 15,055,331 | 2,218,525 | 1,765,000 | 1,687,338 | - | 3,452,338 | 5,670,863 | 2.65x |
| 2031 | 32,815,584 | 17,760,252 | 15,055,331 | 2,218,425 | 1,865,000 | 1,585,850 | - | 3,450,850 | 5,669,275 | 2.66x |
| 2032 | 32,815,584 | 17,760,252 | 15,055,331 | 2,219,725 | 1,975,000 | 1,478,613 | - | 3,453,613 | 5,673,338 | 2.65x |
| 2033 | 32,815,584 | 17,760,252 | 15,055,331 | 2,222,200 | 2,090,000 | 1,365,050 | - | 3,455,050 | 5,677,250 | 2.65x |
| 2034 | 32,815,584 | 17,760,252 | 15,055,331 | 2,220,625 | 2,205,000 | 1,244,875 | - | 3,449,875 | 5,670,500 | 2.66x |
| 2035 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,335,000 | 1,118,088 | - | 3,453,088 | 3,453,088 | 4.36x |
| 2036 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,470,000 | 983,825 | - | 3,453,825 | 3,453,825 | 4.36x |
| 2037 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,610,000 | 841,800 | - | 3,451,800 | 3,451,800 | 4.36x |
| 2038 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,760,000 | 691,725 | - | 3,451,725 | 3,451,725 | 4.36x |
| 2039 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,920,000 | 533,025 | - | 3,453,025 | 3,453,025 | 4.36x |
| 2040 | 32,815,584 | 17,760,252 | 15,055,331 | - | 3,085,000 | 365,125 | - | 3,450,125 | 3,450,125 | 4.36x |
| 2041 | 32,815,584 | 17,760,252 | 15,055,331 | - | 3,265,000 | 187,738 | - | 3,452,738 | 3,452,738 | 4.36x |
| | | | | $ 102,639,169 | $ 47,500,000 | $ 52,485,872 | $ 3,307,847 | $ 96,678,025 | $ 199,317,194 | |

(1) Actual revenue and expense information was provided by Florida International University and has not been audited. Projected revenues and expenses for Fiscal Years 2011-12 through 2016-17, assuming annual rate increases of 3% and operating expenditures increasing at 2% annually, were provided by the University. Projections for Fiscal Year 2016-17 and thereafter are held constant; however, no representation is made that the amounts shown in any fiscal year will be collected. The new facility being constructed is scheduled to open fall 2013 (Fiscal Year 2013-14).

(2) Debt service on the proposed bonds has been calculated at 5.75%.

(3) Assumes capitalized interest through July 1, 2013, which is included in bond proceeds.

(4) Coverage of Pledged Revenues is determined by dividing Pledged Revenues by Total Outstanding Debt Service.

**STATE BOARD OF ADMINISTRATION**
**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**

---

**TO:** Ash Williams
**FROM:** Robert Copeland
**SUBJECT:** Fiscal Sufficiency
**DATE:** March 7, 2012

---

**APPROVAL OF FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $7,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE REFUNDING BONDS, SERIES (TO BE DETERMINED):**

The Division of Bond Finance of the State Board of Administration (the "Division") has submitted for approval as to fiscal sufficiency a proposal to issue an amount not exceeding $7,000,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Refunding Bonds, Series (to be determined) (the "Bonds"), for the purpose of refunding all or a portion of the outstanding Series 1998 Bonds and to pay costs associated with the issuance and sale of the Bonds.

The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, as amended by a resolution adopted September 23, 1998, and by the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively, and the Sixth Supplemental Resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012 (collectively referred to herein as the "Resolution"). The Division has heretofore issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A (collectively, the "Outstanding Bonds"). The Division has submitted for approval as to fiscal sufficiency a proposal to issue not exceeding $47,500,000 Florida International University Dormitory Revenue Bonds, Series 2012A (the "2012A Bonds") for approval at the March 20, 2012, meeting of the State Board of Administration. The Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues as defined in the Resolution, with the Outstanding Bonds, and the 2012A Bonds when and if approved and issued.

A study of this proposal and the estimates of revenue expected to accrue indicate that the proposed Bonds are fiscally sufficient and that the proposal will be executed pursuant to the applicable provisions of law.

**RECOMMENDATION:** It is recommended that the Board approve the proposal outlined above.

cc: Janie Knight

**A RESOLUTION OF THE STATE BOARD OF ADMINISTRATION APPROVING THE FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $7,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, FLORIDA INTERNATIONAL UNIVERSITY DORMITORY REVENUE REFUNDING BONDS, SERIES (TO BE DETERMINED)**

**WHEREAS,** the Division of Bond Finance of the State Board of Administration (the "Division") proposes to issue an amount not exceeding $7,000,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Refunding Bonds, Series (to be determined) (the "Bonds"), for the purpose of refunding all or a portion of the outstanding Series 1998 Bonds and to pay costs associated with the issuance and sale of the Bonds; and,

**WHEREAS,** the Division has requested the State Board of Administration to approve the fiscal sufficiency of the proposed issue as required by Section 215.73, Florida Statutes; and,

**WHEREAS,** The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, as amended by a resolution adopted September 23, 1998, and by the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively, and the Sixth Supplemental Resolution which is anticipated to be adopted by the Governor and Cabinet on March 20, 2012 (collectively referred to herein as the "Resolution"); and,

**WHEREAS,** the Division has heretofore issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A (collectively, the "Outstanding Bonds"); and,

**WHEREAS,** the Division has submitted for approval as to fiscal sufficiency a proposal to issue not exceeding $47,500,000 Florida International University Dormitory Revenue Bonds, Series 2012A (the "2012A Bonds") for approval at the March 20, 2012, meeting of the State Board of Administration; and,

**WHEREAS,** the Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues as described in the Resolution, and in all other respects, with the Outstanding Bonds, and the 2012A Bonds when and if approved and issued; and,

**WHEREAS,** the principal of and interest due on the Bonds shall be paid solely out of revenues and other amounts pledged therefor, as described in the Resolution; and,

**WHEREAS,** the Bonds do not constitute an obligation, either general or special, of the State of Florida or any of its units of local government and shall not be a debt of the State or of any unit of local government, and neither the State nor any unit of local government shall be liable thereon; and,

**WHEREAS,** Florida International University shall not have the power to pledge the credit, the revenues, or the taxing power of the State or of any unit of local government, and neither the credit, the revenues, nor the taxing power of the State or of any unit of local government shall be deemed to be pledged to the payment of the Bonds; and,

**WHEREAS,** the proceeds of the Bonds shall be and constitute trust funds and shall be used and applied solely in the manner and for the purposes provided in the Resolution; and,

**WHEREAS,** the estimate of funds pledged to the issue indicates that in no State fiscal year will the debt service requirements of the Bonds and all other issues secured by the same pledged revenues exceed the Pledged Revenues available for payment of such debt service requirements and that in no State fiscal year will the moneys pledged for the debt service requirements be less than the required coverage amount; and,

**WHEREAS,** the Division, has furnished sufficient information to enable the State Board of Administration to fulfill its duties pursuant to Section 215.73, Florida Statutes; and,

**WHEREAS,** the State Board of Administration has relied upon information from others but has not independently verified the accuracy or completeness of such information; and,

**WHEREAS,** the State Board of Administration does not approve or disapprove the Bonds as an investment and has not passed upon the accuracy or adequacy of the Official Statement; **Now, Therefore,**

**BE IT RESOLVED,** by the State Board of Administration of Florida, a constitutional body created by Section 4 of Article IV of the Constitution of the State of Florida, as revised in 1968 and subsequently amended, that pursuant to the requirements of Section 215.73, Florida Statutes, the proposal of the Division of Bond Finance of the State Board of Administration to issue an amount not exceeding $7,000,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Refunding Bonds, Series (to be determined) for the uses and purposes hereinabove set forth, is hereby approved as to fiscal sufficiency.

**ADOPTED** March 20, 2012

STATE OF FLORIDA

**DIVISION OF BOND FINANCE**
OF THE STATE BOARD OF ADMINISTRATION

HERMITAGE CENTRE, SUITE 200
1801 HERMITAGE BOULEVARD
TALLAHASSEE, FLORIDA 32308

POST OFFICE BOX 13300
TALLAHASSEE, FLORIDA 32317-3300
(Address mail to P.O. Box; deliveries to street address)

TELEPHONE: (850) 488-4782
TELECOPIER: (850) 413-1315

J. BEN WATKINS III
DIRECTOR

RICK SCOTT
GOVERNOR
AS CHAIRMAN

PAM BONDI
ATTORNEY GENERAL

JEFF ATWATER
CHIEF FINANCIAL OFFICER

ADAM H. PUTNAM
COMMISSIONER OF AGRICULTURE

March 2, 2012

Mr. Ashbel C. Williams
Executive Director & CIO
State Board of Administration
Post Office Box 13300
Tallahassee, Florida 32317-3300

RE: Not Exceeding $7,000,000 State of Florida, Board of Governors, Florida International University Dormitory Revenue Refunding Bonds, Series (to be determined)

Dear Mr. Williams:

In compliance with Section 215.73, Florida Statutes, the Division of Bond Finance requests State Board of Administration approval as to fiscal sufficiency for the above referenced bond issue. We request such approval at your board meeting of March 20, 2012.

The proposed bonds will be secured by the revenues of the housing system after deducting operating expenses. Housing system revenues are derived primarily from student housing rental income. The proposed bonds will be payable on a parity with the previously issued Florida International University Dormitory Revenue Bonds, Series 1998 through 2011A remaining outstanding after issuance of the proposed refunding bonds and including the $47,500,000 dormitory revenue bonds expected to be approved for fiscal sufficiency on March 20, 2012.

The bonds are being issued to refund all or a portion of the outstanding Series 1998 Bonds and to pay costs associated with the issuance and sale of the proposed bonds. The bonds will only be issued if there is a savings derived from the transaction.

Enclosed for your review are the following:

Enclosure 1: an estimated coverage table for the program including the proposed $47,500,000 dormitory revenue bonds, without considering the potential savings from the proposed $7,000,000 refunding bonds; and

Enclosure 2: an estimated debt service and savings schedule from a recent sizing of the proposed bonds.

The bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on June 9, 1998, as amended by a resolution adopted September 23, 1998, and the Second and Fourth Supplemental Resolutions adopted on August 10, 2004 and September 20, 2011, respectively. On March 20, 2012, the Governing Board of the Division of Bond Finance is expected to adopt the Sixth Supplemental Resolution, which will authorize the issuance and sale of the $7,000,000 refunding bonds. Also on March 20, 2012, the Governing Board of the Division of Bond Finance is expected to adopt the Fifth Supplemental Resolution authorizing the issuance of the $47,500,000 dormitory revenue bonds. The Original Resolution and the Second and Fourth Supplemental Resolutions were previously provided; the Fifth and Sixth Supplemental Resolutions will be provided as soon as they are available.

A draft of the fiscal sufficiency resolution should be sent to Donna Biggins and Nora Wittstruck of this office for review. Should you have any questions, please contact either myself, Donna Biggins or Nora Wittstruck at 488-4782. Your consideration of this matter is appreciated.

Sincerely,

J. Ben Watkins III
Director

JBW:nw

Enclosures

cc: Anthoney Doheny
Robert Copeland

# STATE OF FLORIDA, BOARD OF GOVERNORS
# FLORIDA INTERNATIONAL UNIVERSITY
# DORMITORY REVENUE BONDS, SERIES 2012A
# FISCAL SUFFICIENCY REQUEST FOR NOT EXCEEDING $47,500,000

## ESTIMATED DEBT SERVICE COVERAGE

| Fiscal Year Ended June 30 | Gross Revenues | O & M Expenses | Pledged Revenue | Outstanding Debt Service | Estimated Debt Service: Principal | Estimated Debt Service: Interest | Estimated Debt Service: Capitalized Interest | Estimated Debt Service: Total | Total Debt Service | Coverage |
|---|---|---|---|---|---|---|---|---|---|---|
| | (1) | (1) | | | | (2) | (3) | | | (4) |
| **Historical** | | | | | | | | | | |
| 2007 | $19,892,301 | $10,190,840 | $ 9,701,461 | $ 7,124,989 | | | | | $ 7,124,989 | 1.36x |
| 2008 | 21,396,866 | 10,565,212 | 10,831,654 | 7,131,329 | | | | | 7,131,329 | 1.52x |
| 2009 | 22,940,987 | 12,243,140 | 10,697,847 | 7,129,249 | | | | | 7,129,249 | 1.50x |
| 2010 | 23,204,205 | 12,418,545 | 10,785,660 | 7,124,129 | | | | | 7,124,129 | 1.51x |
| 2011 | 26,003,389 | 13,951,606 | 12,051,783 | 7,129,454 | | | | | 7,129,454 | 1.69x |
| **Projected** | | | | | | | | | | |
| 2012 | $25,161,878 | $14,975,162 | $10,186,716 | $ 6,961,829 | $ - | $ - | $ - | $ - | $ 6,961,829 | 1.46x |
| 2013 | 24,705,258 | 14,847,834 | 9,857,424 | 6,846,569 | - | 3,307,847 | 3,307,847 | - | 6,846,569 | 1.44x |
| 2014 | 30,230,729 | 16,735,035 | 13,495,694 | 6,846,219 | 720,000 | 2,731,250 | - | 3,451,250 | 10,297,469 | 1.31x |
| 2015 | 30,955,627 | 17,204,901 | 13,750,726 | 6,853,269 | 765,000 | 2,689,850 | - | 3,454,850 | 10,308,119 | 1.33x |
| 2016 | 31,841,419 | 17,412,012 | 14,429,407 | 6,846,869 | 805,000 | 2,645,863 | - | 3,450,863 | 10,297,732 | 1.40x |
| 2017 | 32,815,584 | 17,760,252 | 15,055,331 | 4,776,269 | 855,000 | 2,599,575 | - | 3,454,575 | 8,230,844 | 1.83x |
| 2018 | 32,815,584 | 17,760,252 | 15,055,331 | 4,773,319 | 905,000 | 2,550,413 | - | 3,455,413 | 8,228,732 | 1.83x |
| 2019 | 32,815,584 | 17,760,252 | 15,055,331 | 4,774,819 | 955,000 | 2,498,375 | - | 3,453,375 | 8,228,194 | 1.83x |
| 2020 | 32,815,584 | 17,760,252 | 15,055,331 | 4,770,219 | 1,010,000 | 2,443,463 | - | 3,453,463 | 8,223,682 | 1.83x |
| 2021 | 32,815,584 | 17,760,252 | 15,055,331 | 4,774,569 | 1,065,000 | 2,385,388 | - | 3,450,388 | 8,224,957 | 1.83x |
| 2022 | 32,815,584 | 17,760,252 | 15,055,331 | 4,773,744 | 1,130,000 | 2,324,150 | - | 3,454,150 | 8,227,894 | 1.83x |
| 2023 | 32,815,584 | 17,760,252 | 15,055,331 | 4,768,994 | 1,195,000 | 2,259,175 | - | 3,454,175 | 8,223,169 | 1.83x |
| 2024 | 32,815,584 | 17,760,252 | 15,055,331 | 4,771,056 | 1,260,000 | 2,190,463 | - | 3,450,463 | 8,221,519 | 1.83x |
| 2025 | 32,815,584 | 17,760,252 | 15,055,331 | 4,923,050 | 1,335,000 | 2,118,013 | - | 3,453,013 | 8,376,063 | 1.80x |
| 2026 | 32,815,584 | 17,760,252 | 15,055,331 | 3,955,500 | 1,410,000 | 2,041,250 | - | 3,451,250 | 7,406,750 | 2.03x |
| 2027 | 32,815,584 | 17,760,252 | 15,055,331 | 3,949,825 | 1,495,000 | 1,960,175 | - | 3,455,175 | 7,405,000 | 2.03x |
| 2028 | 32,815,584 | 17,760,252 | 15,055,331 | 3,953,300 | 1,580,000 | 1,874,213 | - | 3,454,213 | 7,407,513 | 2.03x |
| 2029 | 32,815,584 | 17,760,252 | 15,055,331 | 2,220,250 | 1,670,000 | 1,783,363 | - | 3,453,363 | 5,673,613 | 2.65x |
| 2030 | 32,815,584 | 17,760,252 | 15,055,331 | 2,218,525 | 1,765,000 | 1,687,338 | - | 3,452,338 | 5,670,863 | 2.65x |
| 2031 | 32,815,584 | 17,760,252 | 15,055,331 | 2,218,425 | 1,865,000 | 1,585,850 | - | 3,450,850 | 5,669,275 | 2.66x |
| 2032 | 32,815,584 | 17,760,252 | 15,055,331 | 2,219,725 | 1,975,000 | 1,478,613 | - | 3,453,613 | 5,673,338 | 2.65x |
| 2033 | 32,815,584 | 17,760,252 | 15,055,331 | 2,222,200 | 2,090,000 | 1,365,050 | - | 3,455,050 | 5,677,250 | 2.65x |
| 2034 | 32,815,584 | 17,760,252 | 15,055,331 | 2,220,625 | 2,205,000 | 1,244,875 | - | 3,449,875 | 5,670,500 | 2.66x |
| 2035 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,335,000 | 1,118,088 | - | 3,453,088 | 3,453,088 | 4.36x |
| 2036 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,470,000 | 983,825 | - | 3,453,825 | 3,453,825 | 4.36x |
| 2037 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,610,000 | 841,800 | - | 3,451,800 | 3,451,800 | 4.36x |
| 2038 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,760,000 | 691,725 | - | 3,451,725 | 3,451,725 | 4.36x |
| 2039 | 32,815,584 | 17,760,252 | 15,055,331 | - | 2,920,000 | 533,025 | - | 3,453,025 | 3,453,025 | 4.36x |
| 2040 | 32,815,584 | 17,760,252 | 15,055,331 | - | 3,085,000 | 365,125 | - | 3,450,125 | 3,450,125 | 4.36x |
| 2041 | 32,815,584 | 17,760,252 | 15,055,331 | - | 3,265,000 | 187,738 | - | 3,452,738 | 3,452,738 | 4.36x |
| | | | | $ 102,639,169 | $ 47,500,000 | $52,485,872 | $ 3,307,847 | $ 96,678,025 | $ 199,317,194 | |

(1) Actual revenue and expense information was provided by Florida International University and has not been audited. Projected revenues and expenses for Fiscal Years 2011-12 through 2016-17, assuming annual rate increases of 3% and operating expenditures increasing at 2% annually, were provided by the University. Projections for Fiscal Year 2016-17 and thereafter are held constant; however, no representation is made that the amounts shown in any fiscal year will be collected. The new facility being constructed is scheduled to open fall 2013 (Fiscal Year 2013-14).

(2) Debt service on the proposed bonds has been calculated at 5.75%.

(3) Assumes capitalized interest through July 1, 2013, which is included in bond proceeds.

(4) Coverage of Pledged Revenues is determined by dividing Pledged Revenues by Total Outstanding Debt Service.

End of Section

**STATE BOARD OF ADMINISTRATION**
**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**

---

**TO:** Ash Williams
**FROM:** Robert Copeland
**SUBJECT:** Fiscal Sufficiency
**DATE:** March 7, 2012

---

**APPROVAL OF FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $31,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, UNIVERSITY OF FLORIDA DORMITORY REVENUE BONDS, SERIES 2012A:**

The Division of Bond Finance of the State Board of Administration (the "Division") has submitted for approval as to fiscal sufficiency a proposal to issue an amount not exceeding $31,000,000 State of Florida, Board of Governors, University of Florida Dormitory Revenue Bonds, Series 2012A (the "Bonds"), to finance the renovation of existing student housing facilities on the main campus of the University of Florida; fund a debt service reserve account, if necessary; and pay costs associated with the issuance and sale of the Bonds.

The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on January 10, 1989, as amended and restated in its entirety on June 13, 2000, and as further amended on September 20, 2011, and authorizing and sale resolutions which are anticipated to be adopted on March 20, 2012 (collectively referred to herein as the "Resolution"). The Division has heretofore issued University of Florida Housing Revenue Certificates, Series 1984 (the "Series 1984 Certificates"), Housing Revenue Refunding Bonds, Series 2005A (the "Series 2005A Bonds") and Dormitory Revenue Refunding Bonds, Series 2011A (the "Series 2011A Bonds"). The Bonds shall be junior and subordinate to the outstanding Series 1984 Certificates as to lien on and source and security for payment from the Pledged Revenues as described in the Resolution. The Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues and in all other respects, with the Series 2005A Bonds and Series 2011A Bonds.

A study of this proposal and the estimates of revenue expected to accrue indicate that the proposed Bonds are fiscally sufficient and that the proposal will be executed pursuant to the applicable provisions of law.

**RECOMMENDATION:** It is recommended that the Board approve the proposal outlined above.

cc: Janie Knight

**A RESOLUTION OF THE STATE BOARD OF ADMINISTRATION APPROVING THE FISCAL SUFFICIENCY OF AN AMOUNT NOT EXCEEDING $31,000,000 STATE OF FLORIDA, BOARD OF GOVERNORS, UNIVERSITY OF FLORIDA DORMITORY REVENUE BONDS, SERIES 2012A**

**WHEREAS,** the Division of Bond Finance of the State Board of Administration (the "Division") proposes to issue an amount not exceeding $31,000,000 State of Florida, Board of Governors, University of Florida Dormitory Revenue Bonds, Series (to be determined) (the "Bonds"), to finance the renovation of existing student housing facilities on the main campus of the University of Florida; fund a debt service reserve account, if necessary; and pay costs associated with the issuance and sale of the Bonds; and,

**WHEREAS,** the Division has requested the State Board of Administration to approve the fiscal sufficiency of the proposed issue as required by Section 215.73, Florida Statutes; and,

**WHEREAS,** The Bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on January 10, 1989, as amended and restated in its entirety on June 13, 2000, and as further amended on September 20, 2011, and authorizing and sale resolutions which are anticipated to be adopted on March 20, 2012 (collectively referred to herein as the "Resolution"); and,

**WHEREAS,** the Division has heretofore issued University of Florida Housing Revenue Certificates, Series 1984 (the "Series 1984 Certificates"), Housing Revenue Refunding Bonds, Series 2005A (the "Series 2005A Bonds") and Dormitory Revenue Refunding Bonds, Series 2011A (the "Series 2011A Bonds"); and,

**WHEREAS,** the Bonds shall be junior and subordinate to the outstanding Series 1984 Certificates as to lien on and source and security for payment from the Pledged Revenues as described in the Resolution; and,

**WHEREAS,** the Bonds shall be payable on a parity and rank equally as to lien on and source and security for payment from the Pledged Revenues and in all other respects, with the Series 2005A Bonds and Series 2011A Bonds; and,

**WHEREAS,** the principal of and interest due on the Bonds shall be paid solely out of revenues and other amounts pledged therefor, as described in the Resolution; and,

**WHEREAS,** the Bonds do not constitute an obligation, either general or special, of the State of Florida or any of its units of local government and shall not be a debt of the State or of any unit of local government, and neither the State nor any unit of local government shall be liable thereon; and,

**WHEREAS,** the University of Florida shall not have the power to pledge the credit, the revenues, or the taxing power of the State or of any unit of local government, and neither the credit, the revenues, nor the taxing power of the State or of any unit of local government shall be deemed to be pledged to the payment of the Bonds; and,

**WHEREAS,** the proceeds of the Bonds shall be and constitute trust funds and shall be used and applied solely in the manner and for the purposes provided in the Resolution; and,

**WHEREAS,** the estimate of funds pledged to the issue indicates that in no State fiscal year will the debt service requirements of the Bonds and all other issues secured by the same pledged revenues exceed the Pledged Revenues available for payment of such debt service requirements and that in no State fiscal year will the moneys pledged for the debt service requirements be less than the required coverage amount; and,

**WHEREAS,** the Division, has furnished sufficient information to enable the State Board of Administration to fulfill its duties pursuant to Section 215.73, Florida Statutes; and,

**WHEREAS,** the State Board of Administration has relied upon information from others but has not independently verified the accuracy or completeness of such information; and,

**WHEREAS,** the State Board of Administration does not approve or disapprove the Bonds as an investment and has not passed upon the accuracy or adequacy of the Official Statement; **Now, Therefore,**

**BE IT RESOLVED,** by the State Board of Administration of Florida, a constitutional body created by Section 4 of Article IV of the Constitution of the State of Florida, as revised in 1968 and subsequently amended, that pursuant to the requirements of Section 215.73, Florida Statutes, the proposal of the Division of Bond Finance of the State Board of Administration to issue an amount not exceeding $31,000,000 State of Florida, Board of Governors, University of Florida Dormitory Revenue Bonds, Series 2012A for the uses and purposes hereinabove set forth, is hereby approved as to fiscal sufficiency.

**ADOPTED** March 20, 2012

STATE OF FLORIDA

**DIVISION OF BOND FINANCE**
OF THE STATE BOARD OF ADMINISTRATION

HERMITAGE CENTRE, SUITE 200
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AS SECRETARY

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CHIEF FINANCIAL OFFICER
AS TREASURER

ADAM H. PUTNAM
COMMISSIONER OF AGRICULTURE

March 2, 2012

Mr. Ashbel C. Williams
Executive Director & CIO
State Board of Administration
Post Office Box 13300
Tallahassee, Florida 32317-3300

RE: Not Exceeding $31,000,000 State of Florida, Board of Governors, University of Florida Dormitory Revenue Bonds, Series 2012A

Dear Mr. Williams:

In compliance with Section 215.73, Florida Statutes, the Division of Bond Finance requests State Board of Administration approval as to fiscal sufficiency for the above referenced bond issue. We request such approval at your board meeting of March 20, 2012.

The proposed bonds will be secured by the revenues of the housing system after deducting operating expenses. Housing system revenues are derived primarily from rental income. The proposed bonds will be junior and subordinate to the previously issued University of Florida Housing Revenue Bonds, Series 1984, and on a parity with the outstanding University of Florida Housing Revenue Bonds, Series 2005A and 2011A.

The proposed bonds will be issued to finance the renovation of existing student housing facilities on the main campus of the University; to fund a reserve account, if necessary; and to pay costs associated with the issuance and sale of the proposed bonds.

Enclosed for your review are the following:

Enclosure 1: an estimated coverage table for the program, including the proposed $31,000,000 Series 2012A Bonds; and

Enclosure 2: an estimated debt service schedule for the proposed bonds.

The bonds will be issued pursuant to the Original Resolution adopted by the Governor and Cabinet on January 10, 1989, as amended and restated in its entirety on June 13, 2000, and as further amended on September 20, 2011, and authorizing and sale resolutions which are anticipated to be adopted on March 20, 2012. The Original Resolution as amended and restated has been previously provided and a draft of the resolution expected to be adopted on March 20, 2012 will be provided when available.

A draft of the fiscal sufficiency resolution should be sent to Kimberly Barrett and Toni Egan of this office for review. Should you have any questions, please contact either myself, Kimberly Barrett or Toni Egan at 488-4782. Your consideration of this matter is appreciated.

Sincerely,

J. Ben Watkins III
Director

JBW:kb

Enclosures

cc: Anthoney Doheny
Robert Copeland

**STATE OF FLORIDA BOARD OF GOVERNORS**
**UNIVERSITY OF FLORIDA**
**DORMITORY REVENUE BONDS, SERIES 2012A**
**FISCAL SUFFICIENCY REQUEST FOR NOT TO EXCEED $31,000,000**
**ESTIMATED DEBT SERVICE COVERAGE**

| Year Ending June 30 | Gross Revenues | Operating Expenses | Net Revenue | Prior Lien Requirement Series 1984 | Pledged Revenue | Outstanding Debt Service | Estimated Debt Service for Proposed Bonds Principal | Interest | Total | Total Estimated Debt Service | Debt Service Coverage [2] |
|---|---|---|---|---|---|---|---|---|---|---|---|
| *Historical* | | | | | | | | | | | |
| 2007 | 38,897,598 | 26,280,764 | 12,616,834 | 189,150 | 12,427,684 | 4,857,090 | | | | | 2.56 |
| 2008 | 39,954,112 | 26,032,956 | 13,921,156 | 184,650 | 13,736,506 | 4,838,023 | | | | | 2.84 |
| 2009 | 41,064,724 | 27,023,135 | 14,041,589 | 185,150 | 13,856,439 | 4,848,098 | | | | | 2.86 |
| 2010 | 44,884,748 | 27,023,478 | 17,861,270 | 185,500 | 17,675,770 | 4,860,390 | | | | | 3.64 |
| 2011 | 44,674,109 | 28,962,074 | 15,712,035 | 185,700 | 15,526,335 | 4,856,640 | | | | | 3.20 |
| *Projected* [1] | | | | | | | | | | | |
| 2012 | 45,955,312 | 30,410,177 | 15,545,135 | 185,750 | 15,359,385 | 4,709,474 | - | 445,656 | 445,656 | 5,155,130 | 2.98 |
| 2013 | 47,333,971 | 31,930,686 | 15,403,285 | 185,650 | 15,217,635 | 4,685,188 | 940,000 | 1,782,500 | 2,722,500 | 7,407,688 | 2.05 |
| 2014 | 48,753,989 | 33,527,221 | 15,226,768 | 185,400 | 15,041,368 | 4,687,313 | 995,000 | 1,728,450 | 2,723,450 | 7,410,763 | 2.03 |
| 2015 | 50,216,610 | 35,203,582 | 15,013,028 | | 15,013,028 | 4,708,763 | 1,055,000 | 1,671,238 | 2,726,238 | 7,435,000 | 2.02 |
| 2016 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 4,703,013 | 1,115,000 | 1,610,575 | 2,725,575 | 7,428,588 | 1.99 |
| 2017 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 4,690,813 | 1,180,000 | 1,546,463 | 2,726,463 | 7,417,275 | 1.99 |
| 2018 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 4,712,563 | 1,245,000 | 1,478,613 | 2,723,613 | 7,436,175 | 1.98 |
| 2019 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 4,701,913 | 1,315,000 | 1,407,025 | 2,722,025 | 7,423,938 | 1.99 |
| 2020 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 3,784,813 | 1,395,000 | 1,331,413 | 2,726,413 | 6,511,225 | 2.27 |
| 2021 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 3,784,013 | 1,475,000 | 1,251,200 | 2,726,200 | 6,510,213 | 2.27 |
| 2022 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 3,791,175 | 1,560,000 | 1,166,388 | 2,726,388 | 6,517,563 | 2.26 |
| 2023 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 3,796,419 | 1,645,000 | 1,076,688 | 2,721,688 | 6,518,106 | 2.26 |
| 2024 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,844,444 | 1,740,000 | 982,100 | 2,722,100 | 5,566,544 | 2.65 |
| 2025 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,852,769 | 1,840,000 | 882,050 | 2,722,050 | 5,574,819 | 2.65 |
| 2026 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,848,006 | 1,945,000 | 776,250 | 2,721,250 | 5,569,256 | 2.65 |
| 2027 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,849,606 | 2,060,000 | 664,413 | 2,724,413 | 5,574,019 | 2.65 |
| 2028 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,851,006 | 2,180,000 | 545,963 | 2,725,963 | 5,576,969 | 2.65 |
| 2029 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,049,750 | 2,305,000 | 420,613 | 2,725,613 | 4,775,363 | 3.09 |
| 2030 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | 2,044,681 | 2,435,000 | 288,075 | 2,723,075 | 4,767,756 | 3.10 |
| 2031 | 51,723,108 | 36,963,761 | 14,759,347 | | 14,759,347 | - | 2,575,000 | 148,063 | 2,723,063 | 2,723,063 | 5.42 |
| | | | | 556,800 | | 71,095,717 | 31,000,000 | 21,203,731 | 52,203,731 | 123,299,448 | |

[1] Actual Revenues and Expenses provided by the University of Florida for Fiscal Years 2007 through 2011. Projections provided by the University of Florida for Fiscal Years 2012 through 2016, assuming 3% annual revenue growth due primarily to rental rate increases and 5% annual increases in expenses. Projections for Fiscal Year 2017 and thereafter are held constant; however, no representation is made that the amounts shown will be collected.

[2] Coverage of Pledged Revenues is determined by dividing Pledged Revenues by Outstanding Debt Service.

End of Section

# Protecting Florida's Investments Act (PFIA)

Quarterly Report – March 20, 2012

***4Q / 2012***

SBA FLORIDA

www.sbafla.com

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***About the State Board of Administration***

The statutory mission of the State Board of Administration (SBA) is to invest, manage and safeguard assets of the Florida Retirement System (FRS) Trust Fund and a variety of other funds for state and local governments. FRS Trustees are dedicated to ensuring that the SBA invests assets and discharges its duties in accordance with Florida law, guided by strict policies and a code of ethics to ensure integrity, prudent risk management and top-tier performance. The SBA is an investment fiduciary under law, and subject to the stringent fiduciary duties and standards of care defined by the Employee Retirement Income Security Act of 1974 (ERISA), as incorporated into Florida law. The SBA has three Trustees: the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary.

As of December 31, 2011, the net asset value of total funds under SBA management was approximately $149 billion. The FRS Pension Plan provides defined pension benefits to 1.1 million beneficiaries and retirees. The strong long-term performance of the FRS Pension Plan, the fourth-largest public pension fund in the nation, reflects our commitment to responsible fiscal management. The SBA strives to meet the highest ethical, fiduciary and professional standards while performing its mission, with a continued emphasis on keeping operating and investment management costs as low as possible for the benefit of Florida taxpayers.

We encourage you to review additional information about the SBA and FRS on our website at www.sbafla.com.

# *Introduction*

On June 8, 2007, the Protecting Florida's Investments Act ("PFIA") was signed into law. The PFIA requires the State Board of Administration ("SBA"), acting on behalf of the Florida Retirement System Trust Fund (the "FRSTF"), to assemble and publish a list of "Scrutinized Companies" that have prohibited business operations in Sudan and Iran. Once placed on the list of Scrutinized Companies, the SBA and its investment managers are prohibited from acquiring those companies' securities and are required to divest those securities if the companies do not cease the prohibited activities or take certain compensating actions. The implementation of the PFIA by the SBA will not affect any FRSTF investments in U.S. companies. The PFIA will solely affect foreign companies with certain business operations in Sudan and Iran involving the petroleum or energy sector, oil or mineral extraction, power production or military support activities. This quarterly report is developed pursuant to Section 215.473 (4), Florida Statutes.

### *Primary Requirements of the PFIA*

The PFIA created new reporting, engagement, and investment requirements for the SBA, including:

1. Quarterly reporting to the Board of Trustees of every equity security in which the SBA has invested for the quarter, along with its industry category. This report is posted on the SBA website.

2. Quarterly presentation to the Trustees of a "Scrutinized Companies" list for both Sudan and Iran for their approval. Scrutinized Company lists are available on the SBA's website, along with information on the FRSTF direct and indirect holdings of Scrutinized Companies.

3. Written notice to external investment managers of all PFIA requirements. Letters request that the managers of actively managed commingled vehicles (i.e., those with FRSTF and other clients' assets) consider removing Scrutinized Companies from the product or create a similar actively managed product that excludes such companies. Similar written requests must be provided to relevant investment managers within the defined contribution plan.

4. Written notice to any company with inactive business operations in Sudan or Iran, informing the company of the PFIA and encouraging it to continue to refrain from reinitiating active business operations. Such correspondence continues semiannually.

5. Written notice to any Scrutinized Company with active business operations, informing the company of its Scrutinized Company status and that it may become subject to divestment. The written notice must inform the company of the opportunity to clarify its Sudan-related or Iran-related activities and encourage the company, within 90 days, to cease its scrutinized business operations or convert such operations to inactive status.

6. A prohibition on further investment on behalf of the FRSTF in any Scrutinized Company once the Sudan and Iran scrutinized lists have been approved by the Trustees. All publicly traded securities of Scrutinized Companies must be divested within 12 months after the company's initial (and continued) appearance on the Scrutinized Companies list. Divestment does not apply to indirect holdings in actively managed commingled investment funds—i.e., where the SBA is not the sole investor in the fund. Private equity funds are considered to be actively managed.

7. Reporting to each member of the Board of Trustees, President of the Senate, and the Speaker of the House of Representatives of Scrutinized Company lists within 30 days of creation, and public disclosure of each list.

8. Quarterly reporting of the following to each member of the Board of Trustees, the President of the Senate, the Speaker of the House of Representatives, the United States Presidential Special Envoy to Sudan, and the United States Presidential Special Envoy to Iran. The report is made publicly available and posted to the SBA's website.

a. A summary of correspondence with engaged companies;
b. A listing of all investments sold, redeemed, divested, or withdrawn;
c. A listing of all prohibited investments;
d. A description of any progress related to external managers offering PFIA compliant funds; and
e. A list of all publicly traded securities held directly by the state.

9. Adoption and incorporation into the FRSTF Investment Policy Statement (IPS) of SBA actions taken in accordance with the PFIA. Changes to the IPS are reviewed by the Investment Advisory Council (IAC) and approved by the Trustees.

10. Relevant Sudan or Iran portions of the PFIA are discontinued if the Congress or President of the United States passes legislation, executive order, or other written certification that:

    a. Darfur genocide has been halted for at least 12 months;
    b. Sanctions imposed against the Government of Sudan are revoked;
    c. Government of Sudan honors its commitments to cease attacks on civilians, demobilize and demilitarize the Janjaweed and associated militias, grant free and unfettered access for deliveries of humanitarian assistance, and allow for the safe and voluntary return of refugees and internally displaced persons;
    d. Government of Iran has ceased to acquire weapons of mass destruction and support international terrorism;
    e. Sanctions imposed against the government of Iran are revoked; or
    f. Mandatory divestment of the type provided for by the PFIA interferes with the conduct of U.S. foreign policy.

11. Cessation of divestment and/or reinvestment into previously divested companies may occur if the value of all FRSTF assets under management decreases by 50 basis points (0.5%) or more as a result of divestment. If cessation of divestment is triggered, the SBA is required to provide a written report to each member of the Board of Trustees, the President of the Senate, and the Speaker of the House of Representatives prior to initial reinvestment. Such condition is required to be updated semiannually.

12. In 2009, the Florida Legislature approved a bill requiring the SBA to identify and offer, by March 1, 2010, at least one terror-free investment product for the FRS Investment Plan. The product must allocate its funds among securities not subject to divestiture, as provided in section 215.473, Florida Statutes.

***Definition of a Scrutinized Company***

The following is a brief review of the criteria on which the active business operations of companies must be judged, in accordance with subsection (1)(t) of Section 215.473, F.S.

***Sudan:***

1. Have a material business relationship with the government of Sudan or a government-created project involving oil related, mineral extraction, or power generation activities, or
2. Have a material business relationship involving the supply of military equipment, or
3. Impart minimal benefit to disadvantaged citizens that are typically located in the geographic periphery of Sudan, or
4. Have been complicit in the genocidal campaign in Darfur.

***Iran:***

1. Have a material business relationship with the government of Iran or a government-created project involving oil related or mineral extraction activities, or
2. Have made material investments with the effect of significantly enhancing Iran's petroleum sector.

Affiliates of companies with scrutinized business operations are also subject to the requirements of the PFIA. An affiliated company is generally defined as any other company that either directly or indirectly controls, is controlled by or is under common control with the company conducting scrutinized active business operations. Control generally means the power to exercise a controlling influence over the management or policies of a company. As well, many companies have parent-subsidiary relationships whereby a parent company may own several other companies. In such cases, the SBA has included any known parent and/or subsidiaries which can be clearly linked to a company with scrutinized active business operations. The SBA has used a 50 percent ownership threshold in determining whether or not companies are affiliated, examining parent company-subsidiary ownership on a pro rata basis.

The SBA views companies which have explicit plans and activities related to discontinuation of active business operations as meeting the PFIA definition of substantial action. For all identified companies, the SBA will request information detailing what a company has actually done, if anything, to discontinue its active business operations or if it has pursued humanitarian efforts (applicable to Sudan only).

***SBA Scrutinized Companies Identification Methodology***

The SBA has developed two lists (the Sudan List and the Iran List) of Scrutinized Companies with active business operations. The lists are developed by principally relying on the research and findings of our "External Research Providers". Below is a brief description of our External Research Providers. MSCI has acquired and combined the operations of two of our longtime providers, RiskMetrics Group and KLD Research & Analytics, resulting in MSCI ESG Research. To maintain input from multiple consultants, we have added research from IW Financial and Jantzi-Sustainalytics.

1. **Conflict Risk Network (CRN).** CRN is a network of institutional investors, financial service providers and related stakeholders and is a project of the Genocide Intervention Network / Save Darfur Coalition (GI-NET/SDC), a non-profit organization that works to prevent and stop genocide and mass atrocities. In support of GI-NET/SDC's overall mission, CRN acts as an intermediary between the business and investment communities, engaging companies operating in GINET/SDC's Areas of Concern, including Sudan. CRN was formerly known as the Sudan Divestment Task Force (SDTF).

2. **MSCI ESG Research (MSCI)**. MSCI combined, through acquisition, the resources of the RiskMetrics Group (Institutional Shareholder Services) and KLD Research & Analytics (KLD). MSCI delivers proxy voting and corporate governance analysis to institutional investors. Through its ESG Research unit, MSCI offers screening services with specific and unique components of state law pertaining to investments in sanctioned countries, including Sudan and Iran.

3. **IW Financial (IWF).** IWF is a provider of environmental, social, and governance research and consulting. IWF partners with Conflict Securities Advisory Group (CSAG) to provide clients with detailed information on the business ties of publicly traded companies in Sudan and Iran.

4. **Jantzi-Sustainalytics, Inc. (Jantzi).** Jantzi provides environmental, social and governance research and analysis, sustainability benchmarks, and investment services, and is the result of the merger between Jantzi Research, Inc. and Sustainalytics in 2009. Jantzi's company database, "Sustainalytics Global Platform," covers business operations in both Iran and Sudan.

Staff members within the Investment Programs & Governance unit, as well as other senior investment staff, review the assessments of the External Research Providers and other publicly available information. The SBA has utilized the following sources to evaluate over 400 companies and affiliates with reported links to Sudan or Iran:

Company disclosures:
- SEC filings (DEF 14A Proxy Statements, 10-K & 20-F Annual Reports, etc.)
- Investor Relations/company websites
- Industry publications and analyst research

Investment/Finance Organizations:
- Industry Analysts
- Index Providers (e.g., Russell)
- Other Institutional Investors/Private Investors

U.S Government Agencies:
- U.S. Treasury, Office of Foreign Asset Control (OFAC)
- U.S. Government Accountability Office (GAO)
- SEC Office of Global Security (EDGAR)
- Dept. of Energy, Energy Information Administration (EIA)
- Congressional Research Service (CRS), Library of Congress

Non-Governmental Organizations (NGOs):
- American Enterprise Institute (AEI)
- Amnesty International
- Yale University (Allard K. Lowenstein International Human Rights Project)
- Human Rights Watch

Other Sources:
- SBA External Investment Managers
- U.S. Federal Sanctions Laws covering State Sponsors of Terror
- Any other publicly available information.

Using the previous information sources, the SBA has developed two separate categorizations of a company's involvement in Sudan and/or Iran.

1. **"Scrutinized"** — Information provided by several External Research Providers indicates that a company meets the classification of a Scrutinized Company as defined by the PFIA as set forth in Section 215.473 (1)(t)1., 2., or 3. [Sudan] or Section 215.473 (4)(t)1. [Iran]. Upon SBA review, no other information sources clearly contradict the conclusions of the External Research Providers.

2. **"Continued Examination"** — At least one External Research Provider indicates that a company meets the classification of a Scrutinized Company as defined by the PFIA as set forth in Section 215.473, (1)(t)1., 2., or 3. [Sudan] or Section 215.473, (4)(t)1. [Iran]. In other words, the External Research Providers do not agree on the status of a company and the SBA is unable to definitively categorize the company's activities as scrutinized without further research to resolve the differences. For companies classified as "Continued Examination" the SBA will begin an engagement process to clarify each firm's current business relationships.

## *Key Changes Since the Previous PFIA Quarterly Report*

### Sudan

Companies *added* to the Sudan Scrutinized List this quarter:

- **None**

Companies *removed* from the Sudan Scrutinized List this quarter:

- **Dongan Motor (aka Harbin Dongan Auto Engine)**
- **Hafei Aviation Industry Co Ltd**
- **KEPCO Plant Service & Engineering Co Ltd**
- **Korea Electric Power (KEPCO) – parent company of KEPCO Plant Service & Engineering**
- **Korea Plant Service & Engineering Co Ltd**

Companies *added* to the Sudan Continued Examination List this quarter:

- **Dongan Motor (aka Harbin Dongan Auto Engine)**
- **Hafei Aviation Industry Co Ltd**
- **KEPCO Plant Service & Engineering Co Ltd**
- **Korea Electric Power (KEPCO) – parent company of KEPCO Plant Service & Engineering**
- **Muhibbah Engineering Bhd**

Companies *removed* from the Sudan Continued Examination List this quarter:

- **Dongfeng Automobile Co. Ltd.**
- **Nuinsco Resources Ltd.**

---

### Iran

Companies *added* to the Iran Scrutinized List this quarter:

- **Rosier SA,** added as a majority owned subsidiary of Total SA, a prohibited investment.
- **Total Kenya Limited,** added as a majority owned subsidiary of Total SA, a prohibited investment.

Companies *removed* from the Iran Scrutinized List this quarter:

- **None**

Companies *added* to the Iran Continued Examination List this quarter:

- **None**

Companies *removed* from the Iran Continued Examination List this quarter:

- **Welspun Corp. Limited (fka Welspun-Gujarat Stahl Rohren Ltd.)**

## *Table 1: Scrutinized Companies with Activities in Sudan*

***No companies were added to the list this quarter.***

| *Company* | *Country of Incorporation* | *Date of Initial Scrutinized Classification* |
|---|---|---|
| AREF Energy Holdings Co. | Kuwait | July 28, 2009 |
| AviChina Industry & Technology Company Limited | China | September 19, 2007 |
| Chennai Petroleum Corp Ltd | India | September 19, 2007 |
| China Petroleum & Chemical Corp (CPCC) Sinopec | China | September 19, 2007 |
| China Petroleum Finance Co. | China | November 9, 2010 |
| CNPC HK Overseas Capital Ltd | China | June 16, 2011 |
| Daqing Huake Group Co Ltd | China | March 25, 2008 |
| Dongfeng Motor Group Co. Ltd. | China | July 29, 2010 |
| Egypt Kuwait Holding Co. SAE | Kuwait | January 13, 2009 |
| Electricity Generating Public Co | Thailand | September 19, 2007 |
| Gas District Cooling (Putrajaya) Sdn Bhd | Malaysia | April 14, 2009 |
| Groupe ONA (ONA SA) | Morocco | November 9, 2010 |
| Harbin Electric Co. Ltd. (fka: Harbin Power Equipment) | China | September 19, 2007 |
| Indian Oil Corp Ltd (IOCL) | India | September 19, 2007 |
| Jiangxi Hongdu Aviation (aka Hongdu Aviation) | China | September 19, 2007 |
| Jinan Diesel Engine Co. Ltd. | China | July 28, 2009 |
| Kingdream PLC | China | April 14, 2009 |
| KLCC Property Holdings Bhd | Malaysia | April 14, 2009 |
| KMCOB Capital Bhd | Malaysia | September 19, 2007 |
| Kunlun Energy Company Ltd (fka: CNPC Hong Kong Limited) | Hong Kong | September 19, 2007 |
| Kuwait Finance House | Kuwait | April 14, 2009 |
| Lanka IOC Ltd | India | September 19, 2007 |
| LS Industrial Systems | South Korea | September 20, 2011 |
| Managem SA | Morocco | November 9, 2010 |
| Mangalore Refinery & Petrochemicals Ltd | India | September 19, 2007 |
| Midciti Resources Sdn Bhd | Malaysia | September 19, 2007 |
| MISC Bhd | Malaysia | September 19, 2007 |
| MISC Capital Ltd. | Malaysia | April 14, 2009 |
| Oil & Natural Gas Corp (ONGC) | India | September 19, 2007 |
| PetroChina | China | September 19, 2007 |
| Petroliam Nasional (Petronas) | Malaysia | September 19, 2007 |
| Petronas Capital Limited | Malaysia | September 19, 2007 |
| Petronas Chemicals Bhd | Malaysia | June 16, 2011 |
| Petronas Dagangan Bhd | Malaysia | September 19, 2007 |
| Petronas Gas Berhad | Malaysia | September 19, 2007 |
| Ranhill Bhd | Malaysia | September 16, 2008 |
| Ranhill Power Sdn Bhd | Malaysia | September 20, 2011 |

| ***Company*** | ***Country of Incorporation*** | ***Date of Initial Scrutinized Classification*** |
|---|---|---|
| Ranhill Powertron Sdn | Malaysia | April 14, 2009 |
| Scomi Engineering Bhd | Malaysia | September 19, 2007 |
| Scomi Group Bhd | Malaysia | September 19, 2007 |
| Sinopec Finance | China | April 14, 2009 |
| Sinopec Kantons Holdings Ltd | Bermuda | September 19, 2007 |
| Sinopec Shanghai Petrochemical | China | September 19, 2007 |
| Sinopec Yizheng Chemical Fibre | China | March 25, 2008 |
| Societe Metallurgique D'imiter | Morocco | November 9, 2010 |
| **# of Sudan Scrutinized Companies** | **45** | |

The following companies were **removed** from the Scrutinized Company List for Sudan during the quarter.

| ***Removed Company*** | ***Country of Incorporation*** |
|---|---|
| ***Dongan Motor (aka Harbin Dongan Auto Engine)*** | ***China*** |
| ***Hafei Aviation Industry Co Ltd*** | ***China*** |
| ***KEPCO Plant Service & Engineering Co Ltd*** | ***South Korea*** |
| ***Korea Electric Power (KEPCO)*** | ***South Korea*** |
| ***Korea Plant Service & Engineering Co Ltd*** | ***South Korea*** |

### *Table 2: Continued Examination Companies with Activities in Sudan*

***New companies on the list are shaded and in bold.***

| Company | Country of Incorporation |
|---|---|
| Alstom | France |
| Alstom Projects India | India |
| AREF Investment Group | Kuwait |
| ASEC Company for Mining S.A.E. | Egypt |
| Bharat Heavy Electricals, Ltd. | India |
| Bollore Group | France |
| China Gezhouba Group Company Ltd | China |
| China North Industries Group Corp (CNGC/Norinco) | China |
| **Dongan Motor (aka Harbin Dongan Auto Engine)** | **China** |
| Drake & Scull International PJSC | United Arab Emirates |
| El Sewedy Cables Holding Company | Egypt |
| GAZ Group | Russia |
| Glencore International AG | Switzerland |
| **Hafei Aviation Industry Co Ltd.** | **China** |
| Infotel Broadband Services Ltd. | India |
| JX Holdings Inc. | Japan |
| Kencana Petroleum Berhad | Malaysia |
| **KEPCO Plant Service & Engineering Co Ltd** | **South Korea** |
| **Korea Electric Power (KEPCO)** | **South Korea** |
| Mercator Lines Limited (Mercator Lines Singapore) | India |
| **Muhibbah Engineering Bhd** | **Malaysia** |
| Nam Fatt | Malaysia |
| Nippo Corporation | Japan |
| Nippon Oil Finance | Japan |
| Oil India Limited | India |
| PetroFac | United Kingdom |
| PT Pertamina Persero | Indonesia |
| PTT Public Company Ltd. | Thailand |
| Reliance Industries Ltd. | India |
| Seadrill Ltd. | Bermuda |
| Sinohydro | China |
| Sudan Telecommunications (Sudatel) | Sudan |
| Total SA | France |
| Wartsila Oyj | Finland |
| Wuhan Boiler Company | China |
| **# of Companies** | **35** |

The following companies were **removed** from the Continued Examination List for Sudan during the quarter.

| ***Removed Company*** | ***Country of Incorporation*** |
|---|---|
| ***Dongfeng Automobile Co. Ltd.*** | ***China*** |
| ***Nuinsco Resources Ltd.*** | ***Canada*** |

### *Table 3: Scrutinized Companies with Activities in the Iran Petroleum Energy Sector*

***New companies on the list are shaded and in bold.***

| Company | Country of Incorporation | Date of Initial Scrutinized Classification |
|---|---|---|
| China Petroleum & Chemical Corp (CPCC) Sinopec | China | September 19, 2007 |
| China Oilfield Services Ltd | China | June 16, 2011 |
| CNOOC Ltd | China | June 16, 2011 |
| CNPC HK Overseas Capital Ltd | China | June 16, 2011 |
| Daelim Industrial Co Ltd | South Korea | June 16, 2011 |
| ENI | Italy | September 19, 2007 |
| Gas District Cooling (Putrajaya) Sdn Bhd | Malaysia | April 14, 2009 |
| Gazprom | Russia | September 19, 2007 |
| Gazprom Neft | Russia | September 16, 2008 |
| Indian Oil Corp Ltd (IOCL) | India | September 19, 2007 |
| Kingdream PLC | China | April 14, 2009 |
| Kunlun Energy Company Ltd. (fka: CNPC Hong Kong Limited) | Hong Kong | September 19, 2007 |
| KLCC Property Holdings Bhd | Malaysia | April 14, 2009 |
| Maire Technimont | Italy | December 6, 2011 |
| Midciti Resources Sdn Bhd | Malaysia | September 19, 2007 |
| MISC Bhd | Malaysia | September 19, 2007 |
| MISC Capital Ltd. | Malaysia | April 14, 2009 |
| Mosenergo | Russia | September 16, 2008 |
| Oil & Natural Gas Corp (ONGC) | India | September 19, 2007 |
| PetroChina | China | September 19, 2007 |
| Petroliam Nasional (Petronas) | Malaysia | September 19, 2007 |
| Petronas Capital Limited | Malaysia | September 19, 2007 |
| Petronas Chemicals Bhd | Malaysia | June 16, 2011 |
| Petronas Dagangan Bhd | Malaysia | September 19, 2007 |
| Petronas Gas Berhad | Malaysia | September 19, 2007 |
| **Rosier SA** | **Belgium** | **March 20, 2012** |
| Sinopec Finance | China | April 14, 2009 |
| Sinopec Kantons Holdings Ltd | Bermuda | September 19, 2007 |
| Sinopec Shanghai Petrochemical | China | September 19, 2007 |
| Sinopec Yizheng Chemical F bre | China | March 25, 2008 |
| Snam Rete Gas | Italy | September 19, 2007 |
| Total Capital | France | November 9, 2010 |
| Total Gabon | Gabon | November 9, 2010 |
| **Total Kenya Ltd** | **Kenya** | **March 20, 2012** |
| Total (Nigeria) PLC | Nigeria | March 25, 2008 |
| Total SA | France | September 19, 2007 |
| **# of Iran Scrutinized Companies** | **36** | |

No companies were **removed** from the Scrutinized Company List for IRAN during the quarter.

### *Table 4: Continued Examination Companies with Petroleum Energy Activities in Iran*

***No companies were added to the list this quarter.***

| Company | Country of Incorporation |
|---|---|
| Aker Solutions ASA (fka Aker Kvaerner ASA) | Norway |
| Clontarf Energy Plc (fka Persian Gold PLC) | United Kingdom |
| Edison Spa | Italy |
| GAIL (India) Limited, aka GAIL Ltd. | India |
| GS Engineering & Construction Corp. | South Korea |
| GS Holdings | South Korea |
| Hyundai Engineering & Construction Co. | South Korea |
| Hyundai Heavy Industries | South Korea |
| INA-Industrija Nafte DD | Croatia |
| Liquefied Natural Gas LNGL | Australia |
| Lukoil OAO | Russia |
| Mangalore Refinery & Petrochemicals Ltd. | India |
| OMV AG | Austria |
| Petrofac Ltd. | United Kingdom |
| PTT Exploration & Production PCL | Thailand |
| Repsol YPF | Spain |
| Royal Dutch Shell PLC | United Kingdom |
| Saipem SpA | Italy |
| Sasol Ltd. | South Africa |
| Siam Cement PCL | Thailand |
| Statoil ASA (fka: Statoil Hydro) | Norway |
| Technip | France |
| **# of Companies** | **22** |

The following companies were **removed** from the Continued Examination Company List for IRAN during the quarter.

| *Removed Company* | *Country of Incorporation* |
|---|---|
| ***Welspun Corp. Limited (fka Welspun-Gujarat Stahl Rohren Ltd.)*** | ***India*** |

### *Table 5: Correspondence & Engagement Efforts with Scrutinized Companies*

In accordance with Section 215.473(3)(a), F.S., the SBA began to engage companies on the September 19, 2007, Scrutinized Company lists. The SBA sent letters to each Scrutinized Company that was owned and held as of September 19, 2007, per the requirements of the law.

The SBA also sent written communication to other scrutinized firms since the initial company engagement effort in September 2007. Each letter encouraged the company to cease any active business operations within 90 days or convert such operations to inactive status to avoid qualifying for divestment by the SBA. In addition, the SBA sent a second letter to scrutinized companies on January 25, 2008, again requesting companies to provide all information necessary to avoid divestment.

On September 30, 2008, the SBA sent a follow-up letter to all Scrutinized Companies. Although, these companies are no longer held by the SBA, the September 30, 2008, letter was intended to once again provide notice of the requirements of the PFIA. Since our original correspondence, several companies on the scrutinized list have replied with valuable information. Each company's response and classification status is summarized below. Any company that responded to the SBA's written correspondence is highlighted in blue text.

| Company | Company Responsive to SBA Communications | Status |
|---|---|---|
| ABB | Yes; January 29, 2009 | Removed from Sudan Scrutinized List |
| Alstom | Yes; October 1, 2007 and October 25, 2011 | Moved to Sudan Continued Examination List |
| Bharat Heavy Electricals Limited | Yes; October 4, 2007 | Sudan Scrutinized Classification Continues |
| Bow Valley Energy | Yes; October 22, 2008 | Removed from Iran Scrutinized List |
| Chennai Petroleum Corporation Limited | Yes; October 16, 2008 | Sudan Scrutinized Classification Continues |
| China Petroleum & Chemical Corp (Sinopec) | No | Iran & Sudan Scrutinized Classification Continues |
| CNOOC Ltd | Yes; October 28, 2008 | Iran Scrutinized Classification Continues |
| Dongfeng Motor Group Co. Ltd. | No | Sudan Scrutinized Classification Continues |
| Electricity Generating PCL | No | Sudan Scrutinized Classification Continues |
| ENI | Yes; February 13, 2008 and May 13, 2011 | Iran Scrutinized Classification Continues |
| GAIL (India) Limited, aka GAIL Ltd. | Yes; October 5, 2010 | Moved to Iran Continued Examination List |
| Gazprom | Yes; November 1, 2007 | Iran Scrutinized Classification Continues |
| Harbin Electric Co. (fka Harbin Power Equipment) | No | Sudan Scrutinized Classification Continues |
| Indian Oil Corp Ltd (IOCL) | No | Iran & Sudan Scrutinized Classification Continues |
| Inpex Corp. | Yes; October 15, 2007 and July 11, 2011 | Removed Iran Scrutinized List |
| Kencana Petroleum | Yes; October 31, 2008 | Moved to Sudan Continued Examination List |
| Korea Electric Power (and subsidiaries, KEPCO Plant/Korea Plant) | Yes; December 27, 2011 | Removed from Sudan Scrutinized List |
| Kunlun Energy Company Ltd. (fka: CNPC Hong Kong Limited) | Yes; October 5, 2007 and May 24, 2008 | Iran & Sudan Scrutinized Classification Continues |
| Lukoil OAO | Yes; October 8, 2007 | Moved to Iran Continued Examination List |
| Lundin Petroleum AB | Yes; October 17, 2008 | Removed from Sudan Scrutinized List |
| Lundin International SA | No | Removed from Sudan Scrutinized List |
| MISC Bhd | No | Iran & Sudan Scrutinized Classification Continues |
| Norsk Hydro | Yes; November 30,2007 | Removed from Iran Scrutinized List |

| Company | Company Responsive to SBA Communications | Status |
|---|---|---|
| OMV AG | Yes; November 6, 2007 and April 14, 2010 | Moved to Iran Continued Examination List |
| PetroChina | Yes; December 22, 2008 | Iran & Sudan Scrutinized Classification Continues |
| Petroleo Brasileiro (Petrobras) | Yes; January 13, 2010 | Removed from Iran Scrutinized List |
| Ranhill Bhd | Yes; October 22, 2008 | Sudan Scrutinized Classification Continues |
| Repsol YPF | Yes; October 15, 2007 | Iran Scrutinized Classification Continues |
| Royal Dutch Shell PLC | Yes; October 5, 2007; January 27, 2011; April 13, 2011 | Moved to Iran Continued Examination List |
| Sinopec Kantons Holdings Ltd. | No | Iran & Sudan Scrutinized Classification Continues |
| Sinopec Shanghai Petrochemical Company | No | Sudan Scrutinized Classification Continues |
| Snam Rete Gas | Yes; October 9, 2008 | Iran Scrutinized Classification Continues |
| Statoil ASA (fka: StatoilHydro) | Yes; February 4, 2008; January 24, 2011; June 16, 2011 | Moved to Iran Continued Examination List |
| Total Capital | Yes; January 26, 2011 and April 25, 2011 | Iran Scrutinized Classification Continues |
| Total SA | Yes; October 12, 2007; October 29, 2010; April 25, 2011 | Iran Scrutinized Classification Continues |
| Wärtsilä Oyj | Yes; December 4, 2007 | Moved to Sudan Continued Examination List |

### *Table 6: Correspondence & Engagement Efforts with Continued Examination Companies*

In addition to Scrutinized Companies, the SBA engaged companies on our initial September 19, 2007, Continued Examination company lists. The SBA also sent written communication to firms added to the Continued Examination list since the initial company engagement effort in September 2007. Such companies were asked to provide information to the SBA in order to assist us in determining the extent of their activities, if any, in Sudan and Iran. The SBA sent a follow-up letter to all companies on September 30, 2008. Each company's response and classification is summarized below. Any company that responded to the SBA's written correspondence is highlighted in blue text.

| Company | Company Responsive to SBA Communications | Continued Examination Status |
|---|---|---|
| Actividades de Construccion y Servicios S.A.(ACS) | No | Removed from Iran List |
| Aggreko PLC | Yes; January 28, 2008 | Removed from Iran List |
| Air Liquide | Yes; November 30, 2007<br>January 28, 2008 | Removed from Iran List |
| Aker Solutions ASA (fka Aker Kvaerner ASA) | No | Iran CE Classification Continues |
| AREF Investment Group | No | Removed from Sudan List |
| Areva SA | Yes; October 27, 2008<br>December 29, 2009 | Removed from Sudan List |
| Bauer Aktiengesellschaft | Yes; March 13, 2008 | Removed from Sudan List |
| BG Group | Yes; November 23, 2007 | Removed from Iran List |
| Bharat Electronics Limited | No | Removed from Sudan CE List |
| Bollore Group | No | Sudan CE Classification Continues |
| Costain Group PLC | Yes; November 5, 2007 | Removed from Iran List |
| Daelim Industrial Co Ltd | No | Moved to Iran Scrutinized List |
| Engineers India Ltd. | Yes; October 16, 2008;<br>September 9, 2010 | Removed from Iran CE List |
| Essar Oil | Yes; January 9, 2009 | Removed from Iran List |
| Finmeccanica SpA | No | Removed from Sudan List |
| Glencore International AG | Yes; September 20, 2010 | Sudan CE Classification Continues |
| GVA Consultants | Yes; September 26, 2007<br>September 30, 2010 | Removed from Iran CE List |
| ICSA India Limited | No | Removed from Sudan List |
| Itochu Corp | Yes; May 9, 2008 | Removed from Iran List |
| JGC Corp | Yes; October 1, 2007 | Removed from Iran List |
| La Mancha Resources | Yes; October 21, 2008 | Removed from Sudan List |
| Linde AG | Yes; November 14, 2007 | Removed from Iran List |
| Liquefied Natural Gas LNGL | No | Iran CE Classification Continues |
| Mitsubishi Heavy Industries Ltd. | Yes; October 26, 2007 | Removed from Iran List |
| Mitsui & Co. | Yes; October 17, 2007 | Removed from Iran List |
| Mitsui Engineering & Shipbuilding | Yes; November 21, 2007<br>December 18, 2007 | Removed from Iran and Sudan Lists |
| MMC Bhd | No | Sudan CE Classification Continues |
| Nam Fatt | No | Sudan CE Classification Continues |
| PT Citra Tubindo Tbk. | Yes; September 27, 2010 | Removed from Iran CE List |

| Company | Company Responsive to SBA Communications | Continued Examination Status |
|---|---|---|
| PTT Public Company Limited | Yes; October 1, 2010 | Sudan CE Classification Continues |
| Saipem | Yes; December 12, 2007 | Removed from Iran List |
| Samsung Engineering Co. Ltd. | No | Removed from Iran CE List |
| Samsung Heavy Industries Co. Ltd. | No | Removed from Iran List |
| Sasol Ltd. | Yes; May 25, 2010<br>September 29, 2010 | Iran CE Classification Continues |
| Seadrill Management AS | Yes; September 20, 2010 | Sudan CE Classification Continues |
| Siam Cement Group (SCG) | Yes; September 24, 2010 | Iran CE Classification Continues |
| Siemens AG | Yes; October 22, 2009<br>October 8, 2010 | Removed from Iran CE List |
| Schlumberger Limited NV | Yes; October 19, 2007 | Removed from Iran and Sudan Lists |
| Siam Cement PCL | Yes; October 21, 2008 | Iran CE Classification Continues |
| SNC - Lavalin Group Inc. | Yes; September 25, 2007 | Removed from Iran List |
| Sudan Telecommunications (Sudatel) | No | Sudan CE Classification Continues |
| Technip | Yes; April 30, 2010 and<br>November 30, 2010 | Iran CE Classification Continues |
| The Weir Group PLC | Yes; November 16, 2007 | Removed from Iran and Sudan Lists |
| Total SA | Yes; October 12, 2007 | Sudan CE Classification Continues |
| Trevi-Finanziaria Industriale S.p.A. | Yes; September 17, 2010 | Removed from Iran CE List |
| Weatherford International, Ltd. | No | Removed from Sudan List |
| Welspun Corp. Limited<br>(fka Welspun-Gujarat Stahl Rohen Ltd.) | Yes; September 24, 2010 | Iran CE Classification Continues |

## *Key Dates for PFIA Activities*

**June 8, 2007 —** Legislation's effective date, upon becoming a law.

**August 6, 2007 —** SBA letter to state agencies requesting data on all publicly traded securities held directly by the State.

**August 20, 2007 —** First of two letters to investment managers providing written notice of PFIA enactment and amendment to Schedule B of investment management contracts.

**September 19, 2007 —** SBA assembles initial Scrutinized Companies lists for Sudan and Iran.

**September 20, 2007 —** SBA engages companies classified as either Scrutinized or needing Continued Examination through written correspondence, subsequent conference calls and additional communication. SBA disclosed the Scrutinized Companies lists on its website, including reporting of all equities held by the State.

**September 21, 2007 —** Second of two letters to investment managers providing Scrutinized Companies lists.

**October 16, 2007 —** SBA formally submits the Scrutinized Companies lists to the Legislature and the United States Special Envoy to Sudan, and continues to do so every quarter.

**November 30, 2007 —** SBA sends notification via email to any owned scrutinized company that has not responded to initial written correspondence. Similar notification was sent to each company classified as needing continued examination.

**January 25, 2008** — SBA sends additional notice of divestment and request for information to all Scrutinized Companies, with emphasis to companies that have been unresponsive to the SBA's prior request for the necessary information.

**July 1, 2008** — In March 2008, the SBA developed a policy approach directing all affected managers to sell their remaining PFIA related holdings no later than July 1, 2008, approximately three months earlier than the statutory deadline of September 18, 2008.

**September 18, 2008 —** Statutory deadline for the SBA to complete divestment of *initial* Scrutinized Companies (i.e., within 12 months of their initial appearance on the September 19, 2007 list), if they do not stop scrutinized active business operations.

**March 1, 2010**— Deadline for the SBA to identify and offer at least one terror-free investment product for the FRS Investment Plan (Defined Contribution).

**Quarterly Reporting**—SBA provides quarterly updates to the Scrutinized Companies lists for Sudan and Iran, including a summary of engagement activities. PFIA quarterly reports have been issued on the following dates:

**September 19, 2007**
**December 18, 2007**
**March 25, 2008**
**June 10, 2008**
**September 16, 2008**
**January 13, 2009**
**April 14, 2009**
**July 28, 2009**
**October 27, 2009**
**January 26, 2010**
**April 27, 2010**
**July 29, 2010**
**November 9, 2010**
**February 22, 2011**
**June 16, 2011**
**September 20, 2011**
**December 6, 2011**
**March 20, 2012**

## *Summary of Investments Sold, Redeemed, Divested or Withdrawn*

In accordance with the PFIA, the SBA must divest all holdings of any scrutinized companies within 12 months of their original appearance on the prohibited securities list. External managers are contractually responsible for administering investments in accordance with restrictions set forth by the SBA, including the prohibited securities list of the PFIA. Beginning in April 2008, the SBA developed a policy approach that directed all affected managers to sell their remaining PFIA related holdings no later than July 1, 2008, approximately three months earlier than the statutory deadline of September 18, 2008. Historical divestment transaction data is contained in prior PFIA Quarterly Reports.

Below is a table showing the aggregate amounts divested by the SBA, by company, since the PFIA's inception:

| | |
|---|---|
| Royal Dutch Shell** | $215,784,700.79 |
| Total SA | $214,536,015.45 |
| Petroleo Brasileiro SA (Petrobras) ** | $206,135,264.10 |
| ENI | $141,403,034.78 |
| Gazprom (a.k.a. OAO Gazprom) | $71,275,453.14 |
| Alstom** | $65,897,698.67 |
| Repsol YPF** | $53,420,179.87 |
| Statoil ASA** (fka: StatoilHydro) | $46,792,677.58 |
| CNOOC Ltd | $45,168,239.86 |
| China Petroleum and Chemical Corp (CPCC) Sinopec | $38,455,440.48 |
| PetroChina | $25,723,158.75 |
| Inpex Corp.** | $24,835,110.63 |
| MISC Bhd | $16,448,397.44 |
| Snam Rete Gas | $9,596,905.78 |
| Lukoil OAO** | $9,487,631.46 |
| OMV AG ** | $8,601,977.98 |
| Shell International Finance** | $8,599,813.40 |
| Wärtsilä Oyj** | $1,797,871.96 |
| Daelim Industrial Co Ltd | $1,566,926.73 |
| Petrofac Ltd ** | $1,496,881.43 |
| The Weir Group PLC ** | $1,322,666.62 |
| Petrobras International Finance** | $1,148,750.00 |
| Lundin Petroleum AB ** | $1,133,120.04 |
| Oil & Natural Gas Corporation (ONGC) | $945,363.83 |
| Petrobras Energia (Participaciones) ** | $298,632.08 |
| Dongfeng Motor Group | $158,623.49 |
| Electricity Generating Public Company | $121,321.38 |
| Gazprom Neft | $37,892.73 |
| ** denotes companies no longer on the Prohibited Company list. | **1,212,189,750.45** |

In accordance with the PFIA, the SBA will report on the performance implications of PFIA-related divestitures and restrictions. Generally, the impact of PFIA legislation on performance is measured as the opportunity cost of not being able to hold prohibited securities, measured by comparing the monthly return of the standard foreign equity benchmark (i.e., the MSCI ACWI ex-US) to a custom foreign equity benchmark based upon PFIA divestiture requirements. The difference in returns between the standard benchmark and custom benchmark represents the opportunity cost to the SBA of not being able to invest in (or hold) prohibited companies. The percent return difference is then applied to the average monthly balance of foreign equity investments to determine a dollar impact. Monthly dollar impacts, whether positive or negative, are added together through time and then compared to the total value of the FRS Pension Plan to determine the percentage or basis point impact of PFIA legislation.

### *Table 7: List of Prohibited Investments (Scrutinized Companies)*

***New companies on the list are shaded and in bold.***

| Company | Scrutinized Country | Country of Incorporation | Initial Appearance on Scrutinized List | Full Divestment |
|---|---|---|---|---|
| AREF Energy Holdings Co. | Sudan | Kuwait | July 28, 2009 | Yes |
| AviChina Industry & Technology Company Limited | Sudan | China | September 19, 2007 | Yes |
| Chennai Petroleum Corp Ltd | Sudan | India | September 19, 2007 | Yes |
| China Petroleum & Chemical Corp (CPCC) Sinopec | Sudan & Iran | China | September 19, 2007 | Yes |
| China Oilfield Services Ltd | Iran | China | June 16, 2011 | Yes |
| China Petroleum Finance Co. | Sudan | China | November 9, 2010 | Yes |
| CNOOC Ltd | Iran | China | June 16, 2011 | By June 15, 2012 |
| CNPC HK Overseas Capital Ltd | Sudan & Iran | China | June 16, 2011 | Yes |
| Daelim Industrial Co Ltd | Iran | South Korea | June 16, 2011 | Yes |
| Daqing Huake Group Co Ltd | Sudan | China | March 25, 2008 | Yes |
| Dongfeng Motor Group Co. Ltd. | Sudan | China | July 29, 2010 | Yes |
| Egypt Kuwait Holding Co. SAE | Sudan | Kuwait | January 13, 2009 | Yes |
| Electricity Generating Public Co | Sudan | Thailand | September 19, 2007 | Yes |
| ENI | Iran | Italy | September 19, 2007 | Yes |
| Gas District Cooling (Putrajaya) Sdn Bhd | Sudan & Iran | Malaysia | April 14, 2009 | Yes |
| Gazprom | Iran | Russia | September 19, 2007 | Yes |
| Gazprom Neft | Iran | Russia | September 16, 2008 | Yes |
| Groupe ONA (ONA SA) | Sudan | Morocco | November 9, 2010 | Yes |
| Harbin Electric Co. Ltd. (fka: Harbin Power Equipment) | Sudan | China | September 19, 2007 | Yes |
| Indian Oil Corp Ltd (IOCL) | Sudan & Iran | India | September 19, 2007 | Yes |
| Jiangxi Hongdu Aviation (aka Hongdu Aviation) | Sudan | China | September 19, 2007 | Yes |
| Jinan Diesel Engine | Sudan | China | July 28, 2009 | Yes |
| Kingdream PLC | Sudan & Iran | China | April 14, 2009 | Yes |
| KLCC Property Holdings Bhd | Sudan & Iran | Malaysia | April 14, 2009 | Yes |
| KMCOB Capital Bhd | Sudan | Malaysia | September 19, 2007 | Yes |
| Kunlun Energy Company Ltd. (fka: CNPC Hong Kong) | Sudan & Iran | Hong Kong | September 19, 2007 | Yes |
| Kuwait Finance House | Sudan | Kuwait | April 14, 2009 | Yes |
| Lanka IOC Ltd | Sudan | India | September 19, 2007 | Yes |
| LS Industrial Systems | Sudan | South Korea | September 20, 2011 | Yes |
| Managem SA | Sudan | Morocco | November 9, 2010 | Yes |
| Mangalore Refinery & Petrochemicals Ltd | Sudan | India | September 19, 2007 | Yes |
| Maire Tecnimont | Iran | Italy | December 6, 2011 | Yes |
| Midciti Resources Sdn Bhd | Sudan | Malaysia | September 19, 2007 | Yes |
| MISC Bhd | Sudan & Iran | Malaysia | September 19, 2007 | Yes |
| MISC Capital Ltd. | Sudan & Iran | Malaysia | April 14, 2009 | Yes |
| Mosenergo | Iran | Russia | September 16, 2008 | Yes |
| Oil & Natural Gas Corp (ONGC) | Sudan & Iran | India | September 19, 2007 | Yes |
| PetroChina | Sudan & Iran | China | September 19, 2007 | Yes |
| Petroliam Nasional (Petronas) | Sudan & Iran | Malaysia | September 19, 2007 | Yes |
| Petronas Capital Limited | Sudan & Iran | Malaysia | September 19, 2007 | Yes |
| Petronas Chemicals Bhd | Sudan & Iran | Malaysia | June 16, 2011 | Yes |

| Company | Scrutinized Country | Country of Incorporation | Initial Appearance on Scrutinized List | Full Divestment |
|---|---|---|---|---|
| Petronas Dagangan Bhd | Sudan & Iran | Malaysia | September 19, 2007 | Yes |
| Petronas Gas Berhad | Sudan & Iran | Malaysia | September 19, 2007 | Yes |
| Ranhill Bhd | Sudan | Malaysia | September 16, 2008 | Yes |
| Ranhill Power Sdn Bhd | Sudan | Malaysia | September 20, 2011 | Yes |
| Ranhill Powertron Sdn | Sudan | Malaysia | April 14, 2009 | Yes |
| **Rosier SA** | **Iran** | **Belgium** | **March 20, 2012** | **Yes** |
| Scomi Engineering BHD | Sudan | Malaysia | September 19, 2007 | Yes |
| Scomi Group Bhd | Sudan | Malaysia | September 19, 2007 | Yes |
| Sinopec Finance | Sudan & Iran | China | April 14, 2009 | Yes |
| Sinopec Kantons Holdings Ltd | Sudan & Iran | Bermuda | September 19, 2007 | Yes |
| Sinopec Shanghai Petrochemical | Sudan & Iran | China | September 19, 2007 | Yes |
| Sinopec Yizheng Chemical Fibre | Sudan & Iran | China | March 25, 2008 | Yes |
| Snam Rete Gas | Iran | Italy | September 19, 2007 | Yes |
| Societe Metallurgique D'imiter | Sudan | Morocco | November 9, 2010 | Yes |
| Total Capital | Iran | France | November 9, 2010 | Yes |
| Total Gabon | Iran | Gabon | November 9, 2010 | Yes |
| **Total Kenya Ltd** | **Iran** | **Kenya** | **March 20, 2012** | **Yes** |
| Total (Nigeria) PLC | Iran | Nigeria | March 25, 2008 | Yes |
| Total SA | Iran | France | September 19, 2007 | Yes |
| **# of Prohibited Investments** | **60** | **-** | **-** | |

The following companies were **removed** from the Prohibited Investments List during the quarter.

| *Removed Company* | *Country of Incorporation* |
|---|---|
| ***Dongan Motor (aka Harbin Dongan Auto Engine)*** | ***China*** |
| ***Hafei Aviation Industry Co Ltd*** | ***China*** |
| **KEPCO Plant Service & Engineering Co Ltd** | ***South Korea*** |
| **Korea Electric Power (KEPCO)** | ***South Korea*** |
| **Korea Plant Service & Engineering** | ***South Korea*** |

### *Table 8: SBA Holdings in Prohibited Investments Subject to Divestment*

[As of the January 31, 2012 PFIA Compliance Review]

The SBA currently has holdings in one company on the Prohibited Investments List in accounts subject to the PFIA divestiture requirements. CNOOC Ltd. was added to the Prohibited Investments List on June 16, 2011, and is subject to full divestment no later than June 15, 2012.

| Issuer | Shares | Market Value |
|---|---|---|
| CNOOC Ltd. | 27,979,480 | $87,309,024.50 |

SBA holdings in the following company have been divested since the previous PFIA Quarterly Report.

| Date | Company | Action | Shares | Proceeds | Account Name |
|---|---|---|---|---|---|
| 12/13/11 | CNOOC Ltd. | Sold | 3,436,000 | 49,894,967.43 HKD | FRSFN1050502 |
| 1/10/12 | CNOOC Ltd. | Sold | 3,200,000 | 48,585,120.03 HKD | FRSFN1030602 |

### *Summary of Progress, SBA Investment Manager Engagement Efforts*

On August 20, 2007, the SBA sent letters to 66 external investment managers notifying them of the Act and informing them of new contract language that would enforce their cooperation with the requirements of the new law.

On September 19, 2007, the SBA sent letters to all affected managers outlining the list of prohibited securities for any future purchases. The letter described the SBA's engagement process with companies on the list, which affords companies a 90-day period in which to comply with the conditions of the law or clarify their activities. The letter directed these managers to cease purchase of securities on the list and to await the direction of the SBA for any divestment necessary in the event engagement fails, with a deadline for divestment under the law of September 18, 2008.

On September 19, 2007, the SBA sent letters to actively-managed, indirectly held funds holding scrutinized securities, including managers of the defined contribution program, asking the funds to review the list of scrutinized securities and consider eliminating such holdings from the portfolio or create a similar fund, devoid of such holdings, per the requirements of the law.

Each quarter, the SBA sends written and electronic notification to all affected managers about the list of prohibited companies.

The SBA has received responses noting our concerns in writing and by phone from several of the contacted managers.

### *Listing of All Publicly Traded Securities (Including Equity Investments)*

Due to the large number of individual securities and the volume of information, this list has been electronically posted to the SBA's website and is updated quarterly. A list of all publicly traded securities owned by the State of Florida can be found within the PFIA information section of the SBA's website. Please observe the electronic report's notes page for important clarifying explanations of included data.

For more information, please contact:

Florida State Board of Administration (SBA)
Investment Programs & Governance
1801 Hermitage Blvd., Suite 100
Tallahassee, FL 32308
www.sbafla.com

or send an email to:
pfia@sbafla.com

SBA FLORIDA
www.sbafla.com

End of Section

**STATE BOARD OF ADMINISTRATION OF FLORIDA**

**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**
**(850) 488-4406**

**POST OFFICE BOX 13300**
**32317-3300**

**RICK SCOTT**
**GOVERNOR**
**AS CHAIRMAN**

**JEFF ATWATER**
**CHIEF FINANCIAL OFFICER**
**AS TREASURER**

**PAM BONDI**
**ATTORNEY GENERAL**
**AS SECRETARY**

**ASH WILLIAMS**
**EXECUTIVE DIRECTOR & CIO**

March 20, 2012

Honorable Debbie Mayfield
Alternating Chair
Joint Legislative Auditing Committee
317 House Office Bldg.
402 S. Monroe Street
Tallahassee, Florida 32399

Honorable Jim Norman
Alternating Chair
Joint Legislative Auditing Committee
214 Senate Office Bldg.
404 S. Monroe Street
Tallahassee, Florida 32399

Dear Representative Mayfield and Senator Norman:

Section 218.409(9), Florida Statutes, requires the Trustees to report to the Joint Legislative Auditing Committee that they have reviewed the Auditor General's annual Financial Audit of the Local Government Surplus Funds Trust Fund (now known as Florida PRIME). The fund's Financial Audit for the fiscal years 2010 and 2011 was completed in December 2011. The Trustees are also required to certify that any necessary item(s) are being addressed by corrective action by the State Board of Administration (SBA). I am pleased to report there was no corrective action recommended by the audit.

Please contact me if you have any questions.

Sincerely,

Ashbel C. Williams
Executive Director & CIO

ACW/db
Attachments
cc: Honorable Larry Ahern
Honorable Daphne Campbell
Honorable Jeff Clemens
Honorable Bryan Nelson
Honorable Kenneth Roberson
Honorable Arthenia Joyner
Honorable Evelyn Lynn
Honorable Maria Lorts Sachs
Honorable Stephen Wise
Ms. Kathy Dubose, Director

DRAFT

REPORT NO. 2012-066
DECEMBER 2011

# STATE OF FLORIDA

# STATE BOARD OF ADMINISTRATION

# LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (AN EXTERNAL INVESTMENT POOL)

## Financial Audit

For the Fiscal Years Ended
June 30, 2011 and 2010

STATE OF FLORIDA
AUDITOR GENERAL
DAVID W. MARTIN, CPA

## STATE BOARD OF ADMINISTRATION

The State Board of Administration's Board of Trustees is composed of the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary. The Trustees delegate administrative and investment authority to an appointed Executive Director. Mr. Ashbel Williams served as Executive Director during the audit period.

The Auditor General conducts audits of governmental entities to provide the Legislature, Florida's citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

The audit team leader was Allen G. Weiner, CPA, and the audit was supervised by Kathryn D. Walker, CPA. Please address inquiries regarding this report to Kathryn D. Walker, CPA, Audit Manager, by e-mail at kathrynwalker@aud.state.fl.us or by telephone at (850) 487-9085.

This report and other reports prepared by the Auditor General can be obtained on our Web site at www.myflorida.com/audgen; by telephone at (850) 487-9175; or by mail at G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450.

STATE BOARD OF ADMINISTRATION
LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (FLORIDA PRIME)

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# EXECUTIVE SUMMARY

## Summary of Report on Financial Statements

**Our audit disclosed that the financial statements prepared by the State Board of Administration (SBA) present fairly, in all material respects, the net assets of the Local Government Surplus Funds Trust Fund (Florida PRIME) and the changes in net assets thereof in accordance with prescribed financial reporting standards.**

## Summary of Report on Internal Control and Compliance

**Our audit did not disclose any deficiencies in internal control over Florida PRIME's financial reporting that we consider to be material weaknesses.**

**The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* issued by the Comptroller General of the United States.**

## Audit Objectives and Scope

**Our audit objectives were to determine whether the SBA had:**

- **Presented Florida PRIME's basic financial statements in accordance with generally accepted accounting principles;**
- **Established and implemented internal control over financial reporting and compliance with requirements that could have a direct and material effect on the financial statements;**
- **Complied with the various provisions of laws, rules, regulations, and contracts that are material to the financial statements;**

**The scope of this audit included an examination of Florida PRIME's basic financial statements as of and for the fiscal years ended June 30, 2011, and 2010. We obtained an understanding of SBA's environment, including its internal control, and assessed the risk of material misstatement necessary to plan the audit of the basic financial statements. We also examined various transactions to determine whether they were executed, both in manner and substance, in accordance with governing provisions of laws, rules, regulations, contracts, and Florida PRIME's investment policy.**

## Audit Methodology

**The methodology used in this report included the examination of pertinent SBA records in connection with the application of procedures required by auditing standards generally accepted in the United States of America and applicable standards contained in *Government Auditing Standards* issued by the Comptroller General of the United States.**

# AUDITOR GENERAL
## STATE OF FLORIDA

G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

DAVID W. MARTIN, CPA
AUDITOR GENERAL

PHONE: 850-488-5534
FAX: 850-488-6975

The President of the Senate, the Speaker of the
House of Representatives, and the
Legislative Auditing Committee

**INDEPENDENT AUDITOR'S**
**REPORT ON FINANCIAL STATEMENTS**

We have audited the accompanying financial statements of the State Board of Administration's (SBA) Local Government Surplus Funds Trust Fund (Florida PRIME), as of and for the fiscal years ended June 30, 2011, and 2010, as listed in the table of contents. These financial statements are the responsibility of SBA's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the net assets and changes in net assets of Florida PRIME and do not purport to, and do not, present fairly the operations of the State of Florida as of June 30, 2011, and 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of Florida PRIME as of June 30, 2011, and 2010, and the changes in its net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report on our consideration of SBA's internal control over financial reporting relating to Florida PRIME and on our tests of its compliance with certain provisions of laws, rules, regulations, contracts, and other matters included under the heading **INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that **MANAGEMENT'S DISCUSSION AND ANALYSIS** on pages 3 through 5 be presented to supplement the basic financial statements. Such information, although not a required part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Respectfully submitted,

David W. Martin, CPA
December 21, 2011

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## FISCAL YEARS ENDED JUNE 30, 2011, AND JUNE 30, 2010

The State Board of Administration (SBA) is responsible for the management of the Local Government Surplus Funds Trust Fund (Florida PRIME).[1] The SBA was established on June 21, 1929, pursuant to Chapter 14486, Laws of Florida (1929). The SBA was subsequently created as a constitutional body corporate on January 1, 1943, by Article IX, Section 16 of the State Constitution of 1885, as amended. The SBA was subsequently continued as a body corporate by Article IV, Section 4(e) of the State Constitution (1968), as amended. The SBA is composed of the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary.

As management of the SBA, we offer readers of Florida PRIME's financial statements this overview and analysis of Florida PRIME's financial results and position for the fiscal years ended June 30, 2011 and 2010. We encourage readers to consider the information presented here in conjunction with the financial statements and notes to the financial statements, which begin on page 6.

## OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements provide financial information about Florida PRIME as an investment trust fund, a fiduciary fund type. Investment trust funds are accounted for using an economic resources measurement focus and the accrual basis of accounting. Earnings on investments are recognized as revenue when earned, and expenses are recorded when a liability is incurred.

Florida PRIME presents the following basic financial statements: a Statement of Net Assets and a Statement of Changes in Net Assets. The Statement of Net Assets presents all Florida PRIME's assets and liabilities with the difference reported as net assets. The Statement of Changes in Net Assets shows the increase or decrease in net assets during the year as a result of investment activities and participant contributions and withdrawals.

## FINANCIAL SUMMARY

A summary comparison of Florida PRIME's Statement of Net Assets at June 30, 2011, and the prior fiscal years at June 30, 2010, and 2009, is presented below (in thousands):

| | At June 30, | | |
|---|---|---|---|
| | 2011 | 2010 | 2009 |
| Total assets | $ 6,824,328 | $ 5,483,034 | $ 5,997,756 |
| Total liabilities | 406 | 2,098 | 13,462 |
| Net assets held in trust for pool participants | $ 6,823,922 | $ 5,480,936 | $ 5,984,294 |

[1] As of August 3, 2009, SBA began using the name "Florida PRIME" when referring to the Local Government Surplus Fund Trust Fund.

A summary comparison of Florida PRIME's Statement of Changes in Net Assets for the current fiscal year ended June 30, 2011, and the prior fiscal years ended June 30, 2010, and 2009, is presented below (in thousands):

| | Year Ended June 30, | | |
|---|---|---|---|
| | 2011 | 2010 | 2009 |
| Increase (decrease) in net assets: | | | |
| Net income from investing activity | $ 17,771 | $ 16,269 | $ 88,429 |
| Redemption fees | …… | …… | 1 |
| Distributions paid and payable | (17,771) | (16,269) | (88,429) |
| Participant contributions | 15,223,064 | 12,653,338 | 9,363,390 |
| Participant withdrawals | (13,968,553) | (13,278,921) | (10,581,058) |
| Investment transfer from Fund B | 88,475 | 122,225 | 138,150 |
| Total increase (decrease) in net assets | 1,342,986 | (503,358) | (1,079,517) |
| Net assets, July 1 | 5,480,936 | 5,984,294 | 7,063,811 |
| Net assets, June 30 | $ 6,823,922 | $ 5,480,936 | $ 5,984,294 |

## FINANCIAL ANALYSIS

### Assets

Total assets increased by $1.3 billion from $5.5 billion at June 30, 2010, to $6.8 billion at June 30, 2011. At the end of fiscal year 2010, total assets were $500 million less than the $6 billion at the end of fiscal year 2009. The increase in total assets in the fiscal year ended June 30, 2011, was due primarily to the fact that participant contributions exceeded participant withdrawals. The decrease in total assets during the fiscal year ended June 30, 2010, was mainly the result of participant withdrawals exceeding participant contributions.

### Liabilities

Total liabilities at June 30, 2011, were $400 thousand, which was $1.7 million lower than the total liabilities of $2.1 million at June 30, 2010. The total liabilities at June 30, 2010, were $11.4 million lower than the June 30, 2009, amount of $13.5 million. The main reason for the decrease in the fiscal years ended June 30, 2011, and June 30, 2010, was a decrease in "Due to local governments" due to a decline in unregistered deposits (deposits sent without prior notification to the SBA). Deposits sent in without being registered by participants are recorded as liabilities until the depositor is identified and credit is awarded to the participant.

### Change in Net Assets

Net assets increased by $1.3 billion from June 30, 2010, to June 30, 2011. Net assets at June 30, 2011, 2010, and 2009 were $6.8 billion, $5.5 billion, and $5.98 billion, respectively. The main reasons for the increase (in the fiscal year ended 2011) and decrease (in the fiscal year ended 2010) in net assets were participant contributions and withdrawals.

Net income from investing activity for the current fiscal year ended June 30, 2011, was $1.5 million higher than the $16.3 million reported for the fiscal year ended June 30, 2010. Most of the increase in the current fiscal year was the result of higher average participant balances during the period. Net income from investing activity for the fiscal year

ended June 30, 2010, was $72.1 million lower than the $88.4 million reported for fiscal year 2009 because of diminished average participant balances and depressed yields on short-term fixed income investments. The Federal Reserve continued a monetary policy stance (that began in the latter part of the 2009 fiscal year) to keep overnight interest rates to nearly zero in an effort to help stabilize global financial markets. As a result of this policy, other Federal government economic stimulus measures, and slow economic growth, short-term interest rates remained low.

## FINANCIAL HIGHLIGHTS

The purpose of Chapter 218, Part IV, Florida Statutes, is to promote, through State assistance, the maximization of net interest earnings on invested surplus funds of units of local government, based on the principles of investor protection, mandated transparency, and proper governance, with the goal of reducing the need for imposing additional taxes. The primary investment objectives, in priority order, are safety, liquidity, and competitive returns with minimization of risks.

For the fiscal year ended June 30, 2011:

- Participant contributions increased 20 percent over the prior fiscal year, while participant withdrawals increased only 5 percent, resulting in net participant contributions of $1.25 billion.
- Net income from investing activity increased $1.5 million over the prior fiscal year; however, the average participant yield for the fiscal year was .29 percent, the same average yield as the prior fiscal year. The increase in net income from investing activity is due to the higher average participant balances, as interest rates stayed at historic lows during the fiscal year.

For the fiscal year ended June 30, 2010:

- Participant withdrawals increased 25 percent (to $13.3 billion) over the prior fiscal year, while participant contributions increased 35 percent (to $12.7 billion), resulting in net participant withdrawals of $626 million.
- Net income from investing activity decreased $72 million over the prior fiscal year because of diminished average participant balances and depressed yields on short-term fixed income investments.

## CONTACT INFORMATION

These financial statements reflect only the transactions and balances for Florida PRIME. For additional information on this fund, please contact the State Board of Administration, Chief Operating & Financial Officer, 1801 Hermitage Boulevard, Suite 100, Tallahassee, Florida 32308 or visit SBA's website at https://www.sbafla.com/prime/.

## BASIC FINANCIAL STATEMENTS

### STATE BOARD OF ADMINISTRATION
### LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (FLORIDA PRIME)
### STATEMENTS OF NET ASSETS

**As of June 30, 2011, and June 30, 2010**
**(In Thousands)**

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | $ 215 | $ 1,945 |
| Investments: | | |
| Certificates of deposit, negotiable | 2,732,517 | 1,425,500 |
| Commercial paper | 1,977,209 | 1,888,948 |
| Money market funds | 530,210 | 512,266 |
| Domestic corporate bonds and notes | 23,295 | 187,773 |
| Municipal bonds and notes | 12,700 | …… |
| Foreign corporate note | 45,000 | 75,000 |
| Federal agencies | …… | 444,994 |
| U.S. Treasury notes | 30,056 | …… |
| Repurchase agreements | 1,470,000 | 945,000 |
| Total investments | 6,820,987 | 5,479,481 |
| Interest receivable | 3,106 | 1,588 |
| Prepaid fees | 19 | 19 |
| Undistributed expenses | 1 | 1 |
| **Total Assets** | 6,824,328 | 5,483,034 |
| **Liabilities** | | |
| Accounts payable and accrued liabilities | 136 | 102 |
| Distributions payable | 55 | 51 |
| Due to local governments | 215 | 1,945 |
| **Total Liabilities** | 406 | 2,098 |
| **Net Assets** | | |
| Held in trust for pool participants | $ 6,823,922 | $ 5,480,936 |

The notes to the financial statements are an integral part of this statement.

## STATE BOARD OF ADMINISTRATION
## LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (FLORIDA PRIME)
## STATEMENTS OF CHANGES IN NET ASSETS

**Fiscal years ended June 30, 2011, and June 30, 2010**
**(In Thousands)**

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **Additions** | | |
| Investment operations: | | |
| Income from investing activity: | | |
| Interest income | $ 19,314 | $ 17,768 |
| Bank fees | (63) | (58) |
| Compliance review fees | (62) | (39) |
| Standard and Poor's rating maintenance fees | (38) | (19) |
| Investment management fees | (1,002) | (1,038) |
| Administrative service charges | (378) | (345) |
| Net income from investing activity | 17,771 | 16,269 |
| **Total Additions** | 17,771 | 16,269 |
| **Deductions** | | |
| Distributions paid and payable | 17,771 | 16,269 |
| **Total Deductions** | 17,771 | 16,269 |
| **Share Transactions** | | |
| Participant contributions | 15,223,064 | 12,653,338 |
| Participant withdrawals | (13,968,553) | (13,278,921) |
| Transfer from Fund B | 88,475 | 122,225 |
| **Net Increase (Decrease) Resulting from Share Transactions** | 1,342,986 | (503,358) |
| Total increase (decrease) in net assets | 1,342,986 | (503,358) |
| Net assets, beginning of year | 5,480,936 | 5,984,294 |
| Net assets, end of year | $ 6,823,922 | $ 5,480,936 |

The notes to the financial statements are an integral part of this statement.

## NOTES TO FINANCIAL STATEMENTS

**STATE BOARD OF ADMINISTRATION**
**LOCAL GOVERNMENT SURPLUS FUNDS TRUST FUND (FLORIDA PRIME)**
**Fiscal years ended June 30, 2011, and June 30, 2010**

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following summary of the Local Government Surplus Funds Trust Fund's (Florida PRIME's) significant accounting policies is presented to assist the reader in interpreting the financial statements. These policies should be viewed as an integral part of the accompanying financial statements.

#### a. Reporting Entity

The State Board of Administration (SBA) is responsible for the management of Florida PRIME. The SBA was established on June 21, 1929, pursuant to Chapter 14486, Laws of Florida (1929). The SBA was subsequently created as a constitutional body corporate on January 1, 1943, by Article IX, Section 16 of the State Constitution of 1885, as amended. The SBA was subsequently continued as a body corporate by Article IV, Section 4(e) of the State Constitution (1968), as amended. The SBA is composed of the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary.

The Local Government Surplus Funds Trust Fund was created by act of Florida Legislature effective October 1, 1977, (Chapter 218, Part IV, Florida Statutes). The law allowed SBA to manage investments on an individual basis or to establish a pooled account. The funds were managed on an individual basis until January 1, 1982. On August 3, 2009, the SBA began using "Florida PRIME" when referring to the Local Government Surplus Funds Trust Fund.

Sections 218.40 through 218.415, Florida Statutes, and State Board of Administration Rules 19-7.001 through 19-7.017, Florida Administrative Code, promulgated pursuant to Section 218.405(4), Florida Statutes, govern the operation of Florida PRIME.

The assets and liabilities of Florida PRIME are included in the Comprehensive Annual Financial Report (CAFR) of the State of Florida. However, the accompanying financial statements present only Florida PRIME and are not intended to present fairly the financial position of the State of Florida and the results of its operations in conformity with generally accepted accounting principles.

#### b. Regulatory Oversight

Florida PRIME is not a registrant with the Securities and Exchange Commission (SEC); however, SBA has adopted operating procedures consistent with those required of an SEC 2a-7-like fund. A 2a-7-like external investment pool is one that is not registered with the SEC as an investment company, but

nevertheless has a policy that it will, and does, operate in a manner consistent with SEC Rule 2a-7, which governs the operation of SEC regulated money market funds.

### c. Basis of Presentation

These financial statements have been prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and reporting principles.

Florida PRIME is reported as an investment trust fund, a fiduciary fund type.

### d. Measurement Focus and Basis of Accounting

Basis of accounting refers to when the recognition of revenues and expenses and the related assets and liabilities are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied. The accompanying financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with GAAP. Under this method, earnings on investments, including interest income, are recognized as revenue when earned, and expenses are recognized when a liability is incurred.

### e. Cash and Cash Equivalents

Florida PRIME reports as "Cash and cash equivalents" all cash on hand and on deposit in banks, including demand deposits, time deposits, and non-negotiable certificates of deposit.

### f. Investments

Florida PRIME's investments are recorded at amortized cost, consistent with GASB Statement Number 31. Fair values, for note disclosures, are calculated using quoted market prices. If quoted market prices are not available, the discounted cash flow model and broker quotes are used to price securities.

### g. Method Used to Determine Participants' Shares Sold and Redeemed

In a manner similar to that used for SEC Rule 2a-7 money market funds, participants' shares are sold and redeemed in Florida PRIME using the amortized cost method, which is consistent with the method used to report Florida PRIME's investments. The amortized cost method calculates an investment's value by adjusting its acquisition cost for the accretion of discount or amortization of premium over the period from purchase to maturity.

### h. Legally Binding Guarantees

The SBA has not provided or obtained any legally binding guarantees during the fiscal years ended June 30, 2011, and June 30, 2010, for Florida PRIME.

### i. Involuntary Participation

There is no requirement under Florida Statutes for any local government or state agency to participate in Florida PRIME.

### j. Frequency of Determining Fair Value of Shares

The fair value of the investments of Florida PRIME is determined on a daily basis. SEC Rule 2a-7 requires that a periodic comparison be made between amortized cost and market value and that specific actions be taken if the two values differ by more than .50 percent. As of June 30, 2011, and June 30, 2010, the ratios of fair value to amortized cost were 100.01 percent and 99.994 percent, respectively.

### k. Fees and Administrative Service Charges

Federated Investment Counseling (Federated) is the investment manager for Florida PRIME. Federated charges an annual investment management fee based on the average daily net assets (i.e., average daily amortized cost) of Florida PRIME (excluding Federated money market fund balances), as follows:

| | |
|---|---|
| First $1 billion in Account Assets | 3.5 basis points |
| Next $1.5 billion in Account Assets | 3.0 basis points |
| Next $2.5 billion in Account Assets | 2.5 basis points |
| Balance of Account Assets over $5 billion | 2.0 basis points |

This fee is taken out of monthly earnings prior to the allocation of net earnings to participant balances. Total investment management fees incurred by Florida PRIME in the fiscal years ended June 30, 2011, and June 30, 2010, were $1,002,239 and $1,038,212, respectively.

In addition, SBA charges a .6 basis point charge (.00006) on total Florida PRIME assets to cover the SBA's administrative costs of the fund. These charges are taken out of the monthly earnings prior to the distribution of net earnings to participant balances each month. Total administrative service charges incurred by Florida PRIME for the fiscal year ended June 30, 2011, were $377,879 and for June 30, 2010, were $344,852.

Various bank fees, including transaction charges, custody fees, and performance analytics fees are incurred by Florida PRIME. These fees are taken out of the monthly earnings prior to the distribution of net earnings to participant balances each month. The total bank fees incurred by Florida Prime for the fiscal year ended June 30, 2011 were $62,541 and for June 30, 2010 were $58,321. Standard and

Poor's (S&P) rating maintenance fees were $38,000 and $18,844 for fiscal years ending June 30, 2011, and 2010, respectively. Compliance review fees were $62,181 and $38,694 for those same years. The compliance review service fees resulted from the provisions of Section 218.405(3), Florida Statutes, which require that the trustees annually certify to the Joint Legislative Auditing Committee that Florida PRIME is in compliance with Florida law.

### *I. Fund B Surplus Funds Trust Fund*

Pursuant to Section 218.417, Florida Statutes, the Fund B Surplus Funds Trust Fund (Fund B) was created in May 2008. Amounts credited to Fund B consist of the investments, interest earned, and reserve in Fund B of Florida PRIME. Fund B of Florida PRIME was originally formed as part of a restructuring of the Local Government Surplus Funds Trust Fund in December 2007 to hold certain securities with limited liquidity.

Fund B is administered by SBA and SBA distributes cash holdings to Florida PRIME as they become available from maturities, sales, investment interest, and other income received from assets in Fund B. These distributions are recorded on the Statement of Changes in Net Assets as a Transfer from Fund B.

## *2. DEPOSITS AND INVESTMENTS*

### *a. Deposits*

Cash is held in demand deposits at various financial institutions. These deposits totaled $215,499 at June 30, 2011, and $1,945,336 at June 30, 2010. All deposits in Florida PRIME were covered by Federal insurance or the State's collateral pool pursuant to Chapter 280, Florida Statutes. Chapter 280, Florida Statutes, generally requires public funds to be deposited in a bank or savings association designated by the State of Florida Chief Financial Officer (State CFO) as authorized to receive deposits in the State and that meets the collateral requirements as set forth in Chapter 280, Florida Statutes.

The State CFO determines the collateral requirements and collateral pledging level for each Qualified Public Depository following guidelines outlined in Department of Financial Services Rules, Chapter 69C-2, Florida Administrative Code, and Section 280.04, Florida Statutes. Eligible collateral includes Federal, federally-guaranteed, state and local government obligations; corporate bonds; and letters of credit issued by a Federal Home Loan Bank. Other collateral may be eligible, with the State CFO's permission.

### *b. Investment Authority and Compliance*

The SBA has the authority to administer and invest the funds of Florida PRIME in accordance with Chapter 218, Part IV, Florida Statutes. The statute states SBA shall invest the moneys of Florida

PRIME in the same manner and subject to the same restrictions as are set forth in Section 215.47, Florida Statutes, which identifies all authorized securities.

Section 215.47, Florida Statutes, includes a broad range of instruments to enable SBA to administer its varied investment responsibilities. The Investment Policy Statement for Florida PRIME lists the following principal investments:

1. United States (U.S.) Treasury obligations.
2. U.S. Government Agency obligations.
3. Government securities,[2] which are defined as any security issued or guaranteed as to principal or interest by the United States, or by a person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing.
4. Insurance contracts, including guaranteed investment contracts, funding agreements, and annuities.
5. Corporate debt securities, such as notes, bonds, debentures, commercial paper, interests in bank loans to companies, and demand instruments.
6. Bank instruments (including Yankee and Eurodollar), such as bank accounts, time deposits, certificates of deposit, and bankers' acceptances. Yankee instruments are denominated in U.S. dollars and issued by U.S. branches of foreign banks. Eurodollar instruments are denominated in U.S. dollars and issued by non-U.S. branches of U.S. or foreign banks.
7. Asset-backed securities, which may be in the form of commercial paper, notes, or pass-thru certificates.
8. Municipal securities issued by states, counties, cities, and other political subdivisions and authorities.
9. Foreign securities (i.e., U.S. dollar-denominated securities of issuers based outside the United States).
10. Mortgage-backed securities representing interests in pools of mortgages. Mortgages may have fixed or adjustable interest rates.
11. Rule 144A securities – The SBA has determined that Florida PRIME constitutes (i) an "accredited investor" as defined in Rule 501(a)(7) promulgated under the Securities Act of 1933, as amended (the Securities Act), as long as Florida PRIME has total assets in excess of $5,000,000 and (ii) a "qualified purchaser" as defined in Section 2(a)(51)(A)(iv) of the 1940 Act, as long as Florida PRIME in the aggregate owns and invests on a discretionary basis not less than $25,000,000 in investments, but does not constitute a "qualified institutional buyer" as defined in Rule 144A(a)(1) promulgated under the Securities Act. Florida PRIME is restricted from purchasing or acquiring securities or investments that would require Florida PRIME to represent in connection with such purchase or acquisition that it is a "qualified institutional buyer" as defined in Rule 144A(a)(1) promulgated under the Securities Act.

[2] Added in the Investment Policy Statement effective July 1, 2010, and replaces the Investment Policy Statement that was effective July 1, 2009.

12. Shares of registered investment companies that are money market mutual funds, including those that are affiliated with Federated (Investment Manager).

13. Special transactions, including repurchase agreements and delayed delivery transactions. Repurchase agreements involve transactions in which Florida PRIME buys a security from a dealer or bank and agrees to sell the security back at a mutually agreed-upon time and price. Delayed delivery transactions, including when-issued transactions, are arrangements in which Florida PRIME buys securities for a set price, with payment and delivery of the securities scheduled for a future time but no later than seven days in the future.

The primary investment objectives for Florida PRIME, in priority order, are safety, liquidity, and competitive returns with minimization of risks. This is accomplished by structuring the portfolio consistent with Part 270 of the Investment Company Act of 1940 (17 CFR 270.2a-7, Money Market Funds). In buying and selling portfolio securities for Florida PRIME, the Investment Manager will comply with the diversification, maturity, and credit quality conditions imposed by Rule 2a-7 under the 1940 Act; with the requirements imposed by any nationally recognized statistical rating organization (NRSRO) that rates Florida PRIME to ensure that it maintains a AAAm rating (or the equivalent); and with the investment limitations imposed by Section 215.47, Florida Statutes.

When the deviation between the market value and amortized cost of Florida PRIME exceeds 0.25 percent, the Investment Policy Statement requires that the Investment Manager establish a formal action plan. The Investment Policy Statement also requires that the Investment Oversight Group review the formal action plan and prepare a recommendation for the Executive Director's consideration.

When the deviation between the market value and amortized cost of Florida PRIME exceeds 0.50 percent, the Investment Policy Statement requires that the Executive Director promptly consider what action, if any, would be initiated. Where the Executive Director believes the extent of any deviation from Florida PRIME's amortized cost price per share may result in material dilution or other unfair results to investors or existing shareholders, he will cause Florida PRIME to take such action as he deems appropriate to eliminate or reduce to the extent reasonably practicable such dilution or unfair results.

### c. *Summary of Investment Holdings*

The following tables provide a summary of the par value or share amount, carrying amount, fair value, ranges of interest rates, and range of maturity dates for each major investment classification as of June 30, 2011, and June 30, 2010, (expressed in thousands):

**As of June 30, 2011**

| Investment Type | Par | Carrying Value | Fair Value | Range of Interest Rates[1] | Range of Maturity Dates |
|---|---|---|---|---|---|
| Certificates of deposit | $ 2,732,500 | $ 2,732,517 | $ 2,732,995 | .18%-.61% | 7/1/11-3/8/13 |
| Commercial paper | 1,977,769 | 1,977,209 | 1,977,377 | .09%-.51% | 7/5/11-12/8/11 |
| Money market funds | 530,210 | 530,210 | 530,210 | .00%-.10% | N/A[2] |
| Domestic corporate bonds & notes | 23,295 | 23,295 | 23,295 | .18%-.19% | 1/1/28-7/1/29[3] |
| Municipal bonds | 12,700 | 12,700 | 12,700 | .08%-.09% | 8/15/25-8/1/31[3] |
| Foreign corporate note ($ denom) | 45,000 | 45,000 | 45,014 | 0.31% | 7/17/12[4] |
| U.S. Treasury note | 30,000 | 30,056 | 30,081 | 0.75% | 11/30/11 |
| Repurchase agreements | 1,470,000 | 1,470,000 | 1,470,000 | .05%-.06% | 7/1/11 |
| Totals | $ 6,821,474 | $ 6,820,987 | $ 6,821,672 | | |

[1] The coupon rate in effect at June 30, 2011, is reported. If a security is discounted, the purchase yield is reported. The 7 day yield as of June 30, 2011, is reported for the money market funds. The yields fluctuate daily.

[2] Money market funds do not have a specified maturity date.

[3] Florida PRIME may tender these bonds and notes for 100 percent of the principal amount, plus accrued interest (if tendered between interest payment dates) with a minimum of 7 days prior notification to the trustee of the bonds or notes.

[4] Florida PRIME has the option to extend this maturity date on a monthly basis until the final maturity date of March 17, 2017. The maturity date as of June 30, 2011, is July 17, 2012.

**As of June 30, 2010**

| Investment Type | Par | Carrying Value | Fair Value | Range of Interest Rates[1] | Range of Maturity Dates[2] |
|---|---|---|---|---|---|
| Certificates of deposit | $ 1,425,500 | $ 1,425,500 | $ 1,425,206 | .32%-.71% | 7/16/10-6/27/11 |
| Commercial paper | 1,889,993 | 1,888,948 | 1,889,082 | .25%-.61% | 7/1/10-1/28/11 |
| Money market funds | 512,266 | 512,266 | 512,266 | .03%-.22% | N/A |
| Domestic corporate bonds & notes | 186,745 | 187,773 | 187,616 | .33%-5.0% | 7/27/10-8/1/37 |
| Foreign corporate note ($ denom) | 75,000 | 75,000 | 74,982 | 0.40% | 12/11/10 |
| Federal agencies | 445,000 | 444,994 | 445,015 | .40%-.65% | 8/4/10-5/25/11 |
| Repurchase agreements | 945,000 | 945,000 | 945,000 | .03%-.04% | 7/1/10 |
| Totals | $ 5,479,504 | $ 5,479,481 | $ 5,479,167 | | |

[1] The coupon rate in effect at June 30, 2010, is reported. If a security is discounted, the purchase yield is reported. The 7 day yield as of June 30, 2010, is reported for the money market funds. The yields fluctuate daily.

[2] Money market funds do not have a specified maturity date.

### *d. Investment Credit Risk and Concentration of Credit Risk of Debt Securities*

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Concentration of credit risk is the risk of loss attributed to the magnitude of the investment in a single issuer.

Pursuant to the Investment Policy Statement, investment credit risk and concentration of credit risk of debt securities will be managed as follows:

1. The Investment Manager will purchase short-term, high-quality fixed income securities. To be considered high-quality, a security must be rated in the highest short-term rating category by one or more NRSROs, or be deemed to be of comparable quality thereto by the Investment Manager, subject to Section 215.47(1)(j), Florida Statutes.
2. The Investment Manager will perform a credit analysis to develop a database of issuers and securities that meet the Investment Manager's standard for minimal credit risk. The Investment Manager will monitor the credit risks of all Florida PRIME's portfolio securities on an ongoing basis by reviewing the financial data, issuer news and developments, and ratings of designated NRSROs.
3. The Investment Manager generally will comply with the following diversification limitations that are additional to those set forth in Rule 2a-7. First, at least 50 percent of Florida PRIME assets will be invested in securities rated "A-1+" or those deemed to be of comparable credit quality thereto by the Investment Manager (i.e., so long as such deeming is consistent with the requirements of the NRSRO's AAAm (or equivalent) rating criteria), subject to Section

215.47(1)(j), Florida Statutes. Second, exposure to any single non-governmental issuer will not exceed 5 percent (at the time a security is purchased) and exposure to any single money market mutual fund will not exceed 10 percent of Florida PRIME assets.

In the event that a security receives a credit rating downgrade and ceases to be in the highest rating category, or the Investment Manager determines that the security is no longer of comparable quality to the highest short-term rating category (in either case, a "downgrade"), the Investment Manager will reassess whether the security continues to present minimal credit risk and will cause Florida PRIME to take any actions determined by the Investment Manager to be in the best interest of Florida PRIME. The Investment Manager will not be required to make reassessments if Florida PRIME disposes of the security (or the security matures) within five business days of the downgrade.

In the event that a security no longer meets the criteria for purchase due to default, event of insolvency, a determination that the security no longer presents minimal credit risks, or other material event (affected security), the Investment Manager must dispose of the security as soon as practical consistent with achieving an orderly disposition of the affected security, by sale, exercise of a demand feature or otherwise. An affected security may be held only if the Executive Director has determined, based upon a recommendation from the Investment Manager and the Investment Oversight Group, that it would not be in the best interest of Florida PRIME to dispose of the security taking into account market conditions that may affect an orderly disposition.

Florida PRIME's credit quality ratings were as follows at June 30, 2011, and June 30, 2010 (expressed in thousands):

| Fair Value of Florida PRIME Investments as of June 30, 2011 | | | | | | Ratings [1] | |
|---|---|---|---|---|---|---|---|
| Certificates of Deposit | Commercial Paper | Money Market Funds | Domestic Bonds & Notes | Foreign Corporate Note ($ denom) | Total | S&P | Moody's |
| $ …… | $ …… | $ 530,210 | $ …… | $ …… | $ 530,210 | AAAm | |
| …… | …… | …… | 7,700 | …… | 7,700 | AAA | |
| …… | …… | …… | 9,795 | 45,014 | 54,809 | AA | |
| …… | …… | …… | 5,000 | …… | 5,000 | Not rated [1] | Aa |
| …… | 1,977,377 | …… | 13,500 | …… | 1,990,877 | A-1 | |
| 2,732,995 | …… | …… | …… | …… | 2,732,995 | Not rated [1] | Not rated [1] |
| $ 2,732,995 | $1,977,377 | $ 530,210 | $ 35,995 | $ 45,014 | $ 5,321,591 | | |
| | | | | Repurchase agreements | 1,470,000 | Not rated [2] | Not rated [2] |
| | | | | U.S. Treasury notes | 30,081 | Not rated [3] | Not rated [3] |
| | | | | Total | $ 6,821,672 | | |

[1] Ratings for investments are presented using S&P credit ratings. If S&P did not rate a security, then Moody's ratings are presented. All of the investments presented as "Not rated" had short-term issuer credit ratings that met Florida PRIME's investment and SEC Rule 2a-7 guidelines.

[2] Repurchase agreements are not negotiable instruments and do not carry individual security ratings.

[3] U.S. Treasury obligations do not carry individual security ratings, but carried overall ratings of AAA by S&P, Aaa by Moody's and AAA by Fitch as of June 30, 2011. In August 2011, the S&P downgraded U.S. obligations to a AA+ rating. Moody's and Fitch ratings on U.S. debt obligations remain unchanged.

| Fair Value of Florida PRIME Investments as of June 30, 2010 | | | | | | | Ratings [1] | |
|---|---|---|---|---|---|---|---|---|
| Certificates of Deposit | Commercial Paper | Money Market Funds | Domestic Corporate Bonds & Notes | Foreign Corporate Note ($ denom) | Federal Agencies | Total | S&P | Moody's |
| $ …… | $ …… | $ 512,266 | $ …… | $ …… | $ …… | $ 512,266 | AAAm | |
| …… | …… | …… | …… | …… | 445,015 | 445,015 | AAA | |
| …… | …… | …… | 68,129 | …… | …… | 68,129 | AA | |
| …… | …… | …… | 113,487 | …… | …… | 113,487 | A | |
| …… | …… | …… | 6,000 | …… | …… | 6,000 | Not rated [1] | Aa |
| …… | 1,889,082 | …… | …… | …… | …… | 1,889,082 | A-1 | |
| 1,425,206 | …… | …… | …… | 74,982 | …… | 1,500,188 | Not rated [2] | Not rated [2] |
| $ 1,425,206 | $ 1,889,082 | $ 512,266 | $ 187,616 | $ 74,982 | $ 445,015 | $ 4,534,167 | | |
| | | | | Repurchase agreements | | 945,000 | Not rated [3] | Not rated [3] |
| | | | | Total | | $ 5,479,167 | | |

[1] Ratings for investments are presented using S&P credit ratings. If S&P did not rate a security, then Moody's ratings are presented. All of the investments presented as "Not rated" had short-term issuer credit ratings that met the Florida PRIME investment and SEC Rule 2a-7 guidelines.

[2] S&P and Moody's did not report a credit rating for the foreign corporate note, but Fitch did rate this security as AA.

[3] Repurchase agreements are not negotiable instruments and do not carry individual security ratings.

With respect to the concentration of credit risk, at June 30, 2011, and June 30, 2010, Florida PRIME had exposure of 5 percent or more to each of the following issuers (expressed in thousands):

**As of June 30, 2011**

| Issuer Name | Carrying Value | Percent of Portfolio Carrying Value | Fair Value | Percent of Portfolio Fair Value |
|---|---|---|---|---|
| Bank of America - Commercial paper [1] | $ 199,956 | 2.93% | $ 199,975 | 2.93% |
| Bank of America - Repurchase agreements [2] | 1,070,000 | 15.69% | 1,070,000 | 15.69% |
| Bank of America Total | $ 1,269,956 | 18.62% | 1,269,975 | 18.62% |
| BNP Paribas - Commercial paper | $ 38,950 | 0.57% | $ 38,970 | 0.57% |
| BNP Paribas - Certificates of deposit | 315,000 | 4.62% | 315,173 | 4.62% |
| BNP Paribas Total [3] | $ 353,950 | 5.19% | 354,143 | 5.19% |
| Credit Agricole - Commercial paper | $ 108,342 | 1.59% | $ 108,360 | 1.59% |
| Credit Agricole - Certificates of deposit | 236,000 | 3.46% | 236,069 | 3.46% |
| Credit Agricole Total [3] | $ 344,342 | 5.05% | 344,429 | 5.05% |
| Morgan Stanley [3] | $ 400,000 | 5.86% | $ 400,000 | 5.86% |
| Societe Generale - Commercial paper | $ 224,887 | 3.30% | $ 224,951 | 3.30% |
| Societe Generale - Certificates of deposit | 130,000 | 1.90% | 130,019 | 1.90% |
| Societe Generale Total [3] | $ 354,887 | 5.20% | 354,970 | 5.20% |

[1] For purposes of the SEC Rule 2a-7 exposure restriction calculations, the Bank of America commercial paper is considered a separate issuer position from the Bank of America collateralized repurchase agreements.

[2] For purposes of SEC Rule 2a-7 exposure restriction calculations, acquisitions of repurchase agreements may be deemed to be acquisitions of the underlying securities, provided the obligation of the seller is fully collateralized. These agreements are fully collateralized. Consequently, they are not subject to SEC Rule 2a-7 issuer exposure restrictions.

[3] Under SEC Rule 2a-7, liquidations are not required for exposures over 5 percent if the overage is caused by participant account movements (i.e. withdrawals). The excess exposure to BNP Paribas, Credit Agricole, and Societe Generale were caused by participant account movements.

**As of June 30, 2010**

| Issuer Name[1] | Carrying Value | Portfolio Carrying Value | Fair Value | Percent of Portfolio Fair Value |
|---|---|---|---|---|
| Bank of America - Short-term bank notes | $ 100,000 | 1.82% | $ 99,987 | 1.82% |
| Bank of America - Repurchase agreements | 510,000 | 9.31% | 510,000 | 9.31% |
| Bank of America Total | $ 610,000 | 11.13% | 609,987 | 11.13% |
| Federal Home Loan Banks - Unsecured bonds | $ 444,994 | 8.12% | $ 445,015 | 8.12% |
| Morgan Stanley - Repurchase agreements | $ 435,000 | 7.94% | $ 435,000 | 7.94% |

[1]For purposes of SEC Rule 2a-7 exposure restriction calculations, acquisitions of repurchase agreements may be deemed to be acquisitions of the underlying securities, provided the obligation of the seller is fully collateralized. These agreements are fully collateralized. Consequently, they are not subject to SEC Rule 2a-7 issuer exposure restrictions. The Federal Home Loan Banks holdings are federal agency debt securities; therefore, under SEC Rule 2a-7 the Investment Manager is not prohibited from purchasing a concentration greater than 5 percent.

### e. Investments, Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, SBA will not be able to recover the value of investment or collateral securities that are in the possession of an outside party.

The SBA's policy is that custodial credit risk will be minimized through the use of trust accounts maintained at top tier third party custodian banks. To the extent possible, negotiated trust and custody contracts shall require that all deposits, investments, and collateral be held in accounts in the SBA's name, separate and apart from the assets of the custodian banks.

The SBA engaged BNY Mellon (Custodian) to provide asset safekeeping, custody, fund accounting, and performance measurement services to Florida PRIME. At June 30, 2011, and June 30, 2010, all investments, except those in money market funds which are not exposed to custodial credit risk, were held in SBA's name by SBA's custodial bank.

### f. Investments, Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of investments. Pursuant to the Investment Policy Statement, the Investment Manager will target a dollar-weighted average maturity (DWAM) range for Florida PRIME based on its interest rate outlook. The Investment Manager will formulate its interest rate outlook by analyzing a variety of factors, such as current and expected U.S. economic growth; current and expected interest rates and inflation; and the Federal Reserve Board's monetary policy. The Investment Manager will generally shorten Florida PRIME's DWAM when it expects interest rates to rise and extend Florida PRIME's DWAM when it expects interest rates to fall. The Investment Manager will exercise reasonable care to maintain a DWAM of 60 days or less for Florida PRIME. For purposes of calculating DWAM, the maturity of an adjustable rate security generally will be the period remaining until its next interest rate reset date.

Presented below are the investments held in Florida PRIME at June 30, 2011, and June 30, 2010, at fair value (expressed in thousands), with the DWAM for each security type:

**As of June 30, 2011**

| Investment Type | Fair Value | Dollar Weighted Average Days to Maturity [1] |
|---|---|---|
| Certificates of deposit [2] | $ 2,732,995 | 45 |
| Commercial paper [2] | 1,977,377 | 42 |
| Money market funds [3] | 530,210 | 1 |
| Domestic corporate bonds & notes | 23,295 | 7 |
| Municipal bonds & notes | 12,700 | 7 |
| Foreign corporate note ($ denom) | 45,014 | 48 |
| U.S. Treasury notes | 30,081 | 153 |
| Repurchase agreements | 1,470,000 | 1 |
| Total | $ 6,821,672 | |
| **Portfolio dollar-weighted average maturity** | | **31** |

[1] Interest rate reset dates are used in the calculation of the dollar-weighted average days to maturity.

[2] Certificates of deposit and commercial paper include domestic and U.S. dollar-denominated foreign issues.

[3] The weighted average days to maturity of the underlying securities in the three money market funds at June 30, 2011, ranged from 40 to 53 days. However, the money market funds provided daily liquidity.

**As of June 30, 2010**

| Investment Type | Fair Value | Dollar Weighted Average Days to Maturity [1] |
|---|---|---|
| Certificates of deposit [2] | $ 1,425,206 | 48 |
| Commercial paper [2] | 1,889,082 | 41 |
| Money market funds [3] | 512,266 | 1 |
| Domestic corporate bonds & notes | 187,616 | 61 |
| Foreign corporate note ($ denom) | 74,982 | 12 |
| Federal agencies | 445,015 | 206 |
| Repurchase agreements | 945,000 | 1 |
| Total | $ 5,479,167 | |
| **Portfolio dollar-weighted average maturity** | | **46** |

[1] Interest rate reset dates were used in the calculation of the dollar-weighted average days to maturity.

[2] Certificates of deposit and commercial paper include domestic and U.S. dollar-denominated foreign issues.

[3] The weighted average days to maturity of the underlying securities in the three money market funds at June 30, 2010, ranged from 32 to 51 days. However, the money market funds provided daily liquidity.

### *g. Investments, Foreign Currency Risk*

Florida PRIME may purchase only U.S. dollar-denominated securities, and was not exposed to foreign currency risk during the fiscal years ended June 30, 2011, and June 30, 2010. All investments were denominated in U.S. dollars.

## *3. PENDING MATTERS - CLOSED*

On March 3, 2010, the SEC completed its investigation relating to the purchase and sale of secured notes issued by KKR Atlantic, KKR Pacific, Ottimo, and Axon (among others) to the SBA on behalf of the LGIP (Florida PRIME) and other funds by various broker-dealers and did not recommend any enforcement action by the Commission.

# AUDITOR GENERAL
## STATE OF FLORIDA

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AUDITOR GENERAL

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The President of the Senate, the Speaker of the
House of Representatives, and the
Legislative Auditing Committee

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

We have audited the financial statements of the State Board of Administration's (SBA) Local Government Surplus Funds Trust Fund (Florida PRIME), as of and for the fiscal year ended June 30, 2011, and have issued our report thereon included under the heading **INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS.** We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered SBA's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SBA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of SBA's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies,

significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Florida PRIME's financial statements are free of material misstatement, we performed tests of SBA's compliance with certain provisions of laws, rules, regulations, contracts, and policies, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Pursuant to Section 11.45(4), Florida Statutes, this report is a public record and its distribution is not limited. Auditing standards generally accepted in the United States of America require us to indicate that this report is intended solely for the information and use of the Legislative Auditing Committee, members of the Florida Senate and the Florida House of Representatives, and applicable management and is not intended to be and should not be used by anyone other than those specified parties.

Respectfully submitted,

David W. Martin, CPA
December 21, 2011

End of Section

Florida Hurricane Catastrophe Fund

# Memo

**TO:** Ashbel C. Williams, Executive Director & CIO

**THRU:** Jack E. Nicholson, Chief Operating Officer, FHCF

**FROM:** Tracy Allen, Senior Attorney, FHCF

**DATE:** March 8, 2012

**SUBJECT:** Cabinet Meeting for March 20, 2012
Notice of Proposed Rule for Rules 19-8.029, F.A.C., Insurer Reporting Requirements and 19-8.030, F.A.C., Insurer Responsibilities
Request approval to file these two rules for Notice of Proposed Rule and request approval to file these rules for adoption if no member of the public timely requests a rule hearing.

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**ITEM 1. SUMMARY AND REASONS FOR RULE CHANGES:**

Rule 19-8.029, F.A.C., Insurer Reporting Requirements.
Insurers are required by s.215.555(4), F.S., to notify the State Board of Administration of Florida of losses under covered policies and are required by s.215.555(5), F.S., to notify the State Board of Administration of Florida of insured values under covered policies. Rule 19-8.029, F.A.C., Insurer Reporting Requirements, adopts the 2012/2013 Data Call for exposure reporting and the loss forms for loss reporting. In addition, unnecessary or obsolete language has been removed and, due to legislative changes, the references to Citizens Property Insurance Corporation's "High Risk" account have been changed to "Coastal Account" to reflect this account's new name.

Rule 19-8.030, F.A.C., Insurer Responsibilities.
This rule adopts the 2012/2013 exposure examination instructions and the loss examination instructions. In addition, unnecessary or obsolete language has been removed and, due to legislative changes, the references to Citizens Property Insurance Corporation's "High Risk" account have been changed to "Coastal Account" to reflect this account's new name.

**SUMMARY OF INCORPORATED FORM CHANGES:** Attached hereto.

**EXTERNAL INTEREST:** A rule development workshop was held on January 9, 2012. Representatives of the FHCF attended and presented the rules and incorporated forms and

engaged in discussion with members of the public who attended. The rulemaking notice was published in the *Florida Administrative Weekly* on December 22, 2011, Vol. 37, No. 51. Also, the rules and forms were presented, discussed, and approved by the FHCF Advisory Council at a public meeting on January 12, 2012.

**SIGNIFICANT POLICY ISSUES:** None.

**CONTROVERSIAL ISSUES:** None.

**ACTION REQUESTED:** It is requested that the proposed amendments to these two rules be presented to the Cabinet Aides on March 14, 2012, and to the State Board of Administration Trustees ("Board") on March 20, 2012, with a request to approve the filing of these two rules for Notice of Proposed Rule and to approve filing both rules for adoption with the Department of State if no member of the public timely requests a rule hearing. A notice of the meeting of the Board was published in the *Florida Administrative Weekly* on March 2, 2012, Vol. 38, No. 9.

**ATTACHMENTS TO BE INCLUDED WITH THE SBA AGENDA ITEM 1:**

- 2012 Incorporated Form and Rule Changes Summary
- Notice of Proposed Rule
- Notice of Meeting of Board as filed in the *Florida Administrative Weekly*
- Rule 19-8.029, F.A.C., Insurer Reporting Requirements
- Rule 19-8.030, F.A.C., Insurer Responsibilities
- 2012/2013 Contract Year Incorporated Forms –

**Rule 19-8.029, F.A.C.**
**FHCF-D1A**, "Florida Hurricane Catastrophe Fund 2012 Data Call" rev. 01/12; **FHCF-L1A**, "Contract Year 2012 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)" rev. 01/12, Form **FHCF-L1B**, "Contract Year 2012 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)" rev. 01/12.

**Rule 19-8.030, F.A.C.**
Forms incorporated into this rule which will **not** be amended: **UNICEDE ® /PX Data Exchange Format**, Version 4.0.0." and **FHCF C-1**, "Company Contact Information".
Forms incorporated into this rule which **will** be amended: **FHCF-EAP1**, "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination-Contract Year 2012 Advance Preparation Instructions" rev. 01/12; **FHCF-LAP1,** "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination-Contract Year 2012 Advance Preparation Instructions" rev. 01/12

These rules and all incorporated forms to be amended show the proposed amendments in "track changes" format.

2012 Incorporated Form and Rule Changes Summary

## Rules

### 19-8.029 Insurer Reporting Requirements

| | |
|---|---|
| (2)(a) | The reference to Citizens Property Insurance Corporation's "High Risk" account has been changed to "Coastal Account" to reflect this account's new name. (See CS/CS/CS/SB 408; 2011-39, L.O.F.) |
| (2)(e)--(h) | Unnecessary language removed. |
| (3)(b) | Unnecessary language removed. |
| (4)(a)--(4)(e) | Obsolete language removed. |
| (4)(i) | Adopts this Contract Year's Data Call, FHCF-D1A. |
| (5)(b) | Unnecessary language removed. |
| (7)(h) | Adopts this Contract Year's Interim Loss Report and Proof of Loss Report, FHCF-L1A and FHCF-L1B. |

### 19-8.030 Insurer Responsibilities

| | |
|---|---|
| (3)(d) | The reference to Citizens Property Insurance Corporation's "High Risk" account has been changed to "Coastal Account" to reflect this account's new name. (See CS/CS/CS/SB 408; 2011-39, L.O.F.) |
| (3)(i) | Unnecessary language removed. |
| (4)(c) | Unnecessary language removed. |
| (5)(a) | The reference to Citizens Property Insurance Corporation's "High Risk" account has been changed to "Coastal Account" to reflect this account's new name. (See CS/CS/CS/SB 408; 2011-39, L.O.F.) |
| (5)(b)-(d) | Unnecessary language removed. |
| (7)(a)1.& 7. | (Newly renumbered 7.); Obsolete or unnecessary language removed. |
| (7)(a)9. | Adopts this Contract Year's exposure examination instructions, FHCF-EAP1 and this Contract Year's loss reimbursement examination instructions, FHCF-LAP1. |
| (8) | Clarifying language is added and subparagraphs (a) through (f) are removed as obsolete. |
| (11) | This paragraph removed as obsolete. This optional coverage expired on 5/31/12. See Section 215.555(4)(d)4., F.S. |

## Incorporated Documents

***Rule 19-8.029, F.A.C., Incorporated Documents:***

**FHCF-L1A, 2012 Interim Loss Report:** No changes other than the date at the top of the form.

**FHCF-L1B, 2012 Proof of Loss Report:** The date at the top of the form has been updated and references to the Section 215.555(4)(b)4., F.S., $10 million of optional

coverage provided in (4)(b)4., F.S., which expired with the 2011-2012 Contract Year and the Section 215.555(16), F.S., optional coverage known as " TEACO", which expired on 5/31/10 at the end of the 2009-2010 Contract Year, have been removed. In addition, language mirroring language in the Contract has been added to the signature section to impress upon the insurer that the losses reported to the FHCF need to be as accurate as they can be since the FHCF makes critical decisions on bonding and takes other actions based upon these reports.

**Not Provided: FHCF C-1, Company Contact Information**: No Changes.

**FHCF-D1A, 2012 Data Call:** The Data Call contains a list of important changes on Page 2. Primarily the changes to the Data Call are updating the dates, changing the reference to Citizens Property Insurance Corporation's "High Risk" account to the "Coastal Account", and simplification of the Data Call by eliminating the Building Code Effectiveness Grading and the Florida Building Code Indicator fields. In addition, under "Explanation of Exposure Fluctuations", the threshold for providing an explanation has been reduced.

***Rule 19-8.030, F.A.C., Incorporated Documents:***

**FHCF-EAP1, Exposure Examination—Contract Year 2012 Advance Preparation Instructions:** The reference to Citizens Property Insurance Corporation's "High Risk" account has been changed to "Coastal Account" to reflect this account's new name. (See CS/CS/CS/SB 408; 2011-39, L.O.F.) Dates and page numbers have been updated and, to mirror the elimination of the Building Code Effectiveness Grading and Florida Building Code Indicator fields in the Data Call, these fields have also been eliminated in the FHCF-EAP1.

**FHCF-LAP1, Loss Reimbursement Examination—Contract Year 2012 Advance Preparation Instructions:** Dates and non-substantive clean up. No substantive changes.

Notice of Proposed Rule

**STATE BOARD OF ADMINISTRATION**

RULE NO: RULE TITLE

19-8.029: Insurer Reporting Requirements

19-8.030: Insurer Responsibilities

PURPOSE AND EFFECT: The State Board of Administration, Florida Hurricane Catastrophe Fund, seeks to amend the rules listed above to implement Section 215.555, Florida Statutes.

SUMMARY: Rule 19-8.029, F.A.C., is promulgated to implement Section 215.555(5), Florida Statutes, regarding the reporting by insurers of insured values under covered policies to the Florida Hurricane Catastrophe Fund, for the 2012-2013 contract year and to adopt the 2012/2013 Interim and Proof of Loss forms. Rule 19-8.030, F.A.C., Insurer Responsibilities, is being amended to adopt the 2012/2013 Exposure and Loss Reimbursement Examination Advance Preparation Instructions and to adopt the 2012/2013 Interim and Proof of Loss forms. In addition, obsolete material is being removed from both rules.

OTHER RULES INCORPORATING THESE RULES: There are no other rules which incorporate these two rules. However, Rule 19-8.029, F.A.C., is referenced in Rules 19-8.028 and 19-8.030, F.A.C., as follows: Rule 19-8.028(2)(f) and (4)c.3.b.,F.A.C., Reimbursement Premium Formula, and Rule 19-8.030(3)(i), (5)(b)-(c), and (8), F.A.C., Insurer Responsibilities.

EFFECT ON THOSE OTHER RULES: There is no impact on the two rules which reference Rule 19-8.029, F.A.C.

SUMMARY OF STATEMENT OF ESTIMATED REGULATORY COSTS AND LEGISLATIVE RATIFICATION STATEMENT: No Statement of Estimated Regulatory Cost was prepared for either rule. Insurers are required by Section 215.555(4), F.S., to notify the State Board of Administration of Florida of losses under covered policies and are required by Section 215.555(5), F.S., to notify the State Board of Administration of Florida of its insured values under covered policies. Rule 19-8.029, F.A.C., Insurer Reporting Requirements, adopts the 2012/2013 Data Call for exposure reporting and both rules adopt loss forms for loss reporting and provide guidance for such reporting. Upon review of the proposed changes to these two rules and the incorporated forms, the State Board of Administration of Florida has determined that the preparation of a Statement of Estimated Regulatory Costs is not necessary and that neither rule meets the statutory threshold for ratification by the legislature. The changes to these rules do not have an adverse impact on small business and do not directly or indirectly increase regulatory costs in excess of $200,000 in the aggregate within 1 year of implementation. The changes to these rules also do not directly or indirectly have an adverse impact on economic growth, private sector job creation or employment, or private sector investment, business competitiveness or innovation or increase regulatory costs, including any transactional costs, in excess of $1 million in the aggregate within 5 years after the implementation of either rule.

Any person who wishes to provide information regarding a statement of estimated regulatory costs, or provide a proposal for a lower cost regulatory alternative must do so in writing within 21 days of this notice.

SPECIFIC AUTHORITY: 215.555(3), F.S.

LAW IMPLEMENTED: 215.555(2), (3), (4), (5), (6), (7), (10), (17), F.S.

IF REQUESTED WITHIN 21 DAYS OF THE DATE OF THIS NOTICE, A HEARING WILL BE HELD AT THE DATE, TIME AND PLACE SHOWN BELOW (IF NOT REQUESTED, THIS HEARING WILL NOT BE HELD):

DATE AND TIME: April 23, 2012, 9:00 a.m. (ET) to conclusion of meeting.

PLACE: Room 116 (Hermitage Conference Room), 1801 Hermitage Blvd., Tallahassee, Florida 32308.

Pursuant to the provisions of the Americans with Disabilities Act, any person requiring special accommodations to participate in this workshop/meeting is asked to advise the agency at least 7 days before the workshop/meeting by contacting: Tracy Allen, 1801 Hermitage Blvd., Tallahassee, FL 32308, 850-413-1341, tracy.allen@sbafla.com. If you are hearing or speech impaired, please contact the agency using the Florida Relay Service, 1(800)955-8771 (TDD) or 1(800)955-8770 (Voice).

THE PERSON TO BE CONTACTED REGARDING THE PROPOSED RULE IS: Tracy Allen, Senior Attorney, Florida Hurricane Catastrophe Fund, State Board of Administration, P.O. Box 13300, Tallahassee, FL 32317-3300, telephone (850) 413-1341, tracy.allen@sbafla.com.

THE FULL TEXT OF THE PROPOSED RULE IS:

**19-8.029 Insurer Reporting Requirements.**

Paragraphs (1) through (2) (introductory language), No changes.

(2)(a) Citizens Property Insurance Corporation or Citizens means the entity formed under Section 627.351(6), F.S., and includes both the Coastal ~~High Risk~~ Account and the Personal Lines and Commercial Lines Accounts.

(2)(b) through (2)(c), No changes.

(2)(d) Covered Policy is defined in Section 215.555(2)(c), F.S., and in the Reimbursement Contract adopted by and incorporated into Rule 19-8.010, F.A.C.

(e) Data Call or Florida Hurricane Catastrophe Fund Data Call means the annual reporting of insured values ~~forms~~ form FHCF-D1A.. ~~These forms are the FHCF-D1A for the Contract Years after the 2002/2003 Contract Year and the FHCF-D1A and FHCF-D1B for thie Contract Year 2002/2003 and all prior Contract Years.~~

(2)(f) through (2)(g), No changes.

(2)(h) Loss Reporting Forms mean the FHCF-L1A and FHCF-L1B. ~~for Contract Years after the 2002/2003 Contract Year and means the FHCF-L1A, FHCF-L1B and FHCF-L1C for the Contract Years 2002/2003 and alll prior Contract Years.~~

(2)(i) through (3)(a), No changes.

(3)(b) Confidentiality of reports containing insured values under Covered Policies. Section 215.557, F.S., enacted for the express purpose of protecting trade secret and proprietary information submitted to the FHCF by participating insurers, protects the confidentiality of information of the type submitted in the Data Call ~~(FHCF-D1A)~~, examination workpapers, and examination reports. Such information is not subject to the provisions of Section 119.07(1), F.S., or Section 24(a), Article I of the Florida State Constitution. Confidential data and trade secrets reported to the FHCF are protected to the extent allowed by law.

(3)(c) through (3)(d), No changes.

(4)~~(a) For the 1999/2000 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 1999 Data Call," rev. 05/99; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 5.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(b) For the 2000/2001 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2000 Data Call," rev. 05/00; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 6.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Florida Hurricane Catastrophe Fund 2000 Data Call for Newly Licensed Companies," rev. 05/00; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 6.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(c) For the 2001/2002 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2001 Data Call," rev. 05/01; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 7.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Florida Hurricane Catastrophe Fund 2001 Data Call for Newly Licensed Companies," rev. 05/01; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 7.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(d) For the 2002/2003 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call," rev. 05/02 and Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 3/27/01. The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call for Newly Licensed Companies," rev. 05/02; and Form FHCF-MOD "CLASIC DATA FORMAT (tm) for~~

~~Excess Insurance, Version 1.1," rev. 3/27/01. The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(e) For the 2003/2004 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2003 Data Call," rev. 05/03 and UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. A new participant shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator. NOTE: Form FHCF-D1B, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call for Newly Licensed Companies," rev. 05/02 used in past years by new participants is no longer being used. The information new participants must submit is now incorporated into Form FHCF-D1A.~~

(4)(a) ~~(f)~~ For the 2004/2005 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Amended Florida Hurricane Catastrophe Fund 2004 Data Call," rev. 05/11/04 and UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. A new participant shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(b) ~~(g)~~ For the 2005/2006 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2005 Data Call," rev. 05/05 and "UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(c) ~~(h)~~ For the 2006/2007 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2006 Data Call," rev. 05/06, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(d) ~~(i)~~ For the 2007/2008 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2007 Data Call," rev. 05/07, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(e) ~~(j)~~ For the 2008/2009 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2008 Data Call," rev. 05/08, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(f) ~~(k)~~ For the 2009/2010 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2009 Data Call," rev. 05/09, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(g) ~~(l)~~ For the 2010/2011 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2010 Data Call," rev. 05/10, hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(h) ~~(m)~~For the 2011/2012 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2011 Data Call," rev. 01/11, http: //www.flrules.org/Gateway/reference.asp?No= Ref-00413, is hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(i) For the 2012/2013 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2012 Data Call," rev. 01/12, http: //www.flrules.org/Gateway/reference.asp?No= Ref-XXXXX, is hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(5) through (5)(a), No changes.

(5)(b) Insurers shall report their ultimate net losses ~~(as defined in the Reimbursement Contract, adopted and incorporated into Rule 19-8.010, F.A.C.)~~ for each loss occurrence on the Form FHCF-L1B, "Florida Hurricane Catastrophe Fund Proof of Loss Report," for the applicable Contract Year, as specified in subsection (7) herein. To obtain copies of this form, see subsection (6), below. To qualify for reimbursement, the Proof of Loss Report must have the original signatures of two executive officers authorized by the Company to sign the report. Proof of Loss Reports may be faxed only if the Company does not qualify for a reimbursement. While a Company may submit a Proof of Loss Report requesting reimbursement at any time following a loss occurrence, all Companies shall submit a mandatory Proof of Loss Report for each loss occurrence no earlier than December 1 and no later than December 31 of the Contract Year during which the Covered Event(s) occurs using the most current data available, regardless of the amount of Ultimate Net Loss or the amount of loss reimbursements or advances already received. After the mandatory December Proof of Loss Report, quarterly Proof of Loss Reports are required. For purposes of this rule, quarterly Proof of Loss Reports shall be those reports submitted at each quarter end date after December 31 of the Contract Year in which the loss occurrence occurs and continuing until all claims and losses resulting from loss occurrences commencing during the Contract Year are fully discharged, including any adjustments to such losses

due to salvage or other recoveries, in accordance with the reporting requirements in this paragraph. "Fully Discharged" means the earlier of the date on which the insurer has paid its policyholders in full or the commutation clause, in Article X of the Reimbursement Contract~~, adopted in Rule 19-8.010,F.A.C.,~~ takes effect. For the quarterly report due on March 31, any insurer whose losses exceed 50% of its FHCF retention for a specific loss occurrence shall submit a Proof of Loss Report for that loss occurrence. For the quarterly report due on June 30, any insurer whose losses exceed 75% of its FHCF retention for a specific loss occurrence shall submit a Proof of Loss Report for that loss occurrence. For the quarterly reports due on September 30 and thereafter, any insurer which anticipates that its losses will exceed its FHCF retention for a specific loss occurrence shall submit quarterly Proof of Loss Reports until all its losses are paid to its policyholders and the insurer has received reimbursement from the Fund. Annually, all Companies shall submit a mandatory year-end Proof of Loss Report for each loss occurrence, using the most current data available. This Proof of Loss Report shall be filed no earlier than December 1 and no later than December 31 of each year and shall continue until the earlier of the expiration of the commutation period or until all claims and losses resulting from the loss occurrence are fully discharged including any adjustments to such losses due to salvage or other recoveries.

(5)(c) through (7)(g), No changes.

(7)(h) For the 2012/2013 Contract Year, the applicable Interim Loss Report is the "Contract Year 2012 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1A, rev. 01/12, http://www.flrules.org/Gateway/reference.asp?No=Ref-XXXXX, which is hereby adopted and incorporated by reference into this rule. The applicable Proof of Loss Report is the "Contract Year 2012 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 01/12, http://www.flrules.org/Gateway/reference.asp?No=Ref-XXXXX, which is hereby adopted and incorporated by reference into this rule. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(8) Company Contact Information: Companies must submit Form FHCF C-1, Company Contact Information, rev. 05/10, which is hereby adopted and incorporated by reference into this rule, by June 1 of each Contract Year. This form must be updated by the Company as the information provided thereon changes. The FHCF shall have the right to rely upon the information provided by the Company to the FHCF on this form until receipt by the FHCF of a new properly completed and notarized FHCF C-1 from the Company. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

*Rulemaking Authority 215.555(3) FS. Law Implemented 215.555(2), (3), (4), (5), (6), (7), (15) FS. History–New 5-17-99, Amended 6-19-00, 6-3-01, 6-2-02, 11-12-02, 5-13-03, 5-19-04, 8-29-04, 5-29-05, 5-10-06, 5-8-07, 6-8-08, 3-30-09, 8-2-09, 3-29-10, 8-8-10, 7-20-11, X-X-12.*

**19-8.030 Insurer Responsibilities.**

Paragraphs (1) through (3)(c), No changes.

(3)(d) Citizens Property Insurance Corporation or Citizens means the entity formed under Section 627.351(6), F.S., and includes both the Coastal ~~High Risk~~ Account and the Personal Lines and Commercial Lines Accounts.

(3)(e) through (3)(h), No changes.

(3)(i) Data Call or Florida Hurricane Catastrophe Fund Data Call means the annual reporting of insured values ~~forms~~ form FHCF-D1A as adopted and incorporated into Rule 19-8.029,F.A.C. ~~These forms, as adopted and incorporated into Rule 19-8.029, F.A.C., are the FHCF-D1A for Contract Years after the 2002/2003 Contract Year and the FHCF-D1A for the Cntract Year 2002/2003 and all prior Contract Years.~~

(3)(j) through (4)(a)1., No changes.

(4)(a)2. For the 2011/2012 and subsequent Contract Years, each Insurer required to participate in the FHCF must designate a coverage level in the annual Reimbursement Contract, make any required selections therein and execute the Reimbursement Contract and applicable Addenda so that the Contract, including the schedules and applicable Addenda, have been received by ~~the~~ March 1 prior to each Contract Year.

(4)(b), No changes.

(4)(c) New Participants during the period of December 1 through May 31: Those Insurers that first begin writing Covered Policies from December 1 through May 31 of a Contract Year, along with the Insurers described in paragraph (b) immediately above, are New Participants. However, these Insurers shall not complete and submit the Data Call ~~(Form FHCF-D1A)~~ but shall meet all other requirements for New Participants.

(4)(d), No changes.

(5) Exposure Reporting Requirements.

(a) Quota Share Primary Insurance: Citizens and Authorized Insurers may enter into Quota Share Primary Insurance Arrangements with respect to the Coastal ~~High Risk~~ Account policies. The statute also provides, in Section 627.351(6)(c)2.a.(II), F.S., that Citizens shall be responsible for the annual reporting of insured values to the FHCF for both Citizens and the Insurer participating with Citizens in the Quota Share Arrangement. Citizens shall report the insured values covered by the Quota Share Primary Insurance Arrangements in the same manner that all other current participants, as described in paragraph (b) below, report their insured values. Please note that both Citizens and the Quota Share Primary Insurer must keep complete and accurate records, including copies of policy declaration pages and supporting claims documents, for the purpose of exposure and loss reimbursement examinations by the FHCF.

(b) Current Participants: Each Insurer, with Covered Policies as of June 1 of a Contract Year must participate in the FHCF and must complete and submit the Data Call~~. The Data Call is incorporated into Rule 19-8.029, F.A.C., and is due~~, correctly completed, no later than September 1 of the Contract Year.

(c) New Participants during the period of June 1 through November 30: Those Insurers that first begin writing Covered Policies from June 1 through November 30 of a Contract Year must complete and submit the Data Call~~. The Data Call is incorporated into Rule 19-8.029, F.A.C., and is due~~, correctly completed, by March 1 of the Contract Year.

(d) Resubmissions of Data: With one exception noted below, any Insurer which submits a Data Call~~, Form FHCF-D1A~~, with incorrect data, incomplete data, or data in the wrong format and is required to resubmit will be given 30 days from the date on the letter from the FHCF notifying the Insurer of the need to resubmit. An extension of 30 days will be granted if the Insurer can show that the need for the additional time is due to circumstances

beyond the reasonable control of the Insurer. Exception: If the Insurer, at the time it receives notice of the need to resubmit, has already been issued a notice of examinations, the usual 30 day time limitation (measured from the date of the letter giving notice of the need to resubmit) does not apply. In this situation, the time period in which the Insurer must resubmit is measured by counting backwards 30 days from the date that the examinations are scheduled to begin as reflected on the notice of examinations letter. The FHCF needs the information prior to the examinations; thus, no extensions can be granted.

(6) through (7) (introductory language), No changes.

(7)(a)~~1. For Contract Years prior to the 2003/2004 Contract Year, Form FHCF-AP1, as revised for each Contract Year, is the applicable Exposure Examination Advance Preparation Instructions form to use.~~

1.~~2.~~ For the 2004/2005 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Audit – Contract Year 2004 Advance Preparation Instructions," FHCF-AP1, rev. 5/04. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2004 Advance Preparation Instructions," FHCF-LAP1, 05/06.

2. ~~3.~~ For the 2005/2006 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2005 Advance Preparation Instructions," FHCF-AP1, rev. 5/05. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2005 Advance Preparation Instructions," FHCF-LAP1, rev. 05/07.

3. ~~4.~~ For the 2006/2007 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2006 Advance Preparation Instructions," FHCF-EAP1, rev. 5/06. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/06.

4. ~~5.~~ For the 2007/2008 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2007 Advance Preparation Instructions," FHCF-EAP1, rev. 05/07. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/07.

5. ~~6.~~ For the 2008/2009 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2008 Advance Preparation Instructions," FHCF-EAP1, rev. 05/08. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/08.

6. ~~7.~~ For the 2009/2010 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2009 Advance Preparation Instructions," FHCF-EAP1, rev. 05/09. The applicable loss examination instructions form is the "Florida Hurricane

Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/09.

7. ~~8.~~ For the 2010/2011 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2010 Advance Preparation Instructions," FHCF-EAP1, rev. 05/10. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2010 Advance Preparation Instructions," FHCF-LAP1, rev. 05/10. ~~These forms are hereby adopted and incorporated by reference into this rule. Copies of these forms may be obtained from the FHCF website, www.sbafla.com/fhcf or by contacting the State Board of Administration. The mailing address is P.O. Box 13300, Tallahassee, Florida 32317-3300. The street address is 1801 Hermitage Blvd., Tallahassee, Florida 32308.~~

8. ~~9.~~ For the 2011/2012 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2011 Advance Preparation Instructions," FHCF-EAP1, rev. 01/11, http://www flrules.org/Gateway/reference.asp?No=Ref-00416. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2011 Advance Preparation Instructions," FHCF-LAP1, rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00417.

9. For the 2012/2013 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2012 Advance Preparation Instructions," FHCF-EAP1, rev. 01/12, http://www flrules.org/Gateway/reference.asp?No=Ref-XXXXX. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2012 Advance Preparation Instructions," FHCF-LAP1, rev. 01/12, http://www.flrules.org/Gateway/reference.asp?No=Ref-XXXXX.

10. These forms are hereby adopted and incorporated by reference into this rule. Copies of these forms may be obtained from the FHCF website, www.sbafla.com/fhcf or by contacting the State Board of Administration. The mailing address is P. O. Box 13300, Tallahassee, Florida 32317-3300. The street address is 1801 Hermitage Blvd., Tallahassee, Florida 32308.

(7)(b) through (d), No changes.

(8) Loss Reporting. Participating Insurers are required to file the following two types of loss reports at the times prescribed in Rule 19-8.029, F.A.C. Form FHCF-L1A, "Florida Hurricane Catastrophe Fund Interim Loss Report," for the applicable Contract Year and Form FHCF-L1B, "Florida Hurricane Catastrophe Fund Proof of Loss Report," for the applicable Contract Year as adopted in Rule 19-8.029, F.A.C.

~~(a) For the Contract Year 2006-2007, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/06 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/06.~~

~~(b) For the Contract Year 2007-2008, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/07 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/07.~~

~~(c) For the Contract Year 2008-2009, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/08 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/08.~~

~~(d) For the Contract Year 2009-2010, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/09 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/09. These forms are hereby adopted and incorporated by reference into this rule.~~

~~(e) For the Contract Year 2010-2011, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/10 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/10. These forms are hereby adopted and incorporated by reference into this rule.~~

~~(f) For the Contract Year 2011-2012, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00419, and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00418. These forms are hereby adopted and incorporated by reference into this rule.~~

(a) ~~(g)~~ These forms are hereby adopted and incorporated by reference into this rule and may be obtained from the Fund's Administrator, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minneapolis, Minnesota 55437.

(b) Companies must submit a detailed claims listing (in a delimited ASCII format) to support the losses reported in the FHCF-L1B, Proof of Loss Report, at the same time it submits its first Proof of Loss Report for a specific Covered Event that qualifies the Company for reimbursement under that Covered Event, and should be prepared to supply a detailed claims listing for any subsequent Proof of Loss Report upon request. Refer to Form FHCF-LAP1 for the required file layout. The Proof of Loss Report and the detailed claims listing are required to be sent to the FHCF Administrator, Paragon Strategic Solutions Inc., at the address listed above. If your Company submits its Proof of Loss Reports electronically through the FHCF's Online Claims System at www.sbafla.com/fhcf, the detailed claims listing may be attached to the Company's submission.

(9) through (10), No changes.

~~(11) Optional Coverage Programs: Except as provided in this subsection, this rule applies to the Additional Coverage Option created in Section 215.555(4)(b)4., F.S., and the Temporary Increase in Coverage Limit Options created in Section 215.555(17), F.S. (TICL). The definition of Premium in paragraph (3)(m), above, does not apply to Section 215.555(4)(b)4., F.S., Additional Coverage Option. With respect to this Option, the word "Premium" when used in this rule shall refer to the amount payable under Section 215.555(4)(b)4., F.S., for this optional coverage.~~

(11) ~~(12)~~ Company Contact Information: Companies must submit Form FHCF C-1, Company Contact Information, as adopted and incorporated into Rule 19-8.029, F.A.C., by June 1 of each Contract Year to the FHCF Administrator, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minneapolis, Minnesota 55437. This form must be updated by the Company as the information provided thereon changes. The

FHCF shall have the right to rely upon the information provided by the Company to the FHCF on this form until receipt by the FHCF of a new properly completed and notarized FHCF C-1 from the Company.

*Rulemaking Authority 215.555(3) FS. Law Implemented 215.555 FS. History–New 5-13-03, Amended 5-19-04, 5-29-05, 5-10-06, 5-8-07, 8-13-07, 6-8-08, 3-30-09, 3-29-10, 8-8-10, 7-20-11, X-X-12.*

NAME OF PERSON ORIGINATING PROPOSED RULE: Jack E. Nicholson, FHCF Chief Operating Officer, State Board of Administration.

NAME OF AGENCY HEAD WHO APPROVED THE PROPOSED RULE: The Trustees of the State Board of Administration of Florida.

DATE PROPOSED RULE APPROVED BY AGENCY HEAD: March 20, 2012.

DATE NOTICE OF PROPOSED RULE DEVELOPMENT PUBLISHED IN FAW: December 22, 2011, Vol. 37, No. 51.

Notice of Meeting/Workshop Hearing

**STATE BOARD OF ADMINISTRATION**

The Florida Hurricane Catastrophe Fund announces a public meeting to which all persons are invited.

DATE AND TIME: March 20, 2012, 9:00 a m. (ET) to conclusion of the meeting.

PLACE: Cabinet Meeting Room, Lower Level, The Capitol, Tallahassee, Florida.

GENERAL SUBJECT MATTER TO BE CONSIDERED: This is a meeting of the Trustees of the State Board of Administration to authorize the Florida Hurricane Catastrophe Fund to file a Notice of Proposed Rule for Rule 19-8.029, F.A.C., Insurer Reporting Requirements and Rule 19-8.030, F.A.C., Insurer Responsibilities, and to authorize filing these two rules for adoption if no member of the public timely requests a rule hearing. In addition, other general business may be addressed. The rules and incorporated forms reflecting the proposed amendments are available on the Florida Hurricane Catastrophe Fund website: www.sbafla.com/fhcf.

A copy of the agenda may be obtained by contacting: Not available.

Pursuant to the provisions of the Americans with Disabilities Act, any person requiring special accommodations to participate in this workshop/meeting is asked to advise the agency at least 7 days before the workshop/meeting by contacting: Tracy Allen, Florida Hurricane Catastrophe Fund, (850) 413-1341, tracy.allen@sbafla.com, P.O. Drawer 13300, Tallahassee, FL 32317-3300. If you are hearing or speech impaired, please contact the agency using the Florida Relay Service, 1(800)955-8771 (TDD) or 1(800)955-8770 (Voice).

**19-8.029 Insurer Reporting Requirements.**

(1) Purpose. The purpose of this rule is to incorporate and adopt the annual reporting of insured values and the Loss Reporting Forms, to provide the time and place for submission of this required information and to address confidentiality of information provided to the Florida Hurricane Catastrophe Fund (FHCF or Fund).

(2) Definitions. The terms defined below will be capitalized in this rule.

(a) Citizens Property Insurance Corporation or Citizens means the entity formed under Section 627.351(6), F.S., and includes both the Coastal~~High Risk~~ Account and the Personal Lines and Commercial Lines Accounts.

(b) Commutation means that period of time which is not less than 36 months or more than 60 months after the end of the Contract Year during which the loss occurrence took place. The Reimbursement Contract, adopted and incorporated into Rule 19-8.010, F.A.C., may provide for voluntary commutation earlier than the 36 month period under certain circumstances.

(c) Contract Year means the time period which begins at 12:00:01 Eastern Time on June 1 of each calendar year and ends at 12:00 p.m. midnight on May 31 of the following calendar year.

(d) Covered Policy is defined in Section 215.555(2)(c), F.S., and in the Reimbursement Contract adopted by and incorporated into Rule 19-8.010, F.A.C.

(e) Data Call or Florida Hurricane Catastrophe Fund Data Call means the annual reporting of insured values ~~forms.~~ form FHCF-D1A.. ~~These forms are the FHCF-D1A for Contract Years after the 2002/2003 Contract Year and the FHCF-D1A and FHCF-D1B for the Contract Year 2002/2003 and all prior Contract Years~~.

(f) FHCF or Fund means the Florida Hurricane Catastrophe Fund.

(g) Independent Consultant means the independent individual, firm, or organization with which the State Board of Administration of Florida (Board) contracts to prepare the premium formula and any other actuarial services for the FHCF, as determined under the contract with the consultant.

(h) Loss Reporting Forms mean the FHCF-L1A and FHCF-L1B. ~~for Contract Years after the 2002/2003 Contract Year and means the FHCF-L1A, FHCF-L1B and FHCF-L1C for the Contract Years 2002/2003 and all prior Contract Years~~.

(i) Office of Insurance Regulation means that office within the Department of Financial Services and which was created in Section 20.121(3), F.S.

(3) Reporting of Insurer Exposure Data.

(a) No later than September 1 of each Contract Year, authorized insurers and Citizens pursuant to Sections 215.555(5) and 627.351(6), F.S., shall report insured values reflecting wind exposure under Covered Policies by zip code and other relevant factors required to reflect each insurer's relative exposure to hurricane loss, valued as of June 30 of the current Contract Year. Such other relevant factors shall be determined by the Independent Consultant consistent with principles of actuarial science and in conjunction with the development of the premium formula.

(b) Confidentiality of reports containing insured values under Covered Policies. Section 215.557, F.S., enacted for the express purpose of protecting trade secret and proprietary information submitted to the FHCF by participating insurers, protects the confidentiality of information of the type submitted in the Data Call ~~(FHCF-D1A)~~, examination workpapers, and examination reports. Such information is not subject to the provisions of Section 119.07(1), F.S., or Section 24(a), Article I of the Florida State Constitution. Confidential data and trade secrets reported to the FHCF are protected to the extent allowed by law.

(c) Reporting Regarding Insurers Withdrawing from the State or Discontinuing the Writing of All Kinds of Insurance Prior to June 30 of Each Year. Insurers which discontinue writing insurance in Florida and have no remaining Covered Policy exposure as of June 30 of each Contract Year are required to petition for exemption from the Fund pursuant to Rule 19-8.012, F.A.C. Insurers which withdraw from the Florida insurance market prior to June 30 and have no remaining Covered Policy exposure as of that date shall not participate in the Fund. The affected insurer shall provide written evidence obtained from the Office of Insurance Regulation that it has surrendered its certificate of authority and currently has no outstanding Covered Policies in force. Nothing in this rule shall be construed to conflict with the requirements of Section 624.430(1), F.S.

(d) The requirement that the report is due by September 1 means that the report shall be in the physical possession of the Fund's Administrator in Minneapolis no later than 5:00 p m., Central Time, on September 1. If September 1 is a Saturday, Sunday or legal holiday, then the applicable due date will be the day immediately following September 1 which is not a Saturday, Sunday or legal holiday. For purposes of the timeliness of the submission, neither the United States Postal Service postmark nor a postage meter date is in any way determinative. Reports sent to the Board in Tallahassee, Florida, will be returned to the sender. Reports not in the

physical possession of the Fund's Administrator by 5:00 p.m., Central Time, on the applicable due date are late.

(4)

~~(a) For the 1999/2000 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 1999 Data Call," rev. 05/99; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 5.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(b) For the 2000/2001 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2000 Data Call," rev. 05/00; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 6.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Florida Hurricane Catastrophe Fund 2000 Data Call for Newly Licensed Companies," rev. 05/00; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 6.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(c) For the 2001/2002 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2001 Data Call," rev. 05/01; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 7.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Florida Hurricane Catastrophe Fund 2001 Data Call for Newly Licensed Companies," rev. 05/01; Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 12/22/94; and the FHCF computer validation software provided on diskette and called "FHCF Preliminary Validation Software Version 7.0," with its instructions. The two forms and the software with its instructions identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(d) For the 2002/2003 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call," rev. 05/02 and Form FHCF-MOD, "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 3/27/01. The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. For new companies, the company shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator on Form FHCF-D1B, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call for Newly Licensed Companies," rev. 05/02; and Form FHCF-MOD "CLASIC DATA FORMAT (tm) for Excess Insurance, Version 1.1," rev. 3/27/01. The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference.~~

~~(e) For the 2003/2004 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2003 Data Call," rev. 05/03 and UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. A new participant shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator. NOTE: Form FHCF-D1B, "Amended Florida Hurricane Catastrophe Fund 2002 Data Call for Newly Licensed Companies," rev. 05/02 used in past years by new participants is no longer being used. The information new participants must submit is now incorporated into Form FHCF-D1A.~~

(a)~~(f)~~ For the 2004/2005 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Amended Florida Hurricane Catastrophe Fund 2004 Data Call," rev. 05/11/04 and UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. A new participant shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(b)~~(g)~~ For the 2005/2006 Contract Year, the reporting shall be in accordance with the following: Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2005 Data Call," rev. 05/05 and "UNICEDE®/PX Data Exchange Format, Version 4.0.0." The two forms identified in the immediately preceding sentence are hereby adopted and incorporated by reference. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(c)~~(h)~~ For the 2006/2007 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2006 Data Call," rev. 05/06, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(d)~~(i)~~ For the 2007/2008 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2007 Data Call," rev. 05/07, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(e)~~(j)~~ For the 2008/2009 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2008 Data Call," rev. 05/08, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(f)~~(k)~~ For the 2009/2010 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2009 Data Call," rev. 05/09, hereby adopted and incorporated by reference. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(g)~~(l)~~ For the 2010/2011 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2010 Data Call," rev. 05/10, hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(h)~~(m)~~ For the 2011/2012 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2011 Data Call," rev. 01/11, http: //www.flrules.org/Gateway/reference.asp?No= Ref-00413, is hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(i) For the 2012/2013 Contract Year, the reporting shall be in accordance with Form FHCF-D1A, "Florida Hurricane Catastrophe Fund 2012 Data Call," rev. 01/12, http: //www flrules.org/Gateway/reference.asp?No= Ref-XXXXX, is hereby adopted and incorporated by reference into this rule. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) below. A new participant writing covered policies on or after June 1 but prior to December 1, shall report its actual exposure as of December 31 of the Contract Year on or before March 1 of the Contract Year, to the Administrator.

(5) Loss Reimbursement Reporting Requirements.

(a) As directed by the Board, after a covered event occurs, insurers shall report all their estimated ultimate net losses (as defined in the Reimbursement Contract, adopted and incorporated into Rule 19-8.010, F.A.C.) for Covered Policies on the Form FHCF-L1A, "Florida Hurricane Catastrophe Fund Interim Loss Report," for the applicable Contract Year, as specified in subsection (7) herein, in no less than fourteen days from the date of the notice from the Board that such a report is required. The Board may request subsequent Interim Loss Reports. To obtain copies of this form, see subsection (6), below. Prompt reporting in the format requested will aid the Board in determining whether to seek additional sources of funds to pay for reimbursable losses. The losses reported on the Interim Loss Report are expected to result from a good faith effort, using best business practices for the insurance industry, on

the part of the insurer to report as accurately as possible. Preliminary reports will not be binding. Reimbursements by the Fund will be made on the basis of the Proof of Loss Report, adopted in subsection (b) below.

(b) Insurers shall report their ultimate net losses ~~(as defined in the Reimbursement Contract, adopted and incorporated into Rule 19-8.010, F.A.C.)~~ for each loss occurrence on the Form FHCF-L1B, "Florida Hurricane Catastrophe Fund Proof of Loss Report," for the applicable Contract Year, as specified in subsection (7) herein. To obtain copies of this form, see subsection (6), below. To qualify for reimbursement, the Proof of Loss Report must have the original signatures of two executive officers authorized by the Company to sign the report. Proof of Loss Reports may be faxed only if the Company does not qualify for a reimbursement. While a Company may submit a Proof of Loss Report requesting reimbursement at any time following a loss occurrence, all Companies shall submit a mandatory Proof of Loss Report for each loss occurrence no earlier than December 1 and no later than December 31 of the Contract Year during which the Covered Event(s) occurs using the most current data available, regardless of the amount of Ultimate Net Loss or the amount of loss reimbursements or advances already received. After the mandatory December Proof of Loss Report, quarterly Proof of Loss Reports are required. For purposes of this rule, quarterly Proof of Loss Reports shall be those reports submitted at each quarter end date after December 31 of the Contract Year in which the loss occurrence occurs and continuing until all claims and losses resulting from loss occurrences commencing during the Contract Year are fully discharged, including any adjustments to such losses due to salvage or other recoveries, in accordance with the reporting requirements in this paragraph. "Fully Discharged" means the earlier of the date on which the insurer has paid its policyholders in full or the commutation clause, in Article X of the Reimbursement Contract~~, adopted in Rule 19-8.010, F.A.C.,~~ takes effect. For the quarterly report due on March 31, any insurer whose losses exceed 50% of its FHCF retention for a specific loss occurrence shall submit a Proof of Loss Report for that loss occurrence. For the quarterly report due on June 30, any insurer whose losses exceed 75% of its FHCF retention for a specific loss occurrence shall submit a Proof of Loss Report for that loss occurrence. For the quarterly reports due on September 30 and thereafter, any insurer which anticipates that its losses will exceed its FHCF retention for a specific loss occurrence shall submit quarterly Proof of Loss Reports until all its losses are paid to its policyholders and the insurer has received reimbursement from the Fund. Annually, all Companies shall submit a mandatory year-end Proof of Loss Report for each loss occurrence, using the most current data available. This Proof of Loss Report shall be filed no earlier than December 1 and no later than December 31 of each year and shall continue until the earlier of the expiration of the commutation period or until all claims and losses resulting from the loss occurrence are fully discharged including any adjustments to such losses due to salvage or other recoveries.

(c) As a result of reports submitted on Form FHCF-L1B, reimbursements to insurers shall be adjusted in accordance with Section 215.555(4)(d)1., F.S., which requires the Fund to pay additional amounts to insurers and insurers to return overpayments to the Fund, based on the most recent calculation of losses.

(6) All the forms adopted and incorporated by reference in this rule may be obtained from: Administrator, Florida Hurricane Catastrophe Fund, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minnesota, MN 55437.

(7)

(a) For the 2005/2006 and earlier Contract Years the applicable Interim Loss Report is that form that was in effect for the Contract Year as reflected by the revision date on the form. For example, the applicable Interim Loss Report for the Contract Year 2004-2005 is the FHCF-L1A, with the revision date of 05/04.

(b) For the 2006/2007 Contract Year, the applicable Interim Loss Report is the "Contract Year 2006 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)", FHCF-L1A, rev. 05/06, which is hereby adopted and incorporated by reference. The applicable Proof of Loss Report is the "Contract Year 2006 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 05/06, which is hereby adopted and incorporated by reference.

(c) For the 2007/2008 Contract Year, the applicable Interim Loss Report is the "Contract Year 2007 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)", FHCF-L1A, rev. 05/07, which is hereby adopted and incorporated by reference. The applicable Proof of Loss Report is the "Contract Year 2007 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev.05/07, which is hereby adopted and incorporated by reference.

(d) For the 2008/2009 Contract Year, the applicable Interim Loss Report is the "Contract Year 2008 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)", FHCF-L1A, rev. 05/08, which is hereby adopted and incorporated by reference. The applicable Proof of Loss Report is the "Contract Year 2008 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 05/08, which is hereby adopted and incorporated by reference. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(e) For the 2009/2010 Contract Year, the applicable Interim Loss Report is the "Contract Year 2009 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)", FHCF-L1A, rev. 05/09, which is hereby adopted and incorporated by reference. The applicable Proof of Loss Report is the "Contract Year 2009 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 05/09, which is hereby adopted and incorporated by reference. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(f) For the 2010/2011 Contract Year, the applicable Interim Loss Report is the "Contract Year 2010 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)", FHCF-L1A, rev. 05/10, which is hereby adopted and incorporated by reference into this rule. The applicable Proof of Loss Report is the "Contract Year 2010 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 05/10, which is hereby adopted and incorporated by reference into this rule. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(g) For the 2011/2012 Contract Year, the applicable Interim Loss Report is the "Contract Year 2011 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1A, rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00415, which is hereby adopted and incorporated by reference into this rule. The applicable Proof of Loss Report is the "Contract Year 2011 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00414, which is hereby adopted and incorporated by reference into this rule. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(h) For the 2012/2013 Contract Year, the applicable Interim Loss Report is the "Contract Year 2012 Interim Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1A, rev. 01/12, http://www.flrules.org/Gateway/reference.asp?No=Ref-XXXXX, which is hereby adopted and incorporated by reference into this rule. The applicable Proof of Loss Report is the "Contract Year 2012 Proof of Loss Report, Florida Hurricane Catastrophe Fund (FHCF)," FHCF-L1B, rev. 01/12, http://www.flrules.org/Gateway/reference.asp?No=Ref-XXXXX, which is hereby adopted and incorporated by reference into this rule. The forms may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

(8) Company Contact Information: Companies must submit Form FHCF C-1, Company Contact Information, rev. 05/10, which is hereby adopted and incorporated by reference into this rule, by June 1 of each Contract Year. This form must be updated by the Company as the information provided thereon changes. The FHCF shall have the right to rely upon the information provided by the Company to the FHCF on this form until receipt by the FHCF of a new properly completed and notarized FHCF C-1 from the Company. The form may be obtained from the Fund's Administrator at the address stated in subsection (6) above.

*Rulemaking Authority 215.555(3) FS. Law Implemented 215.555(2), (3), (4), (5), (6), (7), (15) FS. History–New 5-17-99, Amended 6-19-00, 6-3-01, 6-2-02, 11-12-02, 5-13-03, 5-19-04, 8-29-04, 5-29-05, 5-10-06, 5-8-07, 6-8-08, 3-30-09, 8-2-09, 3-29-10, 8-8-10, 7-20-11, X-X-12.*

**19-8.030 Insurer Responsibilities.**

(1) Section 215.555(10), F.S., provides that any violation of any provision of Section 215.555, F.S., or of any rule adopted under Section 215.555, F.S., constitutes a violation of the Florida Insurance Code.

(2) Purpose. The purpose of this rule is to clearly establish certain deadlines and other requirements for insurers required to participate in the Florida Hurricane Catastrophe Fund (Fund or FHCF). It is not the intent or purpose of this rule to address every requirement of Participating Insurers which could result in a referral to the Florida Department of Financial Services.

(3) Definitions. The terms defined below will be capitalized in this rule.

(a) Authorized Insurer means an insurer as defined in Section 624.09(1), F.S. and includes Citizens Property Insurance Corporation and any joint underwriting association or similar entity created pursuant to Section 627.351, F.S.

(b) Board or SBA means the State Board of Administration of Florida.

(c) Fund or FHCF means the Florida Hurricane Catastrophe Fund established pursuant to Section 215.555, F.S.

(d) Citizens Property Insurance Corporation or Citizens means the entity formed under Section 627.351(6), F.S., and includes both the Coastal~~High Risk~~ Account and the Personal Lines and Commercial Lines Accounts.

(e) Contract Year means the time period which begins at 12:00:01 Eastern Time on June 1 of each calendar year and ends at 12:00 p.m. midnight on May 31 of the following calendar year.

(f) A Covered Event or Event is a hurricane as defined in Section 215.555(2)(b), F.S., and in Article V of the Reimbursement Contract adopted and incorporated by reference in Rule 19-8.010, F.A.C.

(g) Covered Policy. This term is defined in Section 215.555(2)(c), F.S., and the Reimbursement Contract adopted by and incorporated into Rule 19-8.010, F.A.C.

(h) Department means the Florida Department of Financial Services.

(i) Data Call or Florida Hurricane Catastrophe Fund Data Call means the annual reporting of insured values~~ forms.~~ form FHCF-D1A as adopted and incorporated into Rule 19-8.029, F.A.C.~~ These forms, as adopted and incorporated into Rule 19-8.029, F.A.C., are the FHCF-D1A for Contract Years after the 2002/2003 Contract Year and the FHCF-D1A and FHCF-D1B for Contract Year 2002/2003 and all prior Contract Years~~.

(j) Office of Insurance Regulation means that office within the Department of Financial Services and which was created in Section 20.121(3), F.S.

(k) Participating Insurer, Insurer or Company means an insurer which writes Covered Policies in this state and which has entered into a Reimbursement Contract with the Board, pursuant to Section 215.555(4)(a), F.S.

(l) Reimbursement Contract or Contract means the statutorily required annual contract which provides coverage to Participating Insurers for losses to covered property during a Covered Event.

(m) Reimbursement Premium or Premium means the premium determined by multiplying each $1,000 of insured value reported by the Company in accordance with Section 215.555(5), F.S., by the rate as derived from the premium formula as described in Rule 19-8.028, F.A.C.

(n) Quota Share Primary Insurance Arrangement is defined in Section 627.351(6)(c)2.a.(I), F.S.

(4) Reimbursement Contract.

(a) Current Participants: The Reimbursement Contracts are annual contracts.

1. For the 2010/2011 and earlier Contract Years, each Insurer required to participate in the FHCF must designate a coverage level in the annual Reimbursement Contract, make any required selections therein and execute the Reimbursement Contract and applicable Addenda so that the Contract, including the schedules and applicable Addenda, have been received by June 1 of each Contract Year.

2. For the 2011/2012 and subsequent Contract Years, each Insurer required to participate in the FHCF must designate a coverage level in the annual Reimbursement Contract, make any required selections therein and execute the Reimbursement Contract and applicable Addenda so that the Contract, including the schedules and applicable Addenda, have been received by~~ the~~ March 1 prior to each Contract Year.

(b) New Participants during the period of June 1 through November 30: Those Insurers that first begin writing Covered Policies from June 1 through November 30 of a Contract Year are "New Participants." New Participants must designate a coverage level in the annual Reimbursement Contract, make any required selections therein, and execute the Contract and applicable Addenda simultaneously with issuing the first Covered Policy. The completed and executed Reimbursement Contract, including all required selections, schedules and applicable Addenda, must be returned no later than 30 days after the effective date of the first Covered

Policy.

(c) New Participants during the period of December 1 through May 31: Those Insurers that first begin writing Covered Policies from December 1 through May 31 of a Contract Year, along with the Insurers described in paragraph (b) immediately above, are New Participants. However, these Insurers shall not complete and submit the Data Call~~ (Form FHCF-D1A)~~ but shall meet all other requirements for New Participants.

(d) Optional coverages authorized by law must be chosen by current participants by executing and returning the applicable Addenda to the Reimbursement Contract of the relevant Contract Year by the date required. New Participants choosing optional coverage must execute and return the applicable Addenda to the Reimbursement Contract for the relevant Contract Year prior to the time in which a covered loss occurs and within 30 days of writing its first covered policy. Any current or New Participant failing to meet these deadlines shall not be eligible for such optional coverage.

(5) Exposure Reporting Requirements.

(a) Quota Share Primary Insurance: Citizens and Authorized Insurers may enter into Quota Share Primary Insurance Arrangements with respect to the Coastal~~High-Risk~~ Account policies. The statute also provides, in Section 627.351(6)(c)2.a.(II), F.S., that Citizens shall be responsible for the annual reporting of insured values to the FHCF for both Citizens and the Insurer participating with Citizens in the Quota Share Arrangement. Citizens shall report the insured values covered by the Quota Share Primary Insurance Arrangements in the same manner that all other current participants, as described in paragraph (b) below, report their insured values. Please note that both Citizens and the Quota Share Primary Insurer must keep complete and accurate records, including copies of policy declaration pages and supporting claims documents, for the purpose of exposure and loss reimbursement examinations by the FHCF.

(b) Current Participants: Each Insurer, with Covered Policies as of June 1 of a Contract Year must participate in the FHCF and must complete and submit the Data Call~~. The Data Call is incorporated into Rule 19-8.029, F.A.C., and is due~~, correctly completed, no later than September 1 of the Contract Year.

(c) New Participants during the period of June 1 through November 30: Those Insurers that first begin writing Covered Policies from June 1 through November 30 of a Contract Year must complete and submit the Data Call~~. The Data Call is incorporated into Rule 19-8.029, F.A.C., and is due~~, correctly completed, by March 1 of the Contract Year.

(d) Resubmissions of Data: With one exception noted below, any Insurer which submits a Data Call~~, Form FHCF-D1A,~~ with incorrect data, incomplete data, or data in the wrong format and is required to resubmit will be given 30 days from the date on the letter from the FHCF notifying the Insurer of the need to resubmit. An extension of 30 days will be granted if the Insurer can show that the need for the additional time is due to circumstances beyond the reasonable control of the Insurer. Exception: If the Insurer, at the time it receives notice of the need to resubmit, has already been issued a notice of examinations, the usual 30 day time limitation (measured from the date of the letter giving notice of the need to resubmit) does not apply. In this situation, the time period in which the Insurer must resubmit is measured by counting backwards 30 days from the date that the examinations are scheduled to begin as reflected on the notice of examinations letter. The FHCF needs the information prior to the examinations; thus, no extensions can be granted.

(6) Premiums.

(a) Current Participants: Premium installments for Current Participants are due on August 1, October 1, and December 1. Premium adjustments are due as indicated on the invoice sent to the Insurer. Premiums paid to the FHCF with reference to property covered by Quota Share Primary Insurance Arrangements, as authorized and defined in Section 627.351(6)(c)2.a.(I), F.S., will be allocated by the FHCF between the Insurer and Citizens in accordance with the percentages specified in the Quota Share Primary Insurance Arrangement.

(b) New Participants during the period of June 1 through November 30: Those Insurers that first begin writing Covered Policies from June 1 through November 30 of a Contract Year must submit a payment of $1,000 on or before the date indicated on the invoice. Once a New Participant's Data Call, which is filed on or before March 1 of the Contract Year, has been reviewed by the Administrator and the Company's actual Reimbursement Premium has been determined on its actual exposure, an invoice with the amount due, if any, will be sent to the Company by the Administrator. Payment, if any amounts are shown as due on the invoice, is due within 30 days from the date on the invoice. In no event will the Premium be less than the $1,000.

(c) New Participants during the period of December 1 through May 31: Those Insurers that first begin writing Covered Policies from December 1 through May 31 of a Contract Year shall pay a $1,000 Premium within 30 days from the date on the invoice sent to the Insurer by the FHCF.

(d) With respect to any Company where control of the Company has been transferred through any legal or regulatory proceeding to a state regulator or court appointed receiver or rehabilitator, or the Company has been placed under regulatory supervision, prior to December 1 of the Contract Year, the full annual provisional Reimbursement Premium as billed and any outstanding balances will be due on August 1, or the date that control is transferred if after August 1.

(7) Examination Requirements. A Company is required to prepare and retain an examination file in accordance with the specifications outlined in the Data Call instructions and a detailed claims listing to support losses reported on the Proof of Loss Report. Such records must be retained until the FHCF has completed its examination of a Company's exposure submission and any loss reports applicable to the Data Call Contract Year and commutation for the Contract Year (if applicable) has been concluded. The records provided for examination must be from the examination file as originally prepared unless a subsequent resubmission was sent to the FHCF. Note that both Citizens and Insurers participating in Quota Share Primary Insurance Arrangements must keep complete and accurate records, including copies of policy declaration pages and supporting claims documents, for the purpose of exposure and loss reimbursement examinations by the FHCF.

(a) Advance Examination Record Requirements: Within 30 days from the date on the letter from the FHCF, Companies are required to provide the FHCF with the records indicated in the applicable Contract Year's "Exposure Examination Advance Preparation Instructions" or in the applicable Contract Year's "Loss Reimbursement Examination Advance Preparation Instructions". An extension of 30 days may be granted if the Insurer can show that the need for the additional time is due to circumstances beyond the reasonable control of the Insurer.

~~1. For Contract Years prior to the 2003/2004 Contract Year, Form FHCF-AP1 as revised for each Contract Year, is the applicable Exposure Examination Advance Preparation Instructions form to use.~~

1.~~2.~~ For the 2004/2005 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Audit – Contract Year 2004 Advance Preparation Instructions," FHCF-AP1, rev. 5/04. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2004 Advance Preparation Instructions," FHCF-LAP1, 05/06.

2.~~3.~~ For the 2005/2006 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2005 Advance Preparation Instructions," FHCF-AP1, rev. 5/05. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2005 Advance Preparation Instructions," FHCF-LAP1, rev. 05/07.

3.~~4.~~ For the 2006/2007 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2006 Advance Preparation Instructions," FHCF-EAP1, rev. 5/06. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/06.

4.~~5.~~ For the 2007/2008 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2007 Advance Preparation Instructions," FHCF-EAP1, rev. 05/07. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/07.

5.~~6.~~ For the 2008/2009 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2008 Advance Preparation Instructions," FHCF-EAP1, rev. 05/08. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/08.

6.~~7.~~ For the 2009/2010 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2009 Advance Preparation Instructions," FHCF-EAP1, rev. 05/09. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year XXXX Advance Preparation Instructions," FHCF-LAP1, rev. 05/09.

7.~~8~~. For the 2010/2011 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2010 Advance Preparation Instructions," FHCF-EAP1, rev. 05/10. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2010 Advance Preparation Instructions," FHCF-LAP1, rev. 05/10.~~These forms are hereby adopted and incorporated by reference into this rule. Copies of these forms may be obtained from the FHCF website, www.sbafla.com/fhcf or by contacting the State Board of Administration. The mailing address is P. O. Box 13300, Tallahassee, Florida 32317-3300. The~~

~~street address is 1801 Hermitage Blvd., Tallahassee, Florida 32308.~~

8.~~9.~~ For the 2011/2012 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2011 Advance Preparation Instructions," FHCF-EAP1, rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00416. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2011 Advance Preparation Instructions," FHCF-LAP1, rev. 01/11, http://www flrules.org/Gateway/reference.asp?No=Ref-00417.

9. For the 2012/2013 Contract Year, the applicable exposure examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Exposure Examination – Contract Year 2012 Advance Preparation Instructions," FHCF-EAP1, rev. 01/12, http://www flrules.org/Gateway/reference.asp?No=Ref-XXXXX. The applicable loss examination instructions form is the "Florida Hurricane Catastrophe Fund (FHCF) Loss Reimbursement Examination – Contract Year 2012 Advance Preparation Instructions," FHCF-LAP1, rev. 01/12, http://www flrules.org/Gateway/reference.asp?No=Ref-XXXXX.

10. These forms are hereby adopted and incorporated by reference into this rule. Copies of these forms may be obtained from the FHCF website, www.sbafla.com/fhcf or by contacting the State Board of Administration. The mailing address is P. O. Box 13300, Tallahassee, Florida 32317-3300. The street address is 1801 Hermitage Blvd., Tallahassee, Florida 32308.

(b) On-site Examination Record Requirements: The FHCF-EAP1, "Exposure Examination Advance Preparation Instructions" form and the FHCF-LAP1, "Loss Reimbursement Examination Advance Preparation Instructions" form each contain a list of the information that the Companies must have available, on-site, on the date the exposure or loss examination is to begin. These records must be made available to the FHCF examiner upon request.

(c) Response to the FHCF Examination Report: Within 30 days from the date of the letter accompanying the examination report, a Company must provide a written response to the FHCF. The response must indicate whether the Company agrees with the recommendation of the examination report. If the Company disagrees with the examination findings, the reason for the disagreement will be outlined in the response and the Company will provide supporting information to support its objection. An extension of 30 days will be granted if the Company can show that the need for additional time is due to circumstances beyond the reasonable control of the Company.

(d) Resubmissions as a Result of a Completed Examination: A Company required to resubmit exposure data as a result of the examination must do so within 30 days of the date on the letter from the FHCF notifying the Company of the need to resubmit. An extension of 30 days will be granted if the Company can show that the need for additional time is due to circumstances beyond the reasonable control of the Company.

(8) Loss Reporting. Participating Insurers are required to file the following two types of loss reports at the times prescribed in Rule 19-8.029, F.A.C. Form FHCF-L1A, "Florida Hurricane Catastrophe Fund Interim Loss Report," for the applicable Contract Year and Form FHCF-L1B, "Florida Hurricane Catastrophe Fund Proof of Loss Report," for the applicable Contract Year as adopted in Rule 19-8.029, F.A.C.

~~(a) For the Contract Year 2006-2007, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/06 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/06.~~

~~(b) For the Contract Year 2007-2008, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/07 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/07.~~

~~(c) For the Contract Year 2008-2009, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/08 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/08.~~

~~(d) For the Contract Year 2009-2010, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/09 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/09. These forms are hereby adopted and incorporated by reference into this rule.~~

~~(e) For the Contract Year 2010-2011, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 05/10 and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 05/10. These forms are hereby adopted and incorporated by reference into this rule.~~

~~(f) For the Contract Year 2011-2012, the applicable "Florida Hurricane Catastrophe Fund Interim Loss Report," is the FHCF-L1A rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00419, and the applicable "Florida Hurricane Catastrophe Fund Proof of Loss Report," is the FHCF-L1B rev. 01/11, http://www.flrules.org/Gateway/reference.asp?No=Ref-00418. These forms are hereby adopted and incorporated by reference into this rule.~~

(a)~~(g)~~ These forms are hereby adopted and incorporated by reference into this rule and may be obtained from the Fund's

Administrator, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minneapolis, Minnesota 55437.

(b) Companies must submit a detailed claims listing (in a delimited ASCII format) to support the losses reported in the FHCF-L1B, Proof of Loss Report, at the same time it submits its first Proof of Loss Report for a specific Covered Event that qualifies the Company for reimbursement under that Covered Event, and should be prepared to supply a detailed claims listing for any subsequent Proof of Loss Report upon request. Refer to Form FHCF-LAP1 for the required file layout. The Proof of Loss Report and the detailed claims listing are required to be sent to the FHCF Administrator, Paragon Strategic Solutions Inc., at the address listed above. If your Company submits its Proof of Loss Reports electronically through the FHCF's Online Claims System at www.sbafla.com/fhcf, the detailed claims listing may be attached to the Company's submission.

(9) Penalties and Additional Charges. The Participating Insurers' responsibilities outlined in this rule are not an exhaustive list and Section 215.555, F.S., and other rules promulgated under that section may outline additional responsibilities or deadlines. The failure by a Participating Insurer to meet any of the deadlines or responsibilities outlined in this rule, Section 215.555, F.S., or any other rule applicable to the FHCF constitute a violation of the Florida Insurance Code. In the event of a violation, in addition to the consequences outlined below, the FHCF may notify the Office of Insurance Regulation of the violation. The Office of Insurance Regulation may take whatever action it deems appropriate in addressing the violation.

(a) Resubmissions of Data: A $1,000 resubmission fee (for resubmissions that are not the result of an examination by the SBA) will be invoiced by the FHCF for each submission. If a resubmission is necessary as a result of an examination report issued by the SBA, the resubmission fee will be $2,000. If a Company's examination-required resubmission is inadequate and the SBA requires an additional resubmission(s), the resubmission fee for each subsequent resubmission shall be $2,000.

(b) Premiums and Other Payments: All late payments of Premium, including Premium adjustments, due to the FHCF from an Insurer are subject to interest.

(c) Consequences for Failure to meet the requirements contained in the FHCF-EAP1, "Exposure Examination Advance Preparation Instructions," the FHCF-LAP1, "Loss Reimbursement Examination Advance Preparation Instructions," or the on-site examination record requirements in a timely manner: In addition to other penalties or consequences, the FHCF has the authority, pursuant to Section 215.555(4)(f), F.S., to require that the Insurer pay for the following services under the circumstances outlined below:

1. If an examination is delayed, cannot be conducted as scheduled or cannot be completed and the Insurer is responsible for such, the Insurer shall be required to reimburse the FHCF for all the usual and customary expenses connected to such delay, cancellation or incompletion.

2. If the FHCF finds any Insurer's records or other necessary information to be inadequate or inadequately posted, recorded, or maintained, the FHCF may employ experts to reconstruct, rewrite, record, post, or maintain such records or information, at the expense of the Insurer being examined.

3. An Insurer required to reimburse the FHCF for costs as outlined in subparagraphs 1. and 2. immediately above, will owe interest on the amount owed to the FHCF from the date the FHCF pays such expenses until the date payment from the Insurer is received. The applicable interest rate will be the average rate earned by the SBA for the FHCF for the first four months of the current Contract Year plus 5%. Also, the payment of reimbursements or refunds by the FHCF to any Insurer will be offset by any amounts owed by that Insurer to the FHCF.

(10) Time Deadlines: If any deadline provided for herein falls on a Saturday, Sunday or on a legal holiday, then the applicable due date will be the first business day immediately following the Saturday, Sunday or legal holiday.

~~(11) Optional Coverage Programs: Except as provided in this subsection, this rule applies to the Additional Coverage Option created in Section 215.555(4)(b)4., F.S., and the Temporary Increase in Coverage Limit Options created in Section 215.555(17), F.S. (TICL). The definition of Premium in paragraph (3)(m), above, does not apply to Section 215.555(4)(b)4., F.S., Additional Coverage Option. With respect to this Option, the word "Premium" when used in this rule shall refer to the amount payable under Section 215.555(4)(b)4., F.S., for this optional coverage.~~

(11)~~(12)~~ Company Contact Information: Companies must submit Form FHCF C-1, Company Contact Information, as adopted and incorporated into Rule 19-8.029, F.A.C., by June 1 of each Contract Year to the FHCF Administrator, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minneapolis, Minnesota 55437. This form must be updated by the Company as the information provided thereon changes. The FHCF shall have the right to rely upon the information provided by the Company to the FHCF on this form until receipt by the FHCF of a new properly completed and notarized FHCF C-1 from the Company.

*Rulemaking Authority 215.555(3) FS. Law Implemented 215.555 FS. History–New 5-13-03, Amended 5-19-04, 5-29-05, 5-10-06, 5-8-07, 8-13-07, 6-8-08, 3-30-09, 3-29-10, 8-8-10, 7-20-11, X-X-12.*

DRAFT 11/30/11

# Contract Year ~~2011~~2012 Interim Loss Report
# Florida Hurricane Catastrophe Fund (FHCF)

**Company Name:** _____ Co. NAIC No.: _____

Group NAIC No. (if applicable): _____ Losses as of (most current data available): _____

**HURRICANE:** _____ PCS CAT. NO.: _____ Report Due Date (see schedule below): _____

**ESTIMATED ULTIMATE NET LOSSES ON COVERED POLICIES**

| | Commercial-Residential | Residential | Mobile Home | Tenants | Condominium Unit Owners | Total |
|---|---|---|---|---|---|---|
| Paid Loss* | | | | | | |
| Outstanding Loss* | | | | | | |
| IBNR (unknown losses)* | | | | | | |
| TOTAL* | | | | | | |

**Schedule of Report Due Dates**

If the FHCF determines that an Interim Loss Report is required due to the occurrence of a Covered Event, all participants in the FHCF shall be notified of the required filing and the applicable due date (not less than fourteen days from the notice date). The FHCF will notify participants if subsequent Interim Loss Reports are required or if a detailed claims listing (as outlined on the Form FHCF-L1B – Proof of Loss Report) must be provided to the FHCF.

* Report Ultimate Net Losses only. Do not include Loss Adjustment Expenses. If your company has negative IBNR numbers, report the negatives; do not net with the Outstanding Loss numbers. See Article V of the Reimbursement Contract for the definitions of Covered Event, Covered Policy, and Ultimate Net Loss. See Article VI of the Reimbursement Contract for specific coverage exclusions. Copies of this Interim Loss Report, the Reimbursement Contract, and additional information can be found on the Internet at www.sbafla.com/fhcf or http://fhcf.paragon.aonbenfield.com.

Signature: _____ Executive Title: _____ Date: _____

Printed or Typed Name of Executive: _____

DRAFT 11/30/11

# Contract Year ~~2011~~2012 Proof of Loss Report
# Florida Hurricane Catastrophe Fund (FHCF)

**Company Name:** _____ Co. NAIC No.: _____

Group NAIC No. (if applicable): _____ Losses as of (most current data available): _____

HURRICANE: _____ PCS CAT. NO.: _____ Report Due Date: _____

**SECTION I - MANDATORY** **ULTIMATE NET LOSSES ON COVERED POLICIES**

| | Commercial-Residential | Residential | Mobile Home | Tenants | Condominium Unit Owners | Total |
|---|---|---|---|---|---|---|
| A. Paid Loss* | | | | | | |
| B. Outstanding Loss* | | | | | | |
| C. IBNR (unknown losses)* | | | | | | |
| D. TOTAL* | | | | | | |

* Report Ultimate Net Losses only. Do not include Loss Adjustment Expenses. If your company has negative IBNR numbers, report the negatives; do not net with the Outstanding Loss numbers. See Article V of the Reimbursement Contract for the definitions of Covered Event, Covered Policy, and Ultimate Net Loss. See Article VI of the Reimbursement Contract for specific coverage exclusions. Copies of this Proof of Loss Report, the Reimbursement Contract, and additional information can be found on the Internet at www.sbafla.com/fhcf or http://fhcf.paragon.aonbenfield.com.

**SECTION II - OPTIONAL** **ESTIMATED RECOVERABLE FROM THE FHCF** ~~(excluding reimbursements under 215.555(4)(b)4., F.S)~~

Section II is provided for your Company's use only. The FHCF will calculate loss reimbursements based on the information provided under Section I above.

| | | Incurred Basis |
|---|---|---|
| A. Incurred Ultimate Net Loss | (Sec. I.D.) | |
| B. Less Actual Retention | | |
| C. Subtotal (minimum of -0-) | (A - B) | |
| D. Elected Coverage Percentage | | |
| E. Ultimate Net Loss Excess Retention | (C x D) | |
| F. LAE (5% of Incurred Losses in Excess of Retention) | (E x 5%) | |
| G. Estimated Recoverable from the FHCF on Incurred Basis** | (E + F) | |

| | | Paid Basis |
|---|---|---|
| A. Paid Ultimate Net Loss | (Sec. I.A) | |
| B. Less Actual Retention | | |
| C. Subtotal (minimum of -0-) | (A – B) | |
| D. Elected Coverage Percentage | | |
| E. Ultimate Net Loss Excess of Retention | (C x D) | |
| F. LAE (5% of Paid Losses in Excess of Retention) | (E x 5%) | |
| G. Total Estimated Recoverable | (E + F) | |
| H. Previous Reimbursements | | |
| I. Estimated Recoverable from the FHCF this request** | (G – H) | |

***Estimated recoverables are limited by your Company's share of the claims paying capacity of the FHCF, as limited pursuant to Sections 215.555(4)(c)~~, (16)~~ and (17), Florida Statutes.*

**Company Name:** _____ **Hurricane:** _____

**SECTION III - MANDATORY** **SIGNATURES**

*~~The~~We, the undersigned, ~~does hereby confirm that all losses~~ do state that, to the best of our knowledge, all data reported under Section I of this Proof of Loss Report ~~are~~ is accurate and is for losses under FHCF Covered Policies ~~and have been~~ incurred by the named Company (Company) for the named hurricane. All reported information is subject to examination by the State Board of Administration of Florida (SBA). We are each, respectively, executive officers of the Company, acting within our authority in making this declaration, and we have conducted, or have had conducted, a thorough review of the Company's records and systems to determine the truth of this statement.*

Signature: _____ Executive Title: _____ Date: _____

Printed or Typed Name of Executive: _____

Signature: _____ Executive Title: _____ Date: _____

Printed or Typed Name of Executive: _____

## RECORDS RETENTION REQUIREMENTS

Companies reporting losses and receiving reimbursements or advances from the FHCF for paid losses from Covered Events are subject to examination by the FHCF or its agents pursuant to the Reimbursement Contract entered into between the Company and the FHCF. Therefore, all Companies shall retain complete and accurate records of all losses paid by the FHCF until the FHCF has completed its examination of the Company and commutation for the Contract Year (if applicable) has been concluded. All records, including Form FHCF-L1B (Proof of Loss Report), correspondence, and supporting documentation, must be available with computer runs produced containing the information below. Upon notice of an examination, the Company will be required to provide the following information along with the information outlined in Form FHCF-LAP1 "Loss Reimbursement Examination Advance Preparation Instructions" for the applicable Contract Year.

1. **Detailed claims listing which supports the losses reported on the Proof of Loss Report including:**
   - Claim number
   - Date of loss
   - Policy number
   - Policy effective date
   - FHCF type of business code
   - County code
   - County name
   - ZIP Code
   - Paid loss – habitational building
   - Paid loss – appurtenant structure
   - Paid loss – contents
   - Paid loss – additional living expense
   - Outstanding loss reserve
2. **Claim files which include documentation of the following:**
   - First notice of loss
   - Claim number
   - Date of loss
   - Amount of loss for each category of coverage (building, appurtenant structure, contents, and additional living expense)
   - Claim description
   - Documentation of policyholder's legal fees and/or public adjuster fees paid, if provided to the Company
   - Payment history
   - Policy number and location of property
   - Amount of loss adjustment expense
   - Copies of checks for payment of losses
   - All adjuster estimates, including public adjuster estimates if provided to the Company
   - Evidence of salvage received
   - Evidence of whether the deductible was applied
   - Receipts for any additional living expenses paid
   - Evidence to show the loss was a direct result of a hurricane
3. **Detailed exposure listing, which was retained at the time the exposure data was submitted to the FHCF, for the Contract Year the loss occurred. See the SBA Exam File specifications section of the Data Call applicable to the Contract Year the loss occurred.**
4. **Additional detail on the loss examination requirements can be accessed on the Internet at www.sbafla.com/fhcf.**

NOTE: Companies must submit a detailed claims listing to support the losses reported in the Proof of Loss Report at the same time it submits its first Proof of Loss Report for a specific Covered Event that qualifies the company for reimbursement under that Covered Event, and should be prepared to supply a detailed claims listing for any subsequent Proof of Loss Report upon request. Refer to Form FHCF-LAP1 for the required file layout. The Proof of Loss Reports and the detailed claims listing are required to be sent to the FHCF Administrator, Paragon Strategic Solutions Inc., 8200 Tower, 5600 West 83rd Street, Suite 1100, Minneapolis, MN 55437. If your Company submits its Proof of Loss Reports electronically through the FHCF's Online Claims System at www.sbafla.com/fhcf, the detailed claims listing must be attached in an ASCII format.

**DRAFT 11/30/11**

# FLORIDA HURRICANE CATASTROPHE FUND (FHCF) EXPOSURE EXAMINATION – CONTRACT YEAR 201~~2~~1 ADVANCE PREPARATION INSTRUCTIONS

**Company:**
**Date of Examination:**
**Advance Records Due:**

The following instructions are provided to help your Company prepare for the FHCF's examination. If you have questions pertaining to the preparation and submission of required records, or about the activities or work processes of the examiner which cannot be adequately answered by the examiner, please call Gina T. Wilson, Director of Examinations, at (850) 413-1348.

Please note: If your Company participated in a takeout pursuant to an assumption agreement with Citizens Property Insurance Corporation or the examination is for Citizens Property Insurance Corporation ~~High Risk~~ Coastal Account with quota share primary insurance data, additional instructions apply (see pages 5 and 6).

## ADVANCE RECORDS

Your company is required to submit records to the FHCF in advance of the examiner's on-site review to allow the examiner to fully prepare and to ensure the examination begins as scheduled.

All advance records must be provided on a CD-ROM that is labeled with the Company name and contract year. Be sure to check your CD-ROM to be certain the files were saved and can be opened. A cover letter is not required; however, if there is any information related to the data or the exam that you would like the examiner to know, it can be noted in a cover letter. If more than one company is under examination, preparation of separate data for each company is necessary. If your Company has different departments responsible for compiling portions of your data submission, please have one individual coordinate, compile, and submit the complete package to the FHCF.

### 1. REQUIRED RECORDS CHECKLIST

The Checklist, provided as an attachment in the Notice email, should be completed by the C~~c~~ompany to ensure that all advance records are submitted to the FHCF and should be returned to the FHCF in electronic form with the remainder of the required advance records. Do not use versions from a prior examination. Using the drop-down options located to the right of the list of required records, the ~~c~~Company should indicate whether each of the records is included, not included, or not applicable. The ~~c~~Company should also designate the office location where the on-site examination should take place and provide complete contact information of a Company Coordinator and a C~~c~~ompany ~~e~~Executive. All examination correspondence will be directed through the Company Coordinator you have designated, including the Examination Report, unless otherwise noted on the checklist (the FHCF will only send one printed copy of the Report). The Company Coordinator will be contacted periodically by FHCF staff and the examiner to

help guide the Company in the preparation of information needed to expedite the examination.

## 2. OPERATIONS QUESTIONNAIRE

The electronic questionnaire form should be completed in its entirety and submitted to the FHCF in electronic form. Questions should be answered based on covered policies in force for the contract year being examined. The individual(s) responsible for preparing the questionnaire should be available to answer questions once the examiner arrives on-site.

## 3. FORMS AND ENDORSEMENTS

Your Company must provide a list of all forms and endorsements used (as of the Data Call date) for all covered and reported policies, as well as a specimen copy of each form. The list must include the form and endorsement numbers and titles.

## 4. LIST OF COMPANY CONSTRUCTION TYPES

Your Company must provide a list of company construction types with a definition for each type and the applicable FHCF code used to report each construction.

## 5. DEFINITION OF WINDSTORM MITIGATION FEATURES

Your Company must provide a list of windstorm mitigation features reported to the FHCF for structure opening protection and roof shape, along with a definition for each feature and the applicable FHCF code the feature is mapped to.

## 6. EXAM FILE/EXPOSURE DATA

Your Company is required to submit its Exam File produced and retained in accordance with the specifications given in the Data Call for the current contract year. The Exam File must match the Company's Data Call File submitted to the FHCF Administrator and must be submitted as originally prepared unless a subsequent resubmission was sent to the FHCF. If your Company failed to retain the Exam File, you should immediately contact the FHCF staff for further instructions.

The Exam File must be submitted as one report and be by individual policy, sorted by type of business and line of business. It must be provided in a Microsoft Access database or in delimited ASCII (text) format. The Exam File may not include symbols such as -, +, #, $, ", / and must contain the following fields in the order listed in the table below.

| Field # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Type of Business | Numeric | Only use the codes on pg xx~~8~~ FHCF Data Call |
| 2 | Line of Business | Numeric | Only use the codes on pg xx~~9~~ FHCF Data Call |
| 3 | Construction Type | Numeric | Only use the codes on pgs xx ~~9-10~~ FHCF Data Call |
| 4 | Deductible Group | Text | Only use the codes on pgs xx~~10-11~~ FHCF Data Call |
| 5 | County Code | Numeric | Only use the codes on pg xx~~27~~ FHCF Data Call |
| 6 | ZIP Code | Numeric | |
| 7 | Insured Risks | Numeric | Must be greater than zero |
| 8 | Total Insured Value – Building | Numeric | |
| 9 | Total Insured Value – Appurtenant Structures | Numeric | |
| 10 | Total Insured Value – Contents | Numeric | |
| 11 | Total Insured Value – Additional Living Expenses | Numeric | |

| | | | |
|---|---|---|---|
| 12 | Year Built | Numeric | Only use the codes on pg xx~~14~~ FHCF Data Call |
| ~~13~~ | ~~BCEG Code~~ Reserved for future use | Numeric | ~~Only use the codes on pg 14 FHCF Data Call~~ Enter 00 (two zeros) |
| ~~14~~ | ~~Florida Building Code Indicator~~ Reserved for future use | Numeric | ~~Only use the codes on pg 15 FHCF Data Call~~ Enter 0 (zero) |
| 15 | Structure Opening Protection | Numeric | Only use the codes on pg xx~~15~~ FHCF Data Call |
| 16 | Roof Shape | Numeric | Only use the codes on pg xx~~15~~ FHCF Data Call |
| 17 | Reserved for future use | Numeric | Enter 0 (zero) |
| 18 | Reserved for future use | Numeric | Enter 0 (zero) |
| 19 | Policy Effective Date | Numeric or Date/Time | Numeric Format: yyyymmdd<br>Date/Time Format: month/day/year<br>Effective Date must be in one field and the numeric format must have 8 characters |
| 20 | Policy Expiration Date | Numeric or Date/ Time | Numeric Format: yyyymmdd<br>Date/Time Format: month/day/year<br>Expiration Date must be in one field and the numeric format must have 8 characters |
| 21 | Policy Number | Text | |
| 22 | Citizens Policy Number* | Text | *Applies only to policies assumed from Citizens that have not renewed onto the company's books by June 30, 2012~~1~~. |

## 7. DIRECT WRITTEN PREMIUM REPORT

Your Company must provide (1) a copy of the annual statement page with the direct written premiums for Florida and (2) a report which supports your Company's total direct written premium for all lines where any policy or coverage subject to the FHCF may be written. Both documents must be provided for the period ending December 31, 2011~~0~~. Although the direct written premiums for a line of business may include policies covered and policies not covered by the FHCF, the Direct Written Premium Report must include all policies needed to reconcile to the line item total on the annual statement. It would be helpful to include a notation on the report, which distinguishes ex-wind policies from wind policies. Also, if there are any reconciling entries made to the annual statement, enclose a schedule detailing the reconciling items.

The Direct Written Premium Report must be by individual policy, sorted by type and line of business, must be provided as a Microsoft Access database or in a delimited ASCII (text) format, and must contain the fields in the order listed in the table below. **Policy numbers in the Exam File and Direct Written Premium Report must be formatted alike. If not, an explanation on how to match the policies is required.**

| # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Type of Business | Numeric | Only use the codes on pg xx ~~8~~ FHCF Data Call |
| 2 | Line of Business | Numeric | Only use the codes on pg xx~~9~~ FHCF Data Call |
| 3 | Policy Effective Date | Numeric or Date/Time | Numeric Format: yyyymmdd<br>Date/Time Format: month/day/year<br>Effective Date must be in one field and the numeric format must have 8 characters |
| 4 | Policy Expiration Date | Numeric or Date/Time | Numeric Format: yyyymmdd<br>Date/Time Format: month/day/year<br>Expiration Date must be in one field and the numeric format must have 8 characters |
| 5 | Direct Written Premium | Numeric | |
| 6 | Policy Number | Text | Use the same policy number and format as used in the Exam File |
| 7 | Notation Designating FHCF Covered Policies | Text | If available |

| | | | |
|---|---|---|---|
| 8 | Notation Designating Policy Written with Ex-wind Endorsement | Text | If available |
| 9 | Notation Designating Policy has Endorsement for Scheduled Personal Property | Text | If applicable |
| 10 | Class Code | Numeric | If applicable (typically applies to Commercial policies only) |

For Commercial Multiple Peril, only include policies with premium reported under line 5.1. **DO NOT INCLUDE POLICIES REPORTED UNDER LINE 5.2**.

**Also, if your Company writes Inland Marine endorsements to covered policies and the premium from these policies is included under a line of business other than Line 9 for Inland Marine, provide a separate listing for this premium. Also, be sure to provide separate listings for lines of business that include premiums for both commercial and residential policies.**

## ON-SITE REQUIREMENTS

In order for the examiner to properly conduct and expedite an early conclusion of the Exposure Examination, the Company Coordinator should ensure that the examiner has access to the following:

### 1. EQUIPMENT AND SPACE

The examiner will need a private working space, dedicated telephone line and telephone, and an internet connection.

### 2. COMPANY PERSONNEL

The Company Coordinator may wish to provide names of persons whom the examiner can contact directly for answers to the many questions the examination generates. In addition, the individual(s) responsible for preparing the Operations Questionnaire should be available to answer questions once the examiner arrives on-site.

### 3. REQUIRED RECORDS TO HAVE AVAILABLE ON-SITE

The examiner will also be requesting applications and declaration pages to be available for review on-site. If policy files are in more than one location, your Company is responsible for coordinating the retrieval of the files to one central location. The files must contain at least the following information:

a. Insured's Name
b. Address and ZIP Code for location of property insured
c. Policy Number
d. Policy Period
e. Construction Type
f. Deductible Group
g. County Code
h. Total Insured Values
i. Year Built
~~j. Building Code Effectiveness Grading Code (BCEG)~~
~~k~~j. Evidence to support the reported roof shape code
~~l~~k. Evidence to show a credit is given to the policyholder for structure opening protection

~~m.~~ l. A copy of the Residential Property Insurance Checklist required by the Office of Insurance Regulation Rule 69O-167.013, F.A.C. (This requirement applies to homeowners', mobile homeowners', dwelling or condominium unit owners' policies)
~~n.~~m. All applicable endorsements and policy changes

Online policy files may be acceptable for the review of residential lines of business if the items listed above are viewable on the online system, if the system is the same system that produces the Company's dec pages, and if the examiner determines the system information is reliable. If the examiner determines the online system cannot be used for policy review, then your Company must provide the physical policy files including the applications and underwriting files.

**For review of commercial policies, the complete policy files, including underwriting files, applications, commercial class codes, and statement of values are required.**

### 4. ADDITIONAL ON-SITE REQUIREMENTS

a. A copy of your Company's underwriting manual and rating manual for policies covered by the FHCF and the name of a contact that is familiar with these manuals.
b. If your Company writes policies covering single structures that contain a mix of both commercial and habitational exposure, your Company is required to submit a classification plan to the FHCF Administrator before the September 1st deadline. Be certain an individual familiar with your Company's class codes is available to answer questions before and during the examination. Also, your Company must be able to identify policies insuring single structures that contain a mix of both commercial and habitational exposure for examination purposes.
c. If your Company's reported exposure includes collateral protection policies covered by the FHCF, a copy of the lapsed homeowner's policy or the equivalent of a dec page must be available for the examiner's review in addition to the dec page for the policy in force at June 30, 2012~~1~~.

## SPECIAL EXAMS RELATED TO ASSUMPTIONS AND QUOTA SHARE AGREEMENTS WITH CITIZENS PROPERTY INSURANCE CORPORATION (CITIZENS)

### 1. CITIZENS TAKEOUTS PURSUANT TO ASSUMPTION AGREEMENTS

**a. Requirements for Assuming Companies:**

If your Company was engaged in an assumption agreement with Citizens~~ High Risk~~ Coastal Account and/or Citizens Personal Lines and Commercial Lines Accounts, a separate Exam File should be submitted. One file must contain your Company's FHCF exposure from direct written premiums. The exposure assumed from either Citizens entity which is renewed by June 30, 2012~~1~~ must be included with the direct portion. The other file(s) must contain the FHCF exposure which was assumed from each Citizens entity (one file for each entity) and which was not renewed onto your Company's book by June 30, 2012~~1~~.

**b. Requirements for each Citizens entity engaged in an assumption:**

In addition to the Exam File for all of its FHCF exposure not subject to an assumption agreement, each Citizens entity shall submit the following information for each assumption occurring July 1, 2011~~0~~ through June 30, 2012~~1~~:

1. A separate file that includes a list of all policies that were assumed by each company on the date of the assumption. This file must include the policy number, policy written premium, and policy effective/expiration date.
2. A separate listing of all assumed policies with indicators that identify policies with no wind coverage and cancellations (June 30 monthly extract).
3. A separate file for all FHCF exposure removed from the applicable Citizens entity, which, as of June 30, 2012~~1~~, had not been renewed onto the assuming company's policy forms. This file must be prepared with the Exam File specifications outlined in the Contract Year 2012~~1~~ Data Call.
4. A copy of the assumption agreement between Citizens and the assuming company along with copies of exhibits to show the number of policies assumed.

## 2. CITIZENS~~ HIGH RISK~~COASTAL ACCOUNT – QUOTA SHARE PRIMARY INSURANCE REPORTING REQUIREMENTS

Citizens~~ High Risk~~ Coastal Account shall report all quota share primary insurance exposure data to the FHCF in a separate file, meeting the requirements on page ~~24~~ xx of the Contract Year 2012~~1~~ Data Call. This file is to contain all of the fields in the Exam File specifications and the following two additional fields:

- Field #23: Five-character field indicating NAIC# of insurer for each policy reported, and
- Field #24: Two-character field indicating Citizens' specified percentage of hurricane coverage of the risks reported in a specific record, as set forth in the quota share primary insurance agreement between Citizens and an insurer.

For those policies under a Quota Share Primary Insurance Agreement, Citizens and each participating insurer are required to maintain duplicate copies of policy declaration pages. After receiving a notice for examination, Citizens must have a copy of the following information available on-site:

a. The all-perils policy issued by the insurer for each policy under the Quota Share Primary Insurance Agreement
b. Each endorsement attached to the all-perils policies that shows the specified percentage of participation by Citizens and the insurer under the Quota Share Primary Insurance Agreement
c. The Quota Share Primary Insurance Agreement

**All records, including exposure filings (Data Call File and Exam File), policy files, and supporting documentation must be retained along with any information produced to support the Data Call submission. Such records must be retained until the FHCF has completed its examination of your Company's exposure submission and claims reports (applicable to the Data Call Contract Year) and commutation for the Contract Year (if applicable) has been concluded.**

**DRAFT 12/5/11**

# FLORIDA HURRICANE CATASTROPHE FUND (FHCF)
# LOSS REIMBURSEMENT EXAMINATION – CONTRACT YEAR 2012~~1~~
# ADVANCE PREPARATION INSTRUCTIONS

**Company:**
**Date Examination Scheduled:**
**Date Required Records Due:**
**Events:** **(Event Name) – Proof of Loss Report with losses as of:**
**(Event Name) – Proof of Loss Report with losses as of:**
**(Event Name) – Proof of Loss Report with losses as of:**

In order for the examiner to properly conduct and expedite an early conclusion of the Loss Reimbursement Examination, please follow the guidelines below. If more than one company is under examination, preparation of separate data for each company is necessary. If more than one contract year is scheduled for examination, preparation and submission of separate data for each contract year is necessary.

**(1) Company Coordinator:**

All correspondence will be directed through the Company Coordinator you have designated. The Company Coordinator will be contacted periodically by FHCF staff and the examiner to ensure proper receipt of records and to help guide the Company Coordinator in the preparation of information needed to expedite the examination. Your Company Coordinator may wish to provide the names of people whom the examiner can directly contact for answers to the many questions the examination generates. Please remember that if you do not understand what we need, feel free to ask questions.

**(2) Equipment and Space:**

The examiner will need a private working space, dedicated telephone line and telephone, and an internet connection.

**(3) Work Processes**:

If, at any time, you have questions about the activities or work processes of the examiner, which cannot be adequately answered by the examiner, please call Gina T. Wilson, Director of Examinations, at 850-413-1348.

**(4) Required Records:**

**A. Required Records to be submitted to the FHCF in advance:**

**Claims Process Memo**

Provide a written narrative of your Company's hurricane claims paying process. The narrative should start with how a claim is originated to the time a~~the~~ claim is paid. Please indicate the name and title of primary employees with responsibilities in the process.

## Detailed Claims Listing(s)

Your Company is required to maintain records of all losses paid by the FHCF until the FHCF has completed its examination of the Company and commutation for the Contract Year (if applicable) has been concluded. The records retention requirement, as stipulated in the Proof of Loss Report, page 2, requires the Company to maintain all records, including the Proof of Loss Report, correspondence and supporting documentation to support the losses reported to the FHCF.

The Detailed Claims Listing, which supports the losses reported in the Proof of Loss Report(s), by hurricane, must match the aggregate total amounts for paid losses and outstanding losses reported on page 1 of the Proof of Loss Report. The Detailed Claims Listing must be provided as a Microsoft Access database or in a fixed-width ASCII (text) format, and contain the following fields (do not include symbols, such as, -, +, #, $,", /) in the order listed. Please note: Policy numbers in the Detailed Claims Listing must be in the same format as policy numbers provided in the Exposure Exam File.

| FIELD # | DESCRIPTION | POSITION | LENGTH | TYPE | NOTES |
|---|---|---|---|---|---|
| 1 | Claim Number | 1 | 20 | Text | Only numbers and letters are acceptable |
| 2 | Date of Loss | 21 | 8 | Text | mmddyyyy |
| 3 | Policy Number | 29 | 30 | Text | Only numbers and letters are acceptable and must match the policy numbers and format provided in the 2012~~1~~ Exposure Exam File for policies required to be reported at 6/30/12~~1~~ |
| 4 | Policy Effective Date | 59 | 8 | Text | mmddyyyy |
| 5 | FHCF Type of Business Code | 67 | 1 | Text | Only use the codes on pg x of the Contract Year 2012~~1~~ FHCF Data Call |
| 6 | County Code | 68 | 3 | Text | Only use the codes on pg xx of the Contract Year 2012~~1~~ FHCF Data Call |
| 7 | County Name | 71 | 20 | Text | All capital letters |
| 8 | ZIP Code | 91 | 5 | Text | |
| 9 | Paid Loss – Habitational Building* | 96 | 12 | Text | Enter zeros if none |
| 10 | Paid Loss – Appurtenant Structures * | 108 | 12 | Text | Enter zeros if none |
| 11 | Paid Loss – Contents * | 120 | 12 | Text | Enter zeros if none |
| 12 | Paid Loss – Additional Living Expense * | 132 | 12 | Text | Enter zeros if none |
| 13 | Outstanding Loss Reserve | 144 | 12 | Text | Enter zeros if none |

*** A breakdown of paid losses is required.**

**Example:** A record with the following information:

| FIELD # | DESCRIPTION | TYPE | ENTRY |
|---|---|---|---|
| 1 | Claim Number | | 336733 |
| 2 | Date of Loss | | 09102012~~1~~ |
| 3 | Policy Number | | HCP5670996 |
| 4 | Policy Effective Date | | 02152012~~1~~ |
| 5 | FHCF Type of Business Code | Residential | 2 |
| 6 | County Code | | 049 |
| 7 | County Name | | HARDEE |
| 8 | ZIP Code | | 33890 |
| 9 | Paid Loss – Habitational Building | | 12100 |
| 10 | Paid Loss – Appurtenant Structures | | 3600 |
| 11 | Paid Loss – Contents | | 8000 |
| 12 | Paid Loss – Additional Living Expense | | 1500 |
| 13 | Outstanding Loss Reserve | | 5000 |

Sample record layout:

0000000000000033673309102012~~1~~0000000000000000000HCP5670996021520121~~1~~204
900000000000000HARDEE338900000000121000000000036000000000080000000000
01500000000005000

Each record must have this type of layout. Since each field has a defined length, please "zero fill" the position in each field that will not be used. Each record must be 155 characters in length.

**Provide a separate Detailed Claims Listing to support the Proof of Loss Report(s) for each event listed on the first page of these instructions.** If your company is unable to provide a Detailed Claims Listing that matches the losses reported in the Proof of Loss Report(s), you should immediately contact the FHCF staff for further instructions.

## Incurred But Not Reported (IBNR)

In addition to the Detailed Claims Listing(s), your company is required to submit documentation to support the amount of IBNR reported for each Proof of Loss Report and event listed above.

## List of Claims with Salvage

The Company is required to provide a listing of all FHCF covered claims where salvage was received. This listing must be provided as a Microsoft Access database or in a delimited ASCII (text) format.

The listing must contain a single record for each policy with the following information:

| FIELD # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Claim Number | Text | |
| 2 | Policy Number | Text | |
| 3 | Salvage Received | Text | |

## Multi-State Policy Listing

The Company is required to provide a listing of all FHCF covered commercial policies in effect during the 2012~~1~~ hurricane season that have exposures written with Florida and non-Florida locations on the same policy. This list includes all policies regardless of whether or not a claim was reported to the FHCF for the policy and must be provided as a Microsoft Access database or in a delimited ASCII (text) format.

The listing must contain a single record for each policy with the following information:

| FIELD # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Policy Number | Text | Only numbers and letters are acceptable and must match the policy numbers and format provided in the 2012~~1~~ Exposure Exam File, if the policy was required to be reported |
| 2 | FHCF Type of Business Code | Text | Only use the codes on pg x of the 2012~~1~~ FHCF Data Call |

## Multi-Risk Policy Listing

The Company is required to provide a listing of all FHCF covered commercial policies in effect during the 2012~~1~~ hurricane season that have both covered and non-covered risks written on the same policy. This list includes all policies regardless of whether or not a claim was reported for the policy and must be provided as a Microsoft Access database or in a delimited ASCII (text) format.

The listing must contain a single record for each policy with the following information:

| FIELD # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Policy Number | Text | Only numbers and letters are acceptable and must match the policy numbers and format provided in the 2012~~1~~ Exposure Exam File, if the policy was required to be reported |
| 2 | FHCF Type of Business Code | Text | Only use the codes on pg x of the 2012~~1~~ FHCF Data Call |

## Single Structures Policy Listing

The Company is required to provide a listing of all FHCF covered policies in effect during the 2012~~1~~ hurricane season that insure single structure(s) that are used for both habitational and non-habitational purposes. This listing includes all policies regardless of

whether or not a claim was reported for the policy and must be provided as a Microsoft Access database or in a delimited ASCII (text) format.

The listing must contain a single record for each policy with the following information:

| FIELD # | DESCRIPTION | TYPE | NOTES |
|---|---|---|---|
| 1 | Policy Number | Text | Only numbers and letters are acceptable and must match the policy numbers and format provided in the 2012~~1~~ Exposure Exam File, if the policy was required to be reported |
| 2 | FHCF Type of Business Code | Text | Only use the codes on pg x of the 2012~~1~~ FHCF Data Call |
| 3 | Class Code | Text | Only numbers and letters are acceptable |

## Required Records Checklist and Operations Questionnaire

In addition to the records outlined above, attached are a Required Records Checklist and a Claims Operations Questionnaire that should be prepared electronically and submitted to the FHCF in advance. The individual responsible for preparing the questionnaire should be available to answer questions once the examiner arrives on site.

## Remittance of Required Documents

The reports must be provided on a CD-ROM that is labeled with the Company name, contract year, hurricane(s) and file name. Save each Detailed Claims Listing with the name applicable to each hurricane. Be sure to check your CD-ROM to be certain the files were saved and can be opened.

### B. Required Records to Have Available On Site:

The examiner will also be requesting claims and policy files, based on the sample selection, to be available once the examiner arrives on site. The claims and policy files can be provided either in electronic or hard copy format. The files should be made available upon request and should contain at least the following information:

**Claim File (the complete file)**

a. First notice of loss
b. Claim n~~N~~umber
c. Date of l~~L~~oss
d. Amount of loss for each category of coverage (building, appurtenant structure, contents, and additional living expense)
e. Claim description
f. Policy n~~N~~umber and location of property
g. Amount of loss adjustment expense
h. Copies of checks for payment of losses
i. All adjuster's estimates, including Public Adjuster estimates if provided to the Company
j. Payment history
k. Evidence of salvage received, if any
l. Evidence of whether the deductible was applied

m. Receipts for any additional living expenses paid
n. Evidence to show the loss was a direct result of a hurricane
o. Documentation of policyholder's legal fees and/or Public Adjuster fees paid, if provided to the Company

**Policy File (the complete file in effect at the time of loss)**

a. Policy Declarations
b. Insured's Name
c. Address and ZIP Code for location of property insured
d. Policy Number
e. Policy Period
f. Construction Type
g. Deductible Group
h. County Code
i. County Name
j. Total Insured Values
k. Evidence to support occupancy is primary or secondary residence
l. All applicable forms, endorsements, and policy changes/transactional history

If your Company retains claims and/or policy files on an on-line system, this will be acceptable for the review of residential lines of business as long as the items listed above are available on that system and the examiner determines the system information can be relied on. If the examiner determines the on-line system cannot be used for policy review, then the examiner will need policy files including the application and underwriting files for the specific policies being reviewed. Also, if the Company's on-line system is not the same system that produces the Company's dec pages, then the actual files will need to be provided to the examiner.

**For any commercial policies reviewed, you are required to provide the complete policy file, underwriting file, application, commercial class codes, and statement of values**.

**(5) Additional Requirements:**

The Company may be required to provide a walk through of the claims process once the examiner arrives on site. The examiner will coordinate with the Company prior to arriving on site and provide directions on performing the walk through. The Company should make prior arrangements for the examiner to conduct this walk through with the necessary personnel. Be certain an individual familiar with the Company's claims process is available to answer questions before and during the examination.

If claims and/or policy files are in more than one location, your Company is responsible for coordinating the retrieval of the files to one central location.

Also, provide the examiner with a copy of the claims manual for claims covered by the FHCF and the name of a contact familiar with this manual. It is preferable that the claims manual be provided in electronic format.

**DRAFT 12/5/11**

**Note: Page number references will be updated when changes are accepted.**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Instruction Sheet

Each authorized insurance company writing Covered Policies in the state of Florida is required to pay a reimbursement premium to the Florida Hurricane Catastrophe Fund (FHCF). This premium is based on the Reimbursement Premium Formula specifying the amount of premium to be paid for each $1,000 of insured value for Covered Policies in each Florida ZIP Code by type of business, construction type, deductible group~~, and Building Code Effectiveness Grading (BCEG)~~, Year Built, Structure Opening Protection, and Roof Shape code combinations.

In order to perform the calculation, each authorized insurance company must submit its total covered property exposure (wind/hurricane insurance in force) **by September 1, ~~2011~~2012** for insured values under Covered Policies **as of June 30, ~~2011~~2012**. Covered Policies are defined in subsection (10) of Article V of the FHCF Reimbursement Contract (see page 17 herein; a full copy of the Reimbursement Contract is available on-line at www.sbafla.com/fhcf under "fhcf rules").

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## ** Important Changes in the ~~2011~~2012 Data Call **

1. The Building Code Effectiveness Grading (BCEG) Code field has been eliminated.

2. The Florida Building Code Indicator field has been eliminated.

## ** Steps for Completing Data Call **

1. Complete the Data Call and return the required items as outlined below.

2. Return the following information to the Administrator, Paragon Strategic Solutions Inc. (Paragon):

| **Required Documentation** | **Item to Return** |
|---|---|
| Exposure Data File* | CD-ROM |
| Submission Checklist | Hard Copy (page 29) |
| Brief Written Verification of Exposure Fluctuations | Cover Letter |
| Control Totals Form | Hard Copy (page 30) |
| Statement of Exposure Data Validity | Hard Copy (page 31) |
| Statement of Retention of Exam File | Hard Copy (page 32) |
| Collateral Protection Statement (required only for Companies writing Collateral Protection Policies) | Hard Copy (page 33) |

*Note: **All data for an individual company should be submitted as one file, unless your company has participated in a Citizens Property Insurance Corporation Coastal ~~High Risk~~ Account or Citizens Property Insurance Corporation Personal Lines and Commercial Lines Account assumption agreement (see pages 6 and 23).** If your company has different departments responsible for compiling portions of your data submission, please have one individual coordinate, compile, and submit the complete package to the Administrator.

3. If your company does not have Covered Policies as defined in subsection (10) of Article V of the FHCF Reimbursement Contract (see page 17 herein), but was an active FHCF company for the ~~2010/2011~~2011/2012 contract year, a letter requesting to petition for exemption from the FHCF must be returned to the Administrator no later than **September 1, ~~2011~~2012**.

**Note:** If your company determines at a later time that it does have Covered Policies, or the State Board of Administration of Florida (SBA) denies your company's request for exemption from the FHCF, your company will be subject to any fees and/or administrative action by the Florida Department of Financial Services (Department) for delinquent or inadequate exposure data as defined in this Data Call and/or your company's Reimbursement Contract.

## ** General Data Call Issues **

### Extensions

Data Call submissions must be received by September 1, ~~2011~~2012. Extensions will not be granted.

### Media Type

Provide the exposure data file in a fixed length (82-character) ASCII format on CD-ROM.

### Where to Send Your Submission

For your convenience, we have enclosed a self-addressed envelope for returning the required information to:

Ms. Kathy Mackenthun, CPCU, ARe
Director – FHCF Administration
Paragon Strategic Solutions Inc.
8200 Tower
5600 West 83rd Street, Suite 1100
Minneapolis, MN 55437

If you have any questions about the information to be supplied or about this Data Call, please do not hesitate to call Holly Bertagnolli, Kathy Mackenthun, or Martin Helgestad of Paragon Strategic Solutions Inc. at 1-800-689-FUND (3863).

## ** Data Quality **

Any company submitting an exposure data file in an incorrect format or in noncompliance with the specifications herein will be required to resubmit its data. See Resubmissions for information on resubmission fees.

### Resubmissions

Any company required to resubmit data will be allowed 30 calendar days to resubmit data (may be less than 30 days if the company has been already notified by the SBA for an exam). A $1,000 resubmission fee (for resubmissions that are not the result of an exam by the SBA) will be invoiced by the FHCF for each resubmission.

If a resubmission is necessary as a result of an examination report issued by the SBA, the resubmission fee will be $2,000. If a company's examination-required resubmission is inadequate and the SBA requires an additional resubmission(s), the resubmission fee for each subsequent resubmission shall be $2,000.

### Explanation of Exposure Fluctuations

Compare your current year submission against your submission from the previous year to ensure increases or decreases in reported exposure are valid. The FHCF requires an explanation of exposure increases or decreases for specific FHCF types of business which meet either the combined dollar/ percentage thresholds or the large dollar thresholds below. Please include a brief written explanation of such fluctuations with your Data Call submission. While the degree of detail is left to the discretion of your company, the explanation must provide detail beyond simply stating that "the data has been reviewed and is correct as submitted".

| Type of Business | $ Threshold | | % Threshold | | Large $ Threshold |
|---|---|---|---|---|---|
| Commercial: | +/- $ 25,000,000 | and | +/- 40% | or | +/- $200,000,000 |
| Residential and Other Contents Policies or Endorsements: | +/- $ 50,000,000 | and | +/- 40% | or | +/- $~~2~~1,000,000,000 |
| Mobile Home: | +/- $ 25,000,000 | and | +/- 40% | or | +/- $40,000,000 |
| Tenants: | | | | | +/-$20,000,000 |
| Condominium Unit Owners: | +/- $ 25,000,000 | and | +/- 40% | or | +/- $40,000,000 |

### Preliminary Validation Software

Running the Preliminary Validation Software (Version ~~2011~~2012) will help ensure that your company's data is in the correct format. However, please keep in mind that the software has been designed to identify data formatting errors, percentage of exposure with valid ZIP Codes, and invalid ZIP-to-county mappings. **The software will not identify records with valid FHCF record formatting that have been coded incorrectly according to the policy details.** Such errors may require a resubmission of exposure data. Any examination conducted by the SBA will be the final determinant of data quality.

**Note:** If you make changes to the Data Call file as a result of the Preliminary Validation Software, remember to make the same changes to the SBA exam file (see page 5).

### Aggregate versus Individual Records

Data may be either aggregated or reported by individual policy record. If aggregating data, please aggregate by each type of business, line of business, construction type, deductible group, county, ZIP Code, Year Built, ~~BCEG, Florida Building Code Indicator code,~~ Structure Opening Protection code, and Roof Shape code combinations.

### Rounding

Exposures should be reported in whole dollars and may be rounded to the nearest $1,000, but no greater.

## ** Covered Policies **

Covered Policies are defined in Section 215.555(2)(c), Florida Statutes, as any insurance policy covering a residential structure, or its contents, located in the State of Florida. Covered Policy is further defined in subsection (10) of Article V of the FHCF Reimbursement Contract (see page 17 herein), which includes personal lines residential coverages, commercial lines residential coverages, and mobile home coverages. **The FHCF provides reimbursement only for losses from policies with wind or hurricane coverage**.

All Covered Policies written by an individual insurer must be reported even if they are written in areas eligible for coverage from Citizens Property Insurance Corporation Coastal ~~High Risk~~ Account or Citizens Property Insurance Corporation Personal Lines and Commercial Lines Accounts.

## ** June 30th "as of" Date **

The data reported under this Data Call pertains to a company's insured values under Covered Policies as of June 30, ~~2011~~2012. This data is used by the FHCF to calculate a company's premium, retention, and maximum FHCF coverage under the applicable Reimbursement Contract.

Although changes to coverage under a policy that are effective after June 30th do not impact reporting under the Data Call (including new policy issuance and policy terminations), the policy terms in effect at a time of loss will be considered in determining a company's losses eligible for reimbursement under the FHCF. For example, if a Covered Policy was written effective July 1, ~~2011~~2012, exposure for that policy would not be included under the ~~2011~~2012 Data Call submission, but losses under that policy would be reportable to the FHCF when the company files its loss reports.

Given an "as of" date of June 30th and a statutory Data Call due date of September 1st, a company must determine the date at which it can most accurately capture and report its data to include policy transactions with effective dates of June 30th or earlier, while still being able to meet the statutory Data Call due date. For example, a company writes a policy with an effective date of June 29, ~~2011~~2012, the transaction was processed by the company on July 15, ~~2011~~2012 and the company compiled its data on July 20, ~~2011~~2012. The FHCF would expect the policy to be reported since the policy was in effect on June 30th and the transaction was processed before the date the data was compiled. However, the FHCF recognizes that if a transaction was not processed far enough through a company's systems by the date on which the company compiled its Data Call information, then that transaction would not necessarily be reflected in the company's original Data Call submission. Nonetheless, should the company have to resubmit its Data Call at a later date, then the transaction should be included in the resubmitted data.

## ** SBA Exam File **

### Generation of the SBA Exam File

The SBA exam file should be generated at the same time your Data Call file is created. If fields are unique to the SBA exam file, care must be taken to ensure accuracy with your company's files. The total reported exposure and rating factors in the exam file must match the total exposure and rating factors of the Data Call file. If, at the time the SBA reviews your exam file, it is determined that these files are not in agreement and the files cannot be used to conduct the examination, your company will be required to resubmit both files and will be subject to the $1,000 resubmission fee.

### Retention of Records for SBA Examination

In accordance with Article XIII of the Reimbursement Contract and the SBA's examination program, all records, including exposure filings (Data Call submission), policy files, and supporting documentation, must be retained along with computer runs (exam file) produced to support the Data Call submission. Companies writing covered collateral protection policies, as defined in this Data Call, must be able to provide documentation that the policy covers the borrower's and lender's interest and that the coverage is in an amount at least equal to the coverage for the dwelling in place under the lapsed homeowner's policy. Such records must be retained until the SBA has completed its examination of your company's exposure submission and loss reports (applicable to the Data Call contract year) and commutation for the contract year (if applicable) has been concluded. The exam file must be retained and maintained so that, upon examination by the SBA, changes can be made to correct any errors which may be identified and to allow for a resubmission if required.

## SBA Exam File Specifications

The SBA exam file must be by individual policy, sorted by type of business and line of business, must be available in a delimited ASCII format or as a Microsoft Access database, and must contain the following fields (do not include any symbols such as -, +, #, $, “, /) in the order listed on the following page.

| Field # | Description | Type | Notes |
|---|---|---|---|
| 1 | Type of Business | Numeric | Only use the codes on pages 8-9. |
| 2 | Line of Business | Numeric | Only use the codes on page 9. |
| 3 | Construction Type | Numeric | Only use the codes on pages 9-10. |
| 4 | Deductible Group | Text | Only use the codes on pages 10-11. |
| 5 | County Code | Numeric | Only use the codes on page 27. |
| 6 | ZIP Code | Numeric | |
| 7 | Insured Risks | Numeric | Must be greater than zero. |
| 8 | Total Insured Value – Building | Numeric | |
| 9 | Total Insured Value – Appurtenant Structures | Numeric | |
| 10 | Total Insured Value – Contents | Numeric | |
| 11 | Total Insured Value – Additional Living Expense | Numeric | |
| 12 | Year Built | Numeric | Only use the codes on page 14. |
| 13 | ~~BCEG Code~~Reserved for future use | Numeric | ~~Only use the codes on page 14.~~Enter 00 (zero’s). |
| 14 | ~~Florida Building Code Indicator~~Reserved for future use | Numeric | ~~Only use the codes on page 15.~~ Enter 0 (zero). |
| 15 | Structure Opening Protection | Numeric | Only use the codes on page 15. |
| 16 | Roof Shape | Numeric | Only use the codes on page 15. |
| 17 | Reserved for future use | Numeric | Enter 0 (zero) |
| 18 | Reserved for future use | Numeric | Enter 0 (zero). |
| 19 | Policy Effective Date | Numeric or Date/Time | Numeric Format: yyyymmdd<br>Date/Time Format: Month/day/year<br>Effective Date must be in one field and the numeric format must have 8 characters. |
| 20 | Policy Expiration Date | Numeric or Date/Time | Numeric Format: yyyymmdd<br>Date/Time Format: month/day/year<br>Expiration Date must be in one field and the numeric format must have 8 characters. |
| 21 | Policy Number | Text | |
| 22 | Citizens Policy Number | Text | Applies only to policies assumed from Citizens that have not renewed onto the company’s books by June 30, ~~2011~~2012. |

# Florida Hurricane Catastrophe Fund ~~2011~~2012 Data Call

## File Layout

The following fields must be provided. If you aggregate your company's data, please do so by type of business, line of business, construction type, deductible group, county, ZIP Code, Year Built, ~~BCEG code, Florida Building Code Indicator,~~ Structure Openings Protection, and Roof Shape code combinations.

| Field # | Description | Position | Length | Type | Notes |
|---|---|---|---|---|---|
| 1 | Type of Business | 1 | 1 | Numeric | Only the codes on pages 8-9 are acceptable. |
| 2 | Line of Business | 2 | 1 | Numeric | Only the codes on page 9 are acceptable. |
| 3 | Construction Type | 3 | 2 | Numeric | Only the codes on pages 9-10 are acceptable. |
| 4 | Deductible Group | 5 | 2 | Alpha | Only the codes on pages 10-11 are acceptable. |
| 5 | County Code | 7 | 3 | Numeric | Only the codes on page 27 are acceptable. |
| 6 | ZIP Code | 10 | 5 | Numeric | At least 95% of exposure must have a valid ZIP Code. |
| 7 | Total Insured Risks | 15 | 12 | Numeric | Must be greater than zero. |
| 8 | Total Insured Value – Building* | 27 | 12 | Numeric | * See note below table. |
| 9 | Total Insured Value – Appurtenant Structures* | 39 | 12 | Numeric | * See note below table. |
| 10 | Total Insured Value – Contents* | 51 | 12 | Numeric | * See note below table. |
| 11 | Total Insured Value – ALE* | 63 | 12 | Numeric | * See note below table. |
| 12 | Year Built | 75 | 1 | Numeric | Only the codes on page 14 are acceptable. |
| 13 | Reserved for future use~~BCEG Code~~ | 76 | 2 | Numeric | Enter 00 (zero's).~~Only the codes on page 14 are acceptable.~~ |
| 14 | Reserved for future use~~Florida Building Code Indicator~~ | 78 | 1 | Numeric | Enter 0 (zero).~~Only the codes on page 15 are acceptable.~~ |
| 15 | Structure Opening Protection | 79 | 1 | Numeric | Only the codes on page 15 are acceptable. |
| 16 | Roof Shape | 80 | 1 | Numeric | Only the codes on page 15 are acceptable. |
| 17 | Reserved for future use | 81 | 1 | Numeric | Enter 0 (zero). |
| 18 | Reserved for future use | 82 | 1 | Numeric | Enter 0 (zero). |

*Note: The sum of these four fields for each record must be greater than zero.

**Example:** A record with the following information:

| Field # | Description | Type | Entry |
|---|---|---|---|
| 1 | Type of Business | Residential | 2 |
| 2 | Line of Business | Homeowners | 2 |
| 3 | Construction Type | Frame | 01 |
| 4 | Deductible Group | $2,000 | RC |
| 5 | County Code | | 025 |
| 6 | ZIP Code | | 33130 |
| 7 | Total Insured Risks | | 5 |
| 8 | Total Insured Value – Building | | $500,000 |
| 9 | Total Insured Value – App. Structures | | $100,000 |
| 10 | Total Insured Value – Contents | | $250,000 |
| 11 | Total Insured Value – ALE | | $50,000 |
| 12 | Year Built | Date Range | 1 |
| 13 | Reserved for future use~~BCEG Code~~ | ~~BCEG code of 5~~ | ~~05~~00 |
| 14 | Reserved for future use~~Florida Building Code Indicator~~ | ~~Dwelling built under the 2001 Florida Building Code, or Dwelling located in Miami-Dade or Broward counties and built under the 1994 South Florida Building Code~~ | ~~1~~0 |
| 15 | Structure Openings Protection | No credit is given to policyholder | 0 |
| 16 | Roof Shape | Hip, Mansard, or Pyramid | 1 |
| 17 | Reserved for future use | | 0 |
| 18 | Reserved for future use | | 0 |

Each record must have the following layout:

2201RC025331300000000000050000005000000000001000000000002500000000000500001050100100

Since each field has a defined length, please "zero fill" the positions in each field that will not be used. Each record must be 82 characters in length.

## Description of Data Fields

The FHCF strongly encourages any individual involved in completing this Data Call to review the Reporting Clarifications on pages 19-22 herein.

1. **Type of Business (TOB)**

All exposure should be classified as one of the following FHCF TOBs. Exposure for scheduled personal property written under attachments, endorsements, riders; any policy separately covering personal property; or any policy separately covering commercial residential contents should be reported as the FHCF TOB it is associated with. If the exposure is not associated with another policy, it should be reported as FHCF TOB "4" (Tenants), with the exception of mobile home related property, which must still be reported as FHCF TOB "3" (Mobile Home).

| Type of Business | Code |
|---|---|
| Commercial | 1 |
| Residential | 2 |
| Mobile Home | 3 |

| Type of Business | Code |
|---|---|
| Tenants | 4 |
| Condominium Unit Owners | 6 |

General TOB Instructions:

- **"Commercial"** should be used for commercial-habitational exposures such as apartment buildings and condominium complexes. Do not use this TOB for individual condominium unit owners.

- "**Mobile Home**" should be used for all mobile home coverages, regardless of the policy form on which coverage is written, including coverage provided to a person(s) renting a mobile home.
- "**Tenants**" should be used for policies providing property coverage to a person(s) entitled to occupy a dwelling unit (including a condominium unit) under a rental agreement. Do not use this TOB for any policy providing coverage to a person renting a mobile home. Exposure for scheduled personal property written under attachments, endorsements, riders; any policy separately covering personal property; or any policy separately covering commercial residential contents should be reported as the FHCF TOB it is associated with. If the exposure is not associated with another policy, it should be reported as Tenants.
- "**Condominium Unit Owners**" should be used for individual condominium unit owners, whether owner or tenant occupied. Do not use this TOB for condominium complexes or multi-unit structures.

2. **Line of Business**

Exposure information for Covered Policies is to be reported using the following codes (use the code your company deems most appropriate):

| Line of Business | Code |
|---|---|
| Fire and Allied Lines | 1 |
| Homeowners Multiple Peril | 2 |
| Farmowners Multiple Peril | 3 |

| Line of Business | Code |
|---|---|
| Commercial Multiple Peril | 4 |
| Mobile Homeowners | 5 |
| Inland Marine | 6 |

3. **Construction Type**

The FHCF has further condensed its listing of construction types/definitions. The FHCF's construction codes and definitions are provided on page 25. Your company must use the applicable FHCF codes in its Data Call submission.

If your company's construction definitions do not match those of the FHCF, you must provide the Administrator with your company's construction types and definitions and your recommended mapping to the most similar FHCF construction types as defined on pages 25. This will help you avoid a subsequent resubmission due to improper construction reporting. The Administrator will review your method of mapping construction codes and determine if the mapping between your codes and the FHCF's codes match. Once the Administrator has notified you in writing that your mapping is acceptable, you must complete the actual mapping so that only FHCF constructions are reported in your submission. If a mapping review is necessary for your company, such a review must be done each year to ensure changes to the FHCF construction types have not affected the previously reviewed mapping.

For policies in which your company does not capture construction information, exposure should always be reported using the FHCF Unknown construction code "11" (or code "25" for mobile home exposure). Otherwise, if your company does capture construction information, but has less than $50 million of aggregate exposure, you have the option of reporting <u>all</u> non-mobile home exposure with FHCF default construction code "12" and all mobile home exposure with FHCF default construction code "26".

**Residential**

| Construction Type | Code |
|---|---|
| Frame | 01 |
| Masonry | 02 |
| Masonry Veneer | 10 |
| Unknown (Non-Mobile Home) | 11 |
| Non-Mobile Home Default Construction* | 12 |

**Commercial, Condominium Unit Owners, Tenants**

| Construction Type | Code |
|---|---|
| Frame | 01 |
| Masonry | 02 |
| Masonry with Reinforced Concrete Roof | 15 |
| Superior | 07 |
| Superior with Reinforced Concrete Roof | 16 |
| Masonry Veneer | 10 |
| Unknown (Non-Mobile Home) | 11 |
| Non-Mobile Home Default Construction* | 12 |

**Mobile Home**

| Construction Type | Code |
|---|---|
| Mobile Home - Fully Tied Down, Mfg. before 7/13/94 | 21 |
| Mobile Home - Fully Tied Down, Mfg. on or after 7/13/94 or documented to be in compliance with ANSI/ASCE 7-88 | 22 |
| Mobile Home – Other than Fully Tied Down or Unknown | 25 |
| Mobile Home - Default Construction* | 26 |

* See paragraph preceding the above tables for reporting eligibility

4. **Deductible Group** – *Wind Including Hurricane Deductible, or Hurricane Deductible Only*

Except as instructed for commercial-habitational policies below, report an FHCF percentage or dollar deductible code based on how the policy deductible is written. For example, a $100,000 residential policy written with a 2% deductible must be reported with code R2, not code RC ($1,501 to $2,500 deductible), regardless of how the deductible is "stated" to the policyholder.

For policies written with a percentage deductible and a minimum dollar deductible, report the percentage deductible.

For commercial-habitational policies (regardless of the FHCF Type of Business under which the policy's exposure is reported) that have a policy deductible greater than $50,000, the deductible amount must be converted to a percentage of the total insured building value (Data Call field 8) and reported to the FHCF as a percentage deductible.

For commercial-habitational policies covering multiple structures/contents under an indivisible aggregate deductible, report the full blanket deductible for each record reported.

Following are the FHCF deductible groups and codes:

**Commercial**

| Deductible Group | Code |
|---|---|
| $0 to $2,500 | CA |
| $2,501 to $7,500 | CB |
| $7,501 to $15,000 | CC |
| $15,001 to $50,000 | CD |
| Greater than $50,000 – Convert to a percentage | See % Ded.'s |
| | |
| | |
| | |
| | |
| | |

| Deductible Group | Code |
|---|---|
| Less than or equal to 1% | C1 |
| Greater than 1%, less than or equal to 2% | C2 |
| Greater than 2%, less than or equal to 3% | C3 |
| Greater than 3%, less than or equal to 4% | C4 |
| Greater than 4%, less than or equal to 5% | C5 |
| Greater than 5%, less than or equal to 6% | C6 |
| Greater than 6%, less than or equal to 7% | C7 |
| Greater than 7%, less than or equal to 8% | C8 |
| Greater than 8%, less than 10% | C9 |
| 10% or Greater | C0 |

**Residential, Tenants, or Condominium Unit Owners**

| Deductible Group | Code |
|---|---|
| $0 | RM |
| $1 to $500 | RA |
| $501 to $1,500 | RB |
| $1,501 to $2,500 | RC |
| Greater Than $2,500 | RD |
| Greater than $50,000 – Convert to a percentage | See % Ded.'s |

| Deductible Group | Code |
|---|---|
| Less than or equal to 1% | R1 |
| Greater than 1%, less than or equal to 2% | R2 |
| Greater than 2%, less than or equal to 3% | R3 |
| Greater than 3%, less than or equal to 4% | R4 |
| Greater than 4%, less than or equal to 5% | R5 |
| Greater than 5%, less than or equal to 6% | R6 |
| Greater than 6%, less than or equal to 7% | R7 |
| Greater than 7%, less than or equal to 8% | R8 |
| Greater than 8%, less than 10% | R9 |
| 10% or greater, less than 15% | R0 |
| 15% or Greater | RZ |

**Mobile Home**

| Deductible Group | Code |
|---|---|
| $0 | MM |
| $1 to $250 | MA |
| $251 to $500 | MB |
| Greater Than $500 | MC |
| Greater than $50,000 – Convert to a percentage | See % Ded.'s |

| Deductible Group | Code |
|---|---|
| Less than or equal to 1% | M1 |
| Greater than 1%, less than or equal to 2% | M2 |
| Greater than 2%, less than or equal to 3% | M3 |
| Greater than 3%, less than or equal to 4% | M4 |
| Greater than 4%, less than or equal to 5% | M5 |
| Greater than 5%, less than or equal to 6% | M6 |
| Greater than 6%, less than or equal to 7% | M7 |
| Greater than 7%, less than or equal to 8% | M8 |
| Greater than 8%, less than 10% | M9 |
| 10% or Greater | M0 |

5. **County Code**

Florida county code specifying the location of each covered risk. All records must be coded with a valid Florida county code listed on page 27. There is no "unknown" county code. ZIP Codes and county codes must be cross-referenced to ensure that 95% of your company's aggregate exposure has a valid Florida ZIP Code to county code match. As the FHCF recognizes some ZIP Codes may span county boundaries, the Preliminary Validation Software Version ~~2011~~2012 has been programmed to accept any county immediately bordering the county the FHCF considers to be the county in which a specific ZIP Code resides.

6. **ZIP Code**

The 5-digit ZIP Code location of each covered risk in Florida. A minimum of 95% of your company's aggregate exposure must be coded with valid Florida ZIP Codes. The FHCF ZIP Code database is as of January ~~2011~~2012. If a record contains a ZIP Code that does not match our database, the rate applied will be based on the county code instead of the ZIP Code.

A listing of valid ZIP Codes and corresponding county codes and rating regions is installed with the Preliminary Validation Software CD-ROM under the file name "zipinput.csv."

7. **Total Insured Risks (Must be greater than zero.)**

This is the total number of insured risks for the FHCF Covered Policies included in a given record.

**Reportable Exposure (Data Call Fields 8-11)**

The only wind exposure that should be reported in response to this Data Call is summarized below. Keep in mind that the exposure reportable to the FHCF is less inclusive than the coverage provided by the FHCF. (Covered policies are defined in subsection (10) of Article V of the Reimbursement Contract. See page 17 herein.) Note that under no circumstances should exposure be reported for Ordinance and Law coverage (this type of coverage is reimbursable but is built into the FHCF rates) or loss assessment coverage (this coverage is not reimbursable).

1. Basic wind/hurricane limit for dwellings (often referred to as Coverage A);
2. Basic wind/hurricane limit for appurtenant structures or non-habitational structures (often referred to as Coverage B);
3. Basic wind/hurricane limit for contents (often referred to as Coverage C);
4. Basic wind/hurricane limit for additional living expense (often referred to as Coverage D, and sometimes as Coverage E);
5. Any attachments, endorsements, or riders that modify or increase the limits above; and
6. Any attachments, endorsements, or riders that provide additional wind/hurricane limit for personal property or structures, Building Additions and Alterations coverage, or Unit Owners coverage on Condominium Unit Owners policies.

**Exposure from any additional coverages/coverage extensions written within the policy form and not listed above, regardless of whether the coverage is within the policy limits or in addition to the policy limits, are not reportable to the FHCF under this Data Call.**

***Examples of exposure to be reported to the FHCF:***

- In addition to the $50,000 of Coverage C limit on Patti's renters policy, Patti has $10,000 of coverage for her personal computer system written as scheduled personal property. $60,000 of Coverage C limit must be reported.
- Andy's insurance company does not offer Coverage B as a standard coverage under a homeowners policy, but Coverage B limit can be purchased via an endorsement. If Andy purchases the Coverage B endorsement, this exposure must be reported.
- Jason's insurance policy does not provide a stated limit on the dec page for Coverage B, but under "Other Coverages," Coverage B limit is provided as an additional 10% of Coverage A limit. This exposure must be reported.
- Marcie's renters policy provides for a Coverage C limit of $50,000. The coverage for the tenants policy includes an additional coverage written within the policy form for buildings additions and alterations of 10% of the Coverage C limit. Marcie has purchased an endorsement to increase the buildings additions and alterations coverage to 25% of the Coverage C limit. In addition to reporting the $50,000 Coverage C limit, the additional 15% ($7,500) of the Coverage C limit for building additions and alterations coverage is also reportable, for a total of $57,500 of exposure to be reported.
- An apartment complex is covered on a commercial policy with $500,000 for building and $20,000 for contents. The policy also provides a coverage extension for valuable papers of $2,500. This coverage is offered as part of the policy form and not by endorsement. The amount of reportable exposure is $520,000 since the coverage extension for valuable papers is provided as a coverage extension within the policy form.

***Examples of exposure <u>not to be reported</u> to the FHCF:***

- Any type of Ordinance and Law coverage (coverage is included within the FHCF rates).
- Any exposure for Loss Assessment coverage.
- Any additional exposure for endorsements that specifically increase the limit of liability at the time of a covered loss (i.e., guaranteed replacement cost, specified increase to the dwelling limit.)
- Peggy's renters policy provides for a Coverage C limit of $50,000. The coverage for the tenants policy includes an additional coverage written within the policy form for buildings additions and alterations of 10% of the Coverage C limit. Peggy has not purchased any endorsements to increase the coverages provided under the policy form. The Coverage C limit of $50,000 would be reported. The 10% of the Coverage C limit for building additional and alterations coverage is not reportable as additional exposure.
- Your company's condominium unit owners policy provides for a dwelling limit (additions and alterations coverage) of $1,000, which is listed on every condominium unit owners policy written by the company and is provided at no additional premium. The $1,000 is not reportable to the FHCF as an additional exposure.
- Your company provides ALE coverage at a limit of 50% of the building (Coverage A) limit. Therefore, for a policy with a Coverage A limit of $200,000, your company would also provide $100,000 of ALE limit. Because 40% is the statutory cap with respect to FHCF coverage, your company would only report $80,000 of ALE exposure under this Data Call.
- Appurtenant Structures insured under a policy that does not include coverage for a habitational structure(s) when such a policy is not an attachment/endorsement/rider to a policy providing coverage for a habitational structure(s). For example, if your company writes a policy covering a pool for an apartment complex, but does not insure the apartment complex itself, the pool exposure is not reportable to, or covered by, the FHCF.

For a list of specific exclusions, see Article VI of the Reimbursement Contract applicable to this Data Call.

8. **Total Insured Value - Building**

   This is the total insured building limit for a policy or multiple policies with the same Data Call codes.

9. **Total Insured Value - Appurtenant Structures or Non-Habitational Structures**

   This is the total insured appurtenant structures limit for a policy or multiple policies with the same Data Call codes.

10. **Total Insured Value - Contents**

    This is the total insured contents limit for a policy or multiple policies with the same Data Call codes.

11. **Total Insured Value – Additional Living Expense (ALE)**

    This is the total insured ALE limit for a policy or multiple policies with the same Data Call codes. For ALE coverage provided as a specific dollar limit, report exposure values based on that limit, but not to exceed 40% of the Residential Structure (Coverage A) exposure or 40% of the contents (Coverage C) exposure. If ALE is written as a portion of Coverage A, 40% of Coverage A is the cap. If ALE is written as a portion of Coverage C, 40% of Coverage C is the cap. Note that if the ALE coverage written is less than 40%, ALE should be reported as written.

    For covered policies written with ALE as a time element coverage, you must report ALE exposure in an amount not to exceed 40% of the Residential Structure or 40% of the contents exposure based on

the type of policy (e.g., a homeowners policy is usually based on structure versus a renters policy based on contents).

**Note that the 40% threshold is a statutory cap.** If your company provides coverage to its policyholders that is in excess of this cap, or if rounding of your building or contents exposure results in a higher ALE percentage, report no more than the cap when reporting ALE exposure to the FHCF.

12. **Year Built**

Enter the Year Built from the table below.

| Year Built | FHCF Code |
|---|---|
| Unknown or Mobile Home | 0 |
| 1994 or earlier | 1 |
| 1995 - 2001 | 2 |
| 2002 or later | 3 |

13. ~~**Building Code Effectiveness Grading (BCEG) Code**~~**Reserved for future use – enter 00.**

~~This code is **required** to identify qualifying exposure units that also receive a BCEG credit from their direct insurance writers. Report your actual "community graded" BCEG code (Codes 01 – 10 only). If a BCEG credit is not given or the BCEG code is "Ungraded" or "Non Participating," enter "00."~~

~~If your company has less than $50 million of aggregate non-mobile home exposure, you may choose to report all non-mobile home exposure with default FHCF Code "50". Exposures reported with this default will not receive any credits from the FHCF.~~

~~The FHCF premium credits below will be given for qualifying exposure units that also receive credits from their direct insurance writers:~~

| ~~**Actual BCEG Code**~~ | ~~**FHCF Credit**~~ |
|---|---|
| ~~00~~ | ~~None~~ |
| ~~01 – 03~~ | ~~12%~~ |
| ~~04 – 07~~ | ~~8%~~ |
| ~~08 – 09~~ | ~~4%~~ |
| ~~10~~ | ~~None~~ |
| ~~FHCF Default: 50*~~ | ~~None~~ |

~~*See default eligibility requirement in second paragraph of this section.~~

~~With respect to buildings which have been individually graded and certified as "Grade 1" for windstorm/hail, and are eligible for a BCEG credit from the FHCF, such exposure may be reported to the FHCF with BCEG credit code "01."~~

14. ~~**Florida Building Code Indicator**~~ **Reserved for future use – enter 0.**

~~This code is used to identify dwelling units built under the 2001 Florida Building Code standards effective March 1, 2002 or the Miami-Dade and Broward Counties 1994 South Florida Building Code effective September 1, 1994. Enter the appropriate code from the table below. If a dwelling was built in 2002 or later, or if the dwelling is located in Miami-Dade or Broward counties and was built in 1995 or later, then code "1" should be used. Otherwise, unless there is an inspection report confirming compliance with one of these two building codes, FHCF code "2" should be used.~~

| ~~**Florida Building Code Indicator**~~ | ~~**FHCF Code**~~ |
|---|---|
| ~~Dwelling built under the 2001 Florida Building Code, or Dwelling located in Miami-Dade or Broward counties and built under the 1994 South Florida Building Code~~ | ~~1~~ |
| ~~Dwelling not built under the 2001 Florida Building Code or the 1994 South Florida Building Code, or Unknown~~ | ~~2~~ |

15. **Structure Opening Protection**

Enter the appropriate structure opening protection code from the table below based on whether or not your company gives a structure opening protection credit to its policyholder for the dwelling unit being reported under this Data Call.

| Structure Opening Protection | FHCF Code |
|---|---|
| No credit is given to policyholder | 0 |
| Credit is given to policyholder | 5 |

16. **Roof Shape**

Enter the appropriate roof shape code from the table below.

| Roof Shape | FHCF Code |
|---|---|
| Hip, Mansard, or Pyramid | 1 |
| Gable, Other, or Unknown | 2 |

17. **Reserved for future use – enter 0.**

18. **Reserved for future use – enter 0.**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Attachments

- Article V - Definitions of Additional Living Expense, Covered Policy, Excess Insurance, and Residential Structures, as included in the Reimbursement Contract (page 17)
- Article VI – Excluded Exposures (page 18)
- Reporting Clarifications (pages 19-22)
- Citizens Property Insurance Corporation Takeouts Pursuant to Assumption Agreements (page 23)
- Citizens Property Insurance Corporation ~~High Risk~~ Coastal Account Quota Share Primary Insurance Reporting Requirements (page 24)
- Construction Codes (page 25)
- Florida County Codes (page 27)
- Reference Guide (page 28)
- Submission Checklist (page 29)
- Control Totals Form (page 30)
- Statement of Exposure Data Validity (page 31)
- Statement of Retention of Exam File (page 32)
- Collateral Protection Statement (page 33)
- Supplemental Instruction Sheet for New Participants (page 34)
  (Sent only to new participants)

## Enclosures

- FHCF Preliminary Validation Software Version ~~2011~~2012 CD-ROM
- FHCF Preliminary Validation Software Version ~~2011~~2012 Instruction Sheet

(3) **Additional Living Expenses (ALE)**
ALE losses covered by the FHCF are not to exceed 40 percent of the insured value of a Residential Structure or its contents based on the coverage provided in the policy. Fair rental value, loss of rents, or business interruption losses are not covered by the FHCF.

(10) **Covered Policy or Covered Policies**

(a) Covered Policy, as defined in Section 215.555(2)(c), Florida Statutes, is further clarified to mean only that portion of a binder, policy or contract of insurance that insures real or personal property located in the State of Florida to the extent such policy insures a Residential Structure, as defined in definition (27) herein, or the contents of a Residential Structure located in the State of Florida.

(b) Due to the specialized nature of the definition of Covered Policies, Covered Policies are not limited to only one line of business in the Company's annual statement required to be filed by Section 624.424, Florida Statutes. Instead, Covered Policies are found in several lines of business on the Company's annual statement. Covered Policies will at a minimum be reported in the Company's statutory annual statement as:

- Fire
- Allied Lines
- Farmowners Multiple Peril
- Homeowners Multiple Peril
- Commercial Multiple Peril (non liability portion, covering condominiums and apartments)
- Inland Marine

Note that where particular insurance exposures are reported, e.g., mobile home, on an annual statement is not dispositive of whether or not the exposure is a Covered Policy.

(c) This definition applies only to the first-party property section of a policy pertaining strictly to the structure, its contents, appurtenant structures, or ALE coverage.

(d) Covered Policy also includes any collateral protection insurance policy covering personal residences which protects both the borrower's and the lender's financial interest, in an amount at least equal to the coverage for the dwelling in place under the lapsed homeowner's policy, if such policy can be accurately reported as required in Section 215.555(5), Florida Statutes. A Company will be deemed to be able to accurately report data if the required data, as specified in the Premium Formula adopted in Section 215.555(5), Florida Statutes, is available.

(e) See Article VI of this Contract for specific exclusions.

(13) **Excess Policies**
This term, for the purposes of this Contract, means a policy that provides insurance protection for large commercial property risks that provide a layer of coverage above a primary layer (which is insured by a different insurer) that acts much the same as a very large deductible.

(27) **Residential Structures**
This term means dwelling units, including the primary structure and appurtenant structures insured under the same policy and any other structure covered under endorsements associated with a policy covering a residential structure. Covered Residential Structures do not include any structures listed under Article VI herein or structures used solely for non-residential purposes.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Reimbursement Contract: Article VI – Exclusions

The following selected exclusions from Article VI of the Reimbursement Contract pertain to exposure that should not be reported under this Data Call.

2. Any policy which excludes wind or hurricane coverage.
3. Any Excess Policy or Deductible Buy-Back Policy that requires individual ratemaking.
4. Any policy for Residential Structures, as defined in Article V(27) herein, that provides a layer of coverage underneath an Excess Policy, as defined in Article V(13) herein, issued by a different insurer.
5. Any liability of the Company attributable to losses for fair rental value, loss of rent or rental income, or business interruption.
6. Any collateral protection policy that does not meet the definition of Covered Policy as defined in Article V(10)(d) herein.
7. Any reinsurance assumed by the Company.
8. Any exposure for hotels, motels, timeshares, shelters, camps, retreats, and any other rental property used solely for commercial purposes.
9. Any exposure for homeowner associations if no habitational structures are insured under the policy.
10. Any exposure for homes and condominium structures or units that are non-owner occupied and rented for six (6) or more rental periods by different parties during the course of a twelve (12) month period.
11. Commercial healthcare facilities and nursing homes; however, a nursing home which is an integral part of a retirement community consisting of primarily habitational structures that are not nursing homes will not be subject to this exclusion.
12. Any exposure under commercial policies covering only appurtenant structures or structures that do not function as a habitational structure (e.g., a policy covering only the pool of an apartment complex).
13. Personal contents in a commercial storage facility (including jewelry in an off-premises vault) covered under a policy that covers only those personal contents.
14. Policies covering only Additional Living Expense.
15. Any exposure for barns or barns with apartments.
16. Any exposure for builders risk coverage or new residential structures still under construction.
17. Any exposure for recreational vehicles, golf carts or boats (including boat related equipment) requiring licensing and written on a separate policy or endorsement.
22. Any exposure for, or losses attributable to, loss assessment coverage.
24. Any liability assumed by the Company from Pools, Associations, and Syndicates. Exception: Covered Policies assumed from Citizens under the terms and conditions of an executed assumption agreement between the Authorized Insurer and Citizens are covered by this Contract.
28. Specialized Fine Arts Risks as defined in Rule 19-8.028(4)(d), F.A.C.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Reporting Clarifications

**General Clarifications**

1. *Aggregate Policy Limits (not applicable to Commercial Residential Policies)*

   For policies that provide an aggregate limit without stating a specific limit for buildings, appurtenant structures, contents, or ALE exposures, report the exposure to the FHCF by allocating the total policy limit to the building field if the policy fits the definition of FHCF types of business Residential or Mobile Home, or to the contents field if the policy fits the definition of FHCF types of business Tenants or Condominium Unit Owners.

2. *Farmowners*

   The only exposure under a Farmowners policy that is reportable to the FHCF is exposure for the dwelling, other private structures appurtenant to dwellings, household personal property, and additional living expense coverage. FHCF commercial codes for type of business and deductible may not be used.

~~3. *BCEG Credits that Vary by Coverage Within a Policy*~~

   ~~For policies under which BCEG credits do not apply to every policy coverage (e.g., credit applies to building but not contents), all exposure under the policy may be reported as one record.~~

~~4.~~3. *Multiple Rating Factors (Construction and Deductible) within the Building, Appurtenant Structures, Contents (including scheduled personal property), and ALE Limits*

   If, within a policy, the limits above have different FHCF rating factors, exposure may be reported under one record using the rating factors applicable to the most exposure (e.g., if 70% of the exposure under such a policy is for Building coverage, report the rating factors applicable to the Building coverage). If your company chooses to break such policies into multiple records for FHCF reporting, you must do so consistently across your non-commercial book of business.

   This clarification is also applicable to the Year Built, ~~Florida Building Code Indicator,~~ Structure Opening Protection, and Roof Shape fields.

   For commercial policies covered by the FHCF, see Commercial-Habitational Clarification #1 below.

~~5.~~4. *Golf Cart Coverage*

   If coverage for golf carts is provided with no stated limit (i.e., based on actual cash value at the time of a loss), the exposure required to be reported to the FHCF is $5,000 for each risk. If the coverage is provided by endorsement to a covered policy, the exposure is only reportable when coverage for the golf cart is in addition to the policy limits provided for personal property. If a golf cart requires licensing, it is not reportable to, or covered by, the FHCF.

## Commercial-Habitational Clarifications

The only Commercial policies covered by the FHCF are those covering habitational structures (e.g. apartments and condominiums).

1. *Multiple Rating Factors (Construction and Deductible) within the Building (dwelling), Non-Habitational Structures, Contents, and ALE Limits of a commercial policy*

   One Occupied Dwelling Structure: If, within a commercial policy, the limits above have different rating factors (e.g. a superior masonry apartment building, a frame guardhouse, and a masonry pool), exposure may be reported under one record using the rating factors applicable to the dwelling structure. If your company chooses to break such policies into multiple records to report different constructions and deductibles to the FHCF, you must do so consistently across your commercial book of business.

   Multiple Occupied Dwelling Structures: If, within a commercial policy, several occupied dwelling structures are insured and those structures are in multiple ZIP Codes, a separate record must be reported for each ZIP Code with the exposure applicable to that specific ZIP Code.

   If multiple occupied dwelling structures insured under one policy are in the same ZIP Code and have shared non-habitational structures with different rating factors, your company may report the exposure for the non-habitational structures as appurtenant to the dwelling structure your company deems most appropriate.

   This clarification, in its entirety, is also applicable to the Year Built, ~~Florida Building Code Indicator,~~ Structure Opening Protection, and Roof Shape fields.

2. *Commercial Policies Covering Farms*

   For commercial farms with habitational exposure that is written on a commercial policy form, report the exposure as "Residential" type of business, with the exception of any mobile home related exposure. Dwelling mobile home exposure on the policy, including the contents therein and scheduled personal property, must be reported as "Mobile Home" type of business.

3. *Commercial Policies Covering a Variety of Risks (other than Farm coverage)*

   For a commercial policy covering both commercial habitational exposures and incidental non-commercial habitational exposures (i.e. single-family homes, condominium unit owners, tenants coverage, and mobile homes) in the same ZIP Code, all non-mobile home related exposure may be reported under one record using FHCF type of business "Commercial." The construction, deductible, Year Built, ~~Florida Building Code Indicator,~~ Structure Opening Protection, and Roof Shape codes applicable to the commercial habitational exposure should be reported for that record. Non-commercial habitational exposure is considered incidental if such exposure accounts for less than 50% of the total reportable exposure under that policy. Any mobile home exposure, regardless of the type of policy under which it is written, must be reported to the FHCF as type of business Mobile Home and with the applicable mobile home construction and deductible codes.

   Note that if the exposures are in different ZIP Codes, the exposures under the single commercial policy must be reported as separate records using the ZIP Code applicable to each exposure(s). Should your company choose to report the exposure under such a policy as multiple records (e.g. an apartment building reported as Commercial, the CEO's home reported as Residential, and the president's condominium reported as Condominium Unit Owners), the decision to do so must be applied consistently to all such policies, and the Data Call codes applicable to each record/type of business must be reported.

4. *Blanket Limits*

   For a multiple location policy with a blanket limit, report the lesser of the full blanket limit or the full wind exposure value for each risk/building/exposure. The company must maintain a copy of the Statement of Values to support the policy exposure reported in order for the SBA to confirm correct reporting during examination.

5. *Blanket Deductibles*

   For a policy covering multiple structures/contents under an indivisible aggregate deductible, report each risk/building/exposure with the full blanket deductible amount.

6. *Multiple Location Policy with Non-Florida Risk*

   For a multiple location policy with non-Florida risk, report the lesser of the full policy limit or the full wind exposure value for each Florida risk/building/exposure. The company must maintain a copy of the Statement of Values to support the policy exposure reported in order for the SBA to confirm correct reporting during examination.

7. *Single Structures with Mix of Commercial-Habitational and Non-Habitational or Business Exposure*

   **Important Note:** If this section is applicable to your company, it is necessary for you to review your executed ~~2011~~2012 FHCF Reimbursement Contract.

   A. If a single structure is used for both habitational and non-habitational purposes and the structure has a commercial-residential class code (based on a classification plan submitted to, and reviewed by, the FHCF Administrator), report the entire exposure for the structure to the FHCF. The FHCF will reimburse losses for the entire structure as well. **This requirement applies to all companies insuring such structures.**

   B. If the structure has a commercial non-residential class code (again, as on file with and reviewed by the FHCF Administrator), report only the habitational portion of the policy.

      In recognition of the unusual nature of commercial structures with incidental habitational exposure and the hardship some companies may face in having to carve out such incidental exposure, as well as the losses to such structures, the FHCF will accommodate these companies by allowing them to exclude the entire exposure from their Data Call submission, if all of the following three conditions are met:

      (1) The decision to not carve out and report the incidental habitational exposure shall apply to all such structures insured by the company.
      (2) The company should not report losses to this incidental habitational exposure and the FHCF will not reimburse the losses to this exposure.
      (3) The company must have already indicated its decision to not carve out and report the incidental exposure in the annual Reimbursement Contract. Failure to disclose this decision at the time of the company's execution of the Reimbursement Contract shall be interpreted by the FHCF as the company's intent to carve out and report incidental habitational exposure, and the failure to do so will be considered a reporting error.

   C. If a policy covers multiple structures that each have a mix of commercial-habitational and non-habitational or business exposure, apply the decision rules in A. and B. above separately to each structure. (This process must be consistent with requirement B.(1) above.)

   D. If your company writes policies for which this section is applicable, provide the Administrator with a list of your company's applicable Florida class codes (as on file with and reviewed by the FHCF Administrator), a description of those codes, and your company's recommendation of whether each code is commercial-residential or commercial non-residential. The Administrator will review this information with the SBA, and will respond to your company with respect to the submitted recommendations prior to your Data Call submission.

8. *Policies with a Mix of Commercial Habitational & Non-Habitational Structures*

   Only report exposure which directly covers, or is used in relation to, covered habitational structures. "Used in relation to" is defined as any structure that is used solely by the occupants (or their guests) of the habitational structure. If you are unable to make this determination for a structure, do not report the exposure for that structure in your Data Call submission. Refer to the other clarifications herein with respect to blanket limits or blanket deductibles.

9. *Multiple Family Dwellings on a Commercial Policy & FHCF Type of Business (TOB)*

   Two, three, and four-family dwellings should be reported with an FHCF TOB based on how your company rates the dwellings (either Residential or Commercial FHCF TOB). Dwellings housing more than four families should be reported as FHCF TOB Commercial. For a commercial policy covering exposure that falls under multiple FHCF types of business, see Commercial-Habitational Clarification #3 herein.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Citizens Property Insurance Corporation
## Takeouts Pursuant to Assumption Agreements

Pursuant to Sections 627.351(6)(p)3. and 627.3511, Florida Statutes, for purposes of reporting exposure, calculating reimbursement premium, and determining retention, all FHCF exposure removed from Citizens Property Insurance Corporation ~~High Risk~~ Coastal Account and/or Citizens Property Insurance Corporation Personal Lines and Commercial Lines Accounts pursuant to an assumption agreement shall be treated as the exposure of the assuming insurer.

Insurers engaged in assumption agreements from July 1, ~~2010~~ 2011 through June 30, ~~2011~~2012 with either Citizens entity shall submit **separate** data files to the FHCF (including a Control Totals Form for each file) in the format specified herein. If your company engaged in assumption agreements with both Citizens entities, three files would be submitted in response to this Data Call. One file must contain the insurer's FHCF exposure from direct written premiums. The exposure assumed from either Citizens entity which is renewed by June 30, ~~2011~~2012 must be included with the direct portion. The other two file(s) must contain the FHCF exposure which was assumed from each Citizens entity (one file for each entity) and which was not renewed onto your company's book by June 30, ~~2011~~2012. Providing they are clearly labeled, all files may be submitted on the same diskette or CD-ROM.

**Note: All data for an individual company should be submitted at the same time.** If your company has different departments responsible for compiling portions of your data submission, please have one individual coordinate, compile, and submit the complete package to the Administrator.

For the purpose of this Data Call, each Citizens entity shall submit all of its FHCF exposure not subject to assumption agreements in the format specified herein. In addition, each Citizens entity shall report all FHCF exposure removed from the applicable Citizens entity which, as of June 30, ~~2011~~2012, had not been renewed onto the assuming insurer's policy forms. Such a file is required for each assumption company. Each file shall be reported in the Data Call format specified herein and shall be accompanied by a Control Totals Form.

**The FHCF will compare the file(s) submitted by an assumption company against the file(s) submitted by Citizens and the assumption company will be required to explain discrepancies.**

The FHCF recognizes that policyholders receiving a notice of assumption from an assumption company can opt to not have their policy assumed any time during the policy period. For purposes of reporting assumed policies to the FHCF, Citizens and the assuming company must track the date the policyholder notified the assumption company or Citizens rejecting the assumption company's offer of coverage since the policy is required to be reported to the FHCF based on its status at June 30th. Any decision made by the policyholder to opt out of the assumption after June 30th will not be recognized for exposure reporting purposes by the FHCF and should not affect how the policy is reported. Furthermore, any retroactive coverage changes subsequent to June 30th will not be considered by the FHCF and will not impact Data Call reporting for Citizens or the assuming insurer.

All exposure files requested from the two Citizens entities and insurers engaged in removing exposure from either Citizens entity pursuant to an assumption agreement are subject to examination by the SBA and must be retained as specified under **Retention of Records for SBA Examination** on page 5 herein.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Citizens Property Insurance Corporation ~~High Risk~~ Coastal Account Quota Share Primary Insurance Reporting Requirements

Section 627.351(6)(c)2.f, Florida Statutes, requires that "For all eligible risks covered under quota share primary insurance agreements, the exposure and coverage levels for both the corporation and authorized insurers shall be reported by the corporation to the Florida Hurricane Catastrophe Fund. For all policies of eligible risks covered under quota share primary insurance agreements, the corporation and the authorized insurer shall maintain complete and accurate records for the purpose of exposure and loss reimbursement examinations as required by Florida Hurricane Catastrophe Fund rules. The corporation and the authorized insurer shall each maintain duplicate copies of policy declaration pages and supporting claims documents."

Citizens Property Insurance Corporation ~~High Risk~~ Coastal Account (referred to hereafter on this page as Citizens) shall report all quota share primary insurance exposure data to the FHCF in a separate file meeting the requirements below. **Individual insurers shall not report any such exposure to the FHCF.**

1. File must include quota share primary insurance exposure for all insurers engaged in quota share primary insurance agreements;
2. File must include all data fields as specified in this Data Call; and
3. In addition to the data fields specified in this Data Call, the file must include the following two fields:
   - Field #19: Five-character numeric field indicating NAIC# of insurer for each record reported, and
   - Field #20: Two-character numeric field indicating Citizens' specified percentage of hurricane coverage of the risks reported in a specific record, as set forth in the quota share primary insurance agreement between Citizens and an insurer.
4. A separate SBA exam file, as specified on pages 5-6 of this Data Call, shall also be prepared for this data. The two fields specified immediately above shall be included as fields #23-24 of the SBA exam file.

Based on the separate Data Call file, the FHCF shall:

- Calculate the aggregate FHCF premium, based on the Reimbursement Premium Formula as discussed on page 1 of this Data Call, by insurer;
- Based upon the specified Citizens' percentage of hurricane coverage, allocate the applicable share of FHCF premium to Citizens and to each insurer;
- The allocated premium from above will be added to the FHCF premium calculated from non-quota share primary insurance for Citizens and for each insurer participating in a quota share primary insurance agreement(s) with Citizens; and
- This aggregate premium shall be used for the calculation of retentions and FHCF reimbursements.

When reporting loss information to the FHCF, Citizens and insurers will be required to report only their respective portion of losses under quota share primary insurance agreements.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## FHCF Construction Codes

The construction code identifies the material with which the building is constructed.

| Construction Type/Definition | FHCF Code |
|---|---|
| *Frame*<br>Buildings where the exterior walls are wood or other combustible materials, including wood iron-clad, stucco on wood, or plaster on combustible supports. Also includes aluminum or plastic siding over frame. If a company's definition of frame includes hardiboard, FHCF Frame construction should be used[1]. | 1 |
| *Masonry*<br>Buildings where the exterior walls are constructed of masonry, non-combustible, or fire resistive materials such as adobe, brick, concrete, gypsum block, hollow concrete block, stone, tile or other non-combustible materials. | 2 |
| *Masonry with Reinforced Concrete Roof*<br>Construction meeting the definition of FHCF Masonry construction, as outlined above, and having a reinforced concrete roof. | 15 |
| *Superior*<br>Masonry, non-combustible, or fire resistive construction where one of the following additional conditions exist:<br>▪ Roof deck has a minimum thickness of 2 inches with roof supports having a minimum dimension of 6 inches; or<br>▪ Floors and roof constructed of 2 inches of masonry on steel supports or documented to be constructed of 22 gauge metal or heavier on steel supports; or<br>▪ Roof assembly is documented to have a UL wind uplift classification of 90 or equivalent.<br>**Or**<br>A building of any construction which is 6 or more stories. | 7 |
| *Superior with Reinforced Concrete Roof*<br>Construction meeting the definition of FHCF Superior construction, as outlined above, and having a reinforced concrete roof. | 16 |
| *Masonry Veneer*<br>Buildings with exterior walls of combustible construction veneered with brick, masonry, or stone. If a company's definition of veneer includes hardiboard, FHCF Masonry Veneer construction should be used[1]. | 10 |
| *Unknown*<br>Construction information not collected for the policy or the reportable exposure. Not valid for mobile home or mobile home-related exposure. | 11 |
| *Non-Mobile Home Default Construction*<br>Construction information collected for the policy, but company is eligible to report all non-mobile home exposure using this default code. See page 9 for restrictions on the use of this default. | 12 |

*Mobile Home - Fully Tied Down, manufactured before 7/13/94*[2] 21

Mobile/Manufactured Housing, manufactured before 7/13/94, which has anchors and tie-downs as required by Section 320.8325, Florida Statutes, and Florida Administrative Code rules promulgated thereunder.

*Mobile Home - Fully Tied Down, manufactured on or after 7/13/94*[2] 22

Mobile/Manufactured Housing which has anchors and tie-downs as required by Section 320.8325, Florida Statutes, and Florida Administrative Code rules promulgated thereunder, and was manufactured on or after 7/13/94 or is documented to be in compliance with ANSI/ASCE 7-88.

*Mobile Home – Other than Fully Tied Down or Unknown* 25

Mobile home is not fully tied down, the nature of any tie downs is unknown, or tie down information is not available.

*Mobile Home Default Construction* 26

Construction information collected for the policy, but company is eligible to report all mobile home exposure using this default code. See page 11 for restrictions on the use of this default.

[1]If your company has a specific rate for hardiboard construction (i.e., a rate other frame or veneer), a proposed mapping must be submitted to the FHCF Administrator as specified on page 9 herein.

[2]If you are uncertain whether a mobile home was manufactured on or after 7/13/94, use the manufactured before 7/13/94 code "21." If your company only tracks the year built and not the month, use code "21."

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Florida County Codes*

| County Code | County Name | County Code | County Name | County Code | County Name |
|---|---|---|---|---|---|
| 001 | Alachua | 049 | Hardee | 093 | Okeechobee |
| 003 | Baker | 051 | Hendry | 095 | Orange |
| 005 | Bay | 053 | Hernando | 097 | Osceola |
| 007 | Bradford | 055 | Highlands | 099 | Palm Beach |
| 009 | Brevard | 057 | Hillsborough | 101 | Pasco |
| 011 | Broward | 059 | Holmes | 103 | Pinellas |
| 013 | Calhoun | 061 | Indian River | 105 | Polk |
| 015 | Charlotte | 063 | Jackson | 107 | Putnam |
| 017 | Citrus | 065 | Jefferson | 109 | St. Johns |
| 019 | Clay | 067 | Lafayette | 111 | St. Lucie |
| 021 | Collier | 069 | Lake | 113 | Santa Rosa |
| 023 | Columbia | 071 | Lee | 115 | Sarasota |
| 027 | De Soto | 073 | Leon | 117 | Seminole |
| 029 | Dixie | 075 | Levy | 119 | Sumter |
| 031 | Duval | 077 | Liberty | 121 | Suwannee |
| 033 | Escambia | 079 | Madison | 123 | Taylor |
| 035 | Flagler | 081 | Manatee | 125 | Union |
| 037 | Franklin | 083 | Marion | 127 | Volusia |
| 039 | Gadsden | 085 | Martin | 129 | Wakulla |
| 041 | Gilchrist | 086 | Miami-Dade | 131 | Walton |
| 043 | Glades | 087 | Monroe | 133 | Washington |
| 045 | Gulf | 089 | Nassau | | |
| 047 | Hamilton | 091 | Okaloosa | | |

* Derived from the Federal Information Processing Standards (FIPS) Codes.

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Reference Guide

The FHCF is dedicated to making information pertaining to the FHCF as readily available as possible, and has posted a considerable amount of information on the Internet through both the FHCF (www.sbafla.com/fhcf/) and Paragon (http://fhcf.paragon.aonbenfield.com) web sites.

The following are sample documents/information available on-line:

- Bonding Estimates
- FHCF Calendar
- Contact Request Form (Insurer Contacts)
- Coverage Selections & Premium Calculations
- Data Call
- Examination Information
- Frequently Asked Questions
- Link: FEMA
- Link: Florida Administrative Weekly
- Link: Florida Department of Financial Services
- Link: Online Sunshine
- Loss Reimbursement Preparedness Program
- Loss Reports
- Member Handbook
- Projected Payout Multiple
- Ratemaking Formula Report and Addendum(s), as applicable
- Rates and Retention Multiples
- Reimbursement Contract and Addendum(s), as applicable
- Rule 19-8.010: Reimbursement Contract
- Rule 19-8.012: Ineligibility/Exemption from the FHCF
- Rule 19-8.013: Revenue Bonds
- Rule 19-8.028: Reimbursement Premium Formula
- Rule 19-8.029: Insurer Reporting Requirements
- Rule 19-8.030: Insurer Responsibilities
- Section 215.555, Florida Statutes

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Submission Checklist

### Due September 1, ~~2011~~2012

Please provide us with the following information and return this checklist with your exposure data:

**Company Name:** _____ **NAIC No**. _____

| Item | Included? |
|---|---|
| Exposure Data File | Y / N |
| Completed Submission Checklist (page 29) | Y / N |
| Brief Written Verification of Exposure Fluctuations (criteria on page 4) | Y / N |
| Completed Control Totals Form (page 30) | Y / N |
| Completed Statement of Exposure Data Validity (page 31) | Y / N |
| Completed Statement of Retention of Exam File (page 32) | Y / N |
| Completed Collateral Protection Policies Statement * (page 33) | Y / N |
| *The above Statement is required only for Companies writing Collateral Protection Policies | |
| Validation Printouts (optional) | Y / N |

In the event that we have questions regarding the data submitted, please provide the name of the person responsible for data collection:

| | |
|---|---|
| Name | Telephone Number |
| Title | Facsimile Number |
| Street Address (not P.O. Box) | E-Mail Address |
| City, State, ZIP | |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Control Totals Form

**Due September 1, ~~2011~~2012**

Please complete this form, verify that the totals match both your Data Call submission file and your SBA exam file, and return to Paragon along with your exposure data.

**Company Name**: _____ **NAIC No.** _____

| FHCF Type of Business | Insured Risks | Total Insured Value (Exposure) | | | |
|---|---|---|---|---|---|
| | | Building | Appurtenant Structures | Contents | ALE |
| Commercial | _____ | _____ | _____ | _____ | _____ |
| Residential | _____ | _____ | _____ | _____ | _____ |
| Mobile Home | _____ | _____ | _____ | _____ | _____ |
| Tenants | _____ | _____ | _____ | _____ | _____ |
| Condominium Unit Owners | _____ | _____ | _____ | _____ | _____ |
| Totals | _____ | _____ | _____ | _____ | _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due September 1, ~~2011~~2012**

## Statement of Exposure Data Validity

on behalf of

_____
(Company Name)

We, the undersigned, do state that, to the best of our knowledge, the attached data provided by the captioned Company to the State Board of Administration of Florida (SBA) under Section 215.555(5)(c), Florida Statutes, is complete and accurate.

**The validity of all exposure data sets received by Paragon is subject to examination by the SBA.**

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration, and we have conducted, or have had conducted, a thorough review of said Company's records and systems to determine the truth of this statement.

| | |
|---|---|
| **BY:** _____ Signature | **BY**: _____ Signature |
| **NAME:** _____ Typed/Printed | **NAME:** _____ Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due September 1, ~~2011~~2012**

## Statement of Retention of Exam File

on behalf of

_____
(Company Name)

We, the undersigned, state that the State Board of Administration of Florida (SBA) exam file referenced on pages 5-6 of this Data Call has been produced by the captioned Company in accordance with the required specifications and that the SBA exam file will be retained and maintained by the captioned Company in a secure location. We understand that the SBA exam file will be used when the FHCF conducts an examination of the captioned Company's exposure submission for this Contract Year. The captioned Company will provide the SBA exam file to the FHCF or its designated representative upon notification that an exposure examination for this Contract Year has been scheduled. The captioned Company recognizes that the exposure examination will require documentation in addition to the SBA exam file.

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration, and we have conducted, or have had conducted, a thorough review of the said Company's records and systems to determine the truth of this statement. We understand that our SBA exam file should be generated at the same time our Data Call file is created, and that data fields common to both the Data Call file and the SBA exam file must be the same. We acknowledge that if it is determined, subsequent to our Data Call submission, that these files are not in agreement, our company will be required to resubmit both files and will be subject to a $1,000 resubmission fee for each resubmission.

| | |
|---|---|
| **BY:** _____<br>Signature | **BY:** _____<br>Signature |
| **NAME:** _____<br>Typed/Printed | **NAME:** _____<br>Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due September 1, ~~2011~~2012**

## Collateral Protection Statement

(This form may be disregarded if not applicable to your company)

on behalf of

_____

(Company Name)

We, the undersigned, acknowledge that the captioned Company writes collateral protection policies covering personal residences in the State of Florida that protect both the borrower's and the lender's financial interest, in an amount at least equal to the coverage for the dwelling in place under the lapsed homeowner's policy. We understand that, as referenced in Section 215.555(2)(c), Florida Statutes, for such policies to be covered by the FHCF, our Company must be able to accurately report exposure information for those policies as required in Section 215.555(5), and specifically, as outlined in this Data Call.

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration. We have conducted, or have had conducted, a thorough review of said Company's records to determine whether all necessary information required for collateral protection policies to be covered by, and reported to, the FHCF, as outlined above and in this Data Call, is available for reporting (whether in a hard copy or an electronic format). Accordingly, we certify that (check appropriate box below):

☐ Said Company has collected all information necessary for such policies to be covered by, and reported to, the FHCF, as outlined in this Statement and this Data Call, and has accordingly included collateral protection exposure covered by the FHCF in this Data Call submission.

☐ Said Company **DOES NOT** have available the data as required by the premium formula as specified in Section 215.555(5), Florida Statutes, and therefore is unable to accurately report its collateral protection exposure. We understand that the said Company is ineligible to collect any reimbursements from the FHCF for losses occurring during the ~~2010~~ 2012 FHCF contract year from policies covering collateral protection exposure.

| | |
|---|---|
| **BY:** _____ Signature | **BY:** _____ Signature |
| **NAME:** _____ Typed/Printed | **NAME:** _____ Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## Supplemental Instruction Sheet for New Participants

As explained on page one of this Data Call, each authorized insurance company writing Covered Policies in the state of Florida is required to pay a reimbursement premium to the Florida Hurricane Catastrophe Fund (FHCF). This includes new participants to the FHCF. Rule 19-8.028 Reimbursement Premium Formula, Florida Administrative Code (F.A.C.), defines a new participant as a company that:

> "writes covered policies on or after the beginning of the Fund's contract year on June 1 and did not do so prior to the beginning of the contract year, or if it removes exposure from Citizens Property Insurance Corporation pursuant to an assumption agreement on or after June 1 and had written no other covered policies before June 1."

Rule 19-8.028, F.A.C., requires that a new participant report its insured values under Covered Policies **as of December 31, ~~2011~~2012** by March 1, ~~2012~~2013. To comply with this requirement, please use the ~~2010~~ 2012 Data Call instructions, keeping the following points in mind:

- All references to data as of June 30, ~~2011~~2012 should be as of December 31, ~~2011~~2012 for new participants.
- The Data Call submission for new participants is due by March 1, ~~2012~~2013. Extensions will not be granted.
- The forms included in this supplemental should be used when compiling and submitting your company's data.
- All references to exposure fluctuations from the prior year may be disregarded.

If you have any questions about the information to be supplied as a new participant, please do not hesitate to call Holly Bertagnolli, Martin Helgestad, or Kathy Mackenthun of Paragon Strategic Solutions Inc. at 1-800-689-FUND (3863).

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## New Participants Submission Checklist

**Due March 1, ~~2012~~2013**

Please provide us with the following information and return this checklist with your exposure data:

**Company Name:** _____ **NAIC No.:** _____

| Item | Included? |
|---|---|
| Exposure Data File | Y / N |
| Completed New Participants Submission Checklist (page 35) | Y / N |
| Completed New Participants Control Totals Form (page 36) | Y / N |
| Completed New Participants Statement of Exposure Data Validity (page 37) | Y / N |
| Completed New Participants Statement of Retention of Exam File (page 38) | Y / N |
| Completed New Participants Collateral Protection Policies Statement * (page 39) | Y / N |
| *The above Statement is required only for Companies writing Collateral Protection Policies | |
| Validation Printouts (optional) | Y / N |

In the event that we have questions regarding the data submitted, please provide the name of the person responsible for data collection:

| | |
|---|---|
| Name | Telephone Number |
| Title | Facsimile Number |
| Street Address (not P.O. Box) | E-Mail Address |
| City, State, ZIP | |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

## New Participants Control Totals Form

**Due March 1, ~~2012~~2013**

Please complete this form, verify that the totals match both your Data Call submission file and your SBA exam file, and return to Paragon along with your exposure data.

**Company Name**: _____ **NAIC No.** _____

| FHCF Type of Business | Insured Risks | Total Insured Value (Exposure) | | | |
|---|---|---|---|---|---|
| | | Building | Appurtenant Structures | Contents | ALE |
| Commercial | _____ | _____ | _____ | _____ | _____ |
| Residential | _____ | _____ | _____ | _____ | _____ |
| Mobile Home | _____ | _____ | _____ | _____ | _____ |
| Tenants | _____ | _____ | _____ | _____ | _____ |
| Condominium Unit Owners | _____ | _____ | _____ | _____ | _____ |
| Totals | _____ | _____ | _____ | _____ | _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due March 1, ~~2012~~2013**

## New Participants Statement of Exposure Data Validity

on behalf of

_____
(Company Name)

We, the undersigned, do state that, to the best of our knowledge, the attached data provided by the captioned Company to the State Board of Administration of Florida (SBA) under Section 215.555(5)(c), Florida Statutes, is complete and accurate.

**The validity of all exposure data sets received by Paragon is subject to examination by the SBA.**

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration, and we have conducted, or have had conducted, a thorough review of said Company's records and systems to determine the truth of this statement.

| | |
|---|---|
| **BY:** _____ Signature | **BY:** _____ Signature |
| **NAME:** _____ Typed/Printed | **NAME:** _____ Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due March 1, ~~2012~~2013**

## New Participants Statement of Retention of Exam File

on behalf of

_____
(Company Name)

We, the undersigned, state that the State Board of Administration of Florida (SBA) exam file referenced on pages 5-6 of this Data Call has been produced by the captioned Company in accordance with the required specifications and that the SBA exam file will be retained and maintained by the captioned Company in a secure location. We understand that the SBA exam file will be used when the FHCF conducts an examination of the captioned Company's exposure submission for this Contract Year. The captioned Company will provide the SBA exam file to the FHCF or its designated representative upon notification that an exposure examination for this Contract Year has been scheduled. The captioned Company recognizes that the exposure examination will require documentation in addition to the SBA exam file.

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration, and we have conducted, or have had conducted, a thorough review of the said Company's records and systems to determine the truth of this statement. We understand that our SBA exam file should be generated at the same time our Data Call file is created, and that data fields common to both the Data Call file and the SBA exam file must be the same. We acknowledge that if it is determined, subsequent to our Data Call submission, that these files are not in agreement, our company will be required to resubmit both files and will be subject to a $1,000 resubmission fee for each resubmission.

| | |
|---|---|
| **BY:** _____ Signature | **BY:** _____ Signature |
| **NAME:** _____ Typed/Printed | **NAME:** _____ Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

**RETURN TO PARAGON**

# Florida Hurricane Catastrophe Fund
# ~~2011~~2012 Data Call

Pursuant to Section 215.555(5)(c), Florida Statutes

**Due March 1, ~~2012~~2013**

## New Participants Collateral Protection Statement

(This form may be disregarded if not applicable to your company)

on behalf of

_____

(Company Name)

We, the undersigned, acknowledge that the captioned Company writes collateral protection policies covering personal residences in the State of Florida that protect both the borrower's and the lender's financial interest, in an amount at least equal to the coverage for the dwelling in place under the lapsed homeowner's policy. We understand that, as referenced in Section 215.555(2)(c), Florida Statutes, for such policies to be covered by the FHCF, our Company must be able to accurately report exposure information for those policies as required in Section 215.555(5), and specifically, as outlined in this Data Call.

We are each, respectively, executive officers of said Company, acting within our authority in making this declaration. We have conducted, or have had conducted, a thorough review of said Company's records to determine whether all necessary information required for collateral protection policies to be covered by, and reported to, the FHCF, as outlined above and in this Data Call, is available for reporting (whether in a hard copy or an electronic format). Accordingly, we certify that (check appropriate box below):

☐ Said Company has collected all information necessary for such policies to be covered by, and reported to, the FHCF, as outlined in this Statement and this Data Call, and has accordingly included collateral protection exposure covered by the FHCF in this Data Call submission.

☐ Said Company **DOES NOT** have available the data as required by the premium formula as specified in Section 215.555(5), Florida Statutes, and therefore is unable to accurately report its collateral protection exposure. We understand that the said Company is ineligible to collect any reimbursements from the FHCF for losses occurring during the ~~2010~~ 2012 FHCF contract year from policies covering collateral protection exposure.

| | |
|---|---|
| **BY:** _____ Signature | **BY:** _____ Signature |
| **NAME:** _____ Typed/Printed | **NAME:** _____ Typed/Printed |
| **TITLE:** _____ | **TITLE:** _____ |
| **DATE:** _____ | **DATE:** _____ |

End of Section

**STATE BOARD OF ADMINISTRATION OF FLORIDA**

**1801 HERMITAGE BOULEVARD**
**TALLAHASSEE, FLORIDA 32308**
**(850) 488-4406**

**POST OFFICE BOX 13300**
**32317-3300**

**RICK SCOTT**
**GOVERNOR**
**AS CHAIRMAN**

**JEFF ATWATER**
**CHIEF FINANCIAL OFFICER**
**AS TREASURER**

**PAM BONDI**
**ATTORNEY GENERAL**
**AS SECRETARY**

**ASH WILLIAMS**
**EXECUTIVE DIRECTOR & CIO**

# M E M O R A N D U M

**TO:** Honorable Rick Scott
Honorable Jeff Atwater
Honorable Pam Bondi

**FROM:** Ash Williams

**DATE:** March 20, 2012

**SUBJECT:** Appointment of Charles E. Cobb to the Investment Advisory Council

---

Charles E. Cobb has been appointed to serve on the Investment Advisory Council. Pursuant to Section 215.444, F.S., upon approval of the appointment by the Trustees, the appointment will be submitted to the Florida Senate for confirmation during the next legislative session.

**Charles E. Cobb**

**P.O. Box 14-4200** **305-441-1700 t / 305-445-5674 f**
**Coral Gables, FL 33114-4200** **ccobb@cobbpartners.com**

Corporate Career: Chuck Cobb is the CEO and Senior Managing Director of Cobb Partners, Ltd., an investment firm. He was the Chairman and Chief Executive Officer of Arvida Corporation and Disney Development Company during the 1970s and 1980s. Arvida was a public company and then a subsidiary of Penn Central and later of Walt Disney Company. He also served as a member of the Walt Disney Board of Directors and the Executive Committee of the Disney Board. Earlier he was the Chief Operating Officer and a Director of Penn Central Corporation, a multi-industry company that had approximately 40,000 employees. He led a leveraged buy-out of Arvida Corporation from Penn Central with the Bass family in Texas and subsequently merged Arvida with Walt Disney. Earlier he was an investment manager with Dodge & Cox and the CEO of subsidiaries of Kaiser Aluminum.

Government Career: Ambassador Cobb was the U.S. Ambassador to Iceland during the GHW Bush Administration. During the Reagan Administration, he served as Under Secretary and Assistant Secretary at the U. S. Department of Commerce. In the 1950s he served as an Officer in the United States Navy. Florida Governors, Jeb Bush and Charlie Crist, appointed Ambassador Cobb as Chairman of Florida FTAA and Gateway Florida which have the responsibility for Florida's international trade agenda. Ambassador Cobb created the Cobb Award for Export Advocacy within the U.S. Department of State that is awarded annually to the career ambassador who best leads U.S. trade policy.

Community Development Career: In his 40 years as the CEO of Arvida Corporation, Disney Development, Kaiser Community Development, and Cobb Partners, Cobb has had the responsibility for the development of more than 30 new towns and master-planned communities.

Education Involvement: Cobb was educated at Stanford University where he received a BA and MBA. He is the past Chairman of the Board of Trustees of the University of Miami, having been the Chairman, Vice Chairman or past Chairman of the Trustees for over 35 years. He is a former Trustee of the Stanford Business School Trust Fund, a member of the Advisory Council for the Stanford Business School, and the past President of two Stanford alumni organizations. He was the Chairman of the Board of the Florida Business/Higher Education Partnership, the Co-Founder and Trustee of the Barry University Charter School, a Director of the South Florida Annenberg Challenge, a Director of the Council for Educational Change and a former member of the Florida Governor's Commission on Education.

Directorships and Civic Affairs: Cobb has served on the Boards of nine publicly-traded corporations (Arvida, Penn Central, Walt Disney, LNR Property Corporation, WCI Communities, Ameritas, Pan Am Corporation, CLC of America, and Southeast Banking) and many private corporate boards (Florida Savings, Kirkwood, Durango, Telluride, Tubac, and Observer Group). Cobb has been an officer and/or member of the Executive Committee of The Florida Council of 100 (Chairman 2000-2002), Florida Chamber of Commerce, the South Florida Coordinating Council, the Greater Miami Chamber of Commerce and several other economic development organizations. Cobb also serves on the Board and the Investment Committee for the University of Miami, Woodrow Wilson International Center for Scholars, Eisenhower Fellowships, Orange Bowl Committee, Council of American Ambassadors and Cobb Family Foundation. He was the Co-Chairman of the committee that secured $9 billion of federal funds for South Florida after Hurricane Andrew. Other civic boards and memberships include Plymouth Congregational Church, The American-Scandinavian Foundation, the Icelandic-American Chamber of Commerce, Orange Bowl Committee, Council on Foreign Relations, the Urban Land Institute, and the Lincoln Institute of Land Policy.

Honors: Cobb has received the Order of the Falcon Grand Cross Star from the Nation of Iceland (Iceland's highest honor to a non-Icelandic citizen), The Florida Council of 100 Governor's Award, the NCCJ Silver Medallion Award, South Florida Achievement of the Decade Award, Junior Achievement Hall of Fame, Harvard Business Club of South Florida Business Statesman of the Year, Chief Executive Officer Annual Award for the Hotel and Real Estate Industry, Honorary Doctorate from Barry University, Liberty Bell Award for Florida Higher Education and was a member of the U.S. Olympic Team as an alternate in the 110m high hurdles in 1960.

Family: Cobb has been married for 53 years to Ambassador Sue McCourt Cobb, former U.S. Ambassador to Jamaica and Secretary of State of Florida. Ambassador Sue Cobb is a lawyer, sportswoman, and author who chronicled her 1988 attempt to be the first woman from the United States to reach the summit of Mount Everest with a book entitled, *The Edge of Everest*. They have two sons, Christian (architect and Harvard MBA) and Tobin (investment banker and NYU MBA), and seven grandchildren.

End of Section

# State Board of Administration of Florida

## Major Mandate Review
## Fourth Quarter 2011

Hewitt ennisknupp
An Aon Company

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   - Market Update
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2. Pension Plan Review
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4. CAT Fund Review
5. Lawton Chiles Endowment Fund Review
6. Florida PRIME and Fund B Review
7. Appendix
   - Pension Plan Performance Report
   - Investment Plan Performance Report
   - Lawton Chiles Endowment Fund Performance Report

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# Executive Summary

Fourth Quarter 2011

Hewitt ennisknupp

An Aon Company

# Executive Summary

- The major mandates outperformed their respective benchmarks over all longer time periods through December 2011 with an exception of the FRS Investment Plan and the CAT Operating Fund. The FRS Investment Plan slightly underperformed its benchmark for the trailing one-year period and the CAT Operating Fund slightly underperformed its benchmark over the five-year period.
- 2011 was a difficult year for the equity markets, especially internationally as Europe struggled to deal with its debt issues. This was reflected in the one-year performance of the pension in the form of negative absolute returns; however, the Pension Plan was able to preserve value and outperform the benchmark for the period.
- The Investment Plan slightly underperformed during the one-year period mainly due to the underperformance of the PIMCO Total Return Fund but posted a positive absolute return due to participants' exposure to cash and bonds.
- Due to the flight to quality and concerns about inflation, the Lawton Chiles Endowment Fund benefited significantly from its allocation to Treasury Inflation-Protected Securities (TIPS) that performed very well during 2011.
- The shorter term mandates, including the CAT Fund and Florida PRIME, continued to experience subdued returns due to the low yields on short-term bonds.

# Market Update

Fourth Quarter 2011

Hewitt ennisknupp

An Aon Company

# Market Highlights

| Returns of the Major Capital Markets | | | | | |
|---|---|---|---|---|---|
| | | Annualized Periods Ending 12/31/2011 | | | |
| | Fourth Quarter | 1-Year | 3-Year | 5-Year | 10-Year |
| **Domestic Stock Indices** | | | | | |
| Russell 3000 Index | 12.1% | 1.0% | 14.9% | 0.0% | 3.5% |
| Dow Jones U.S. Total Stock Market Index | 12.1% | 1.1% | 15.2% | 0.2% | 3.9% |
| S&P 500 Index | 11.8% | 2.1% | 14.1% | -0.3% | 2.9% |
| Russell 2000 Index | 15.5% | -4.2% | 15.6% | 0.2% | 5.6% |
| **Domestic/Foreign Bond Indices** | | | | | |
| Barclays Capital Aggregate Bond Index | 1.1% | 7.8% | 6.8% | 6.5% | 5.8% |
| Barclays Capital Long Gov't Index | 1.8% | 29.1% | 7.5% | 10.8% | 8.9% |
| Barclays Capital Long Credit Index | 3.2% | 17.1% | 14.8% | 8.6% | 8.1% |
| Barclays Capital Long Gov't/Credit Index | 2.6% | 22.5% | 11.2% | 9.7% | 8.5% |
| SSB Non-U.S. WGBI | -0.5% | 5.2% | 4.9% | 7.2% | 8.4% |
| **Foreign/Global Stock Indices** | | | | | |
| MSCI All Country World IMI Index | 7.2% | -7.9% | 12.8% | -1.6% | 4.9% |
| MSCI All Country World ex-U.S. IMI Index | 3.3% | -14.3% | 11.5% | -2.7% | 7.0% |
| MSCI EAFE Index | 3.3% | -12.1% | 7.6% | -4.7% | 4.7% |
| MSCI Emerging Markets Index | 4.4% | -18.4% | 20.1% | 2.4% | 13.9% |

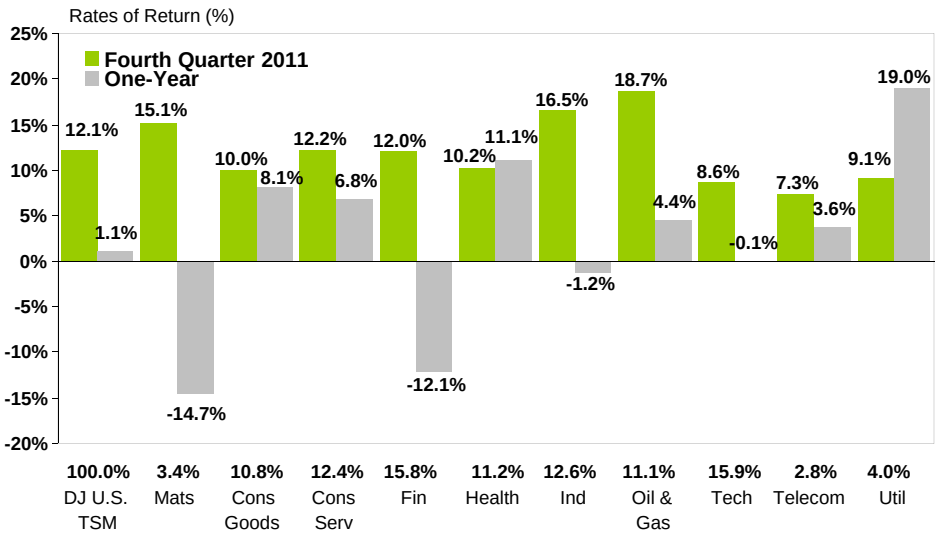
- Performance across capital markets was broadly positive during the fourth quarter. U.S. equities significantly outperformed non-U.S. markets over the quarter and full year. The rally in the U.S. equity markets during the fourth quarter was only enough to offset the losses over the prior three quarters, leaving most U.S. equity indices virtually flat for 2011. Better than expected economic data in the U.S. led to a strong “Santa’s Rally” which began in October.

- Concerns over the European debt crisis and slowing growth in emerging countries weighed on non-U.S. equities. These markets ended 2011 with double-digit negative returns.

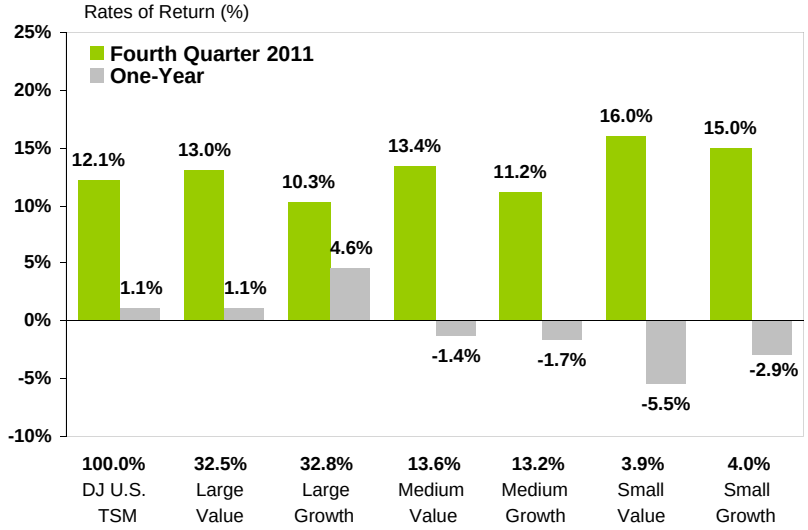
- For the year, fixed income markets generally produced strong positive returns. Higher quality, long-dated securities were rewarded. The Barclays Capital Long Government Index, consisting primarily of long duration U.S. Treasury bonds, finished the year with a 29.1% return, topping all asset classes.

# U.S. Equity Markets

**SECTOR RETURNS**
**AS OF 12/31/2011**




**STYLE RETURNS**
**AS OF 12/31/2011**




- Better than expected consumer spending data, increased manufacturing activities, as well as favorable labor market data injected a much desired level of optimism into the U.S. equity market during the fourth quarter.
- The Dow Jones Total Stock Market Index soared 12.1% during the quarter.
- All sectors within the Dow Jones Total Stock Market Index posted strong gains in the fourth quarter. Cyclical sectors outperformed defensive sectors. Oil & gas, industrials, and materials were among the top-performing sectors, returning 18.7%, 16.5%, and 15.1%, respectively.
- During the fourth quarter, risk appetite returned to the market. All areas within the market capitalization spectrum produced positive results.



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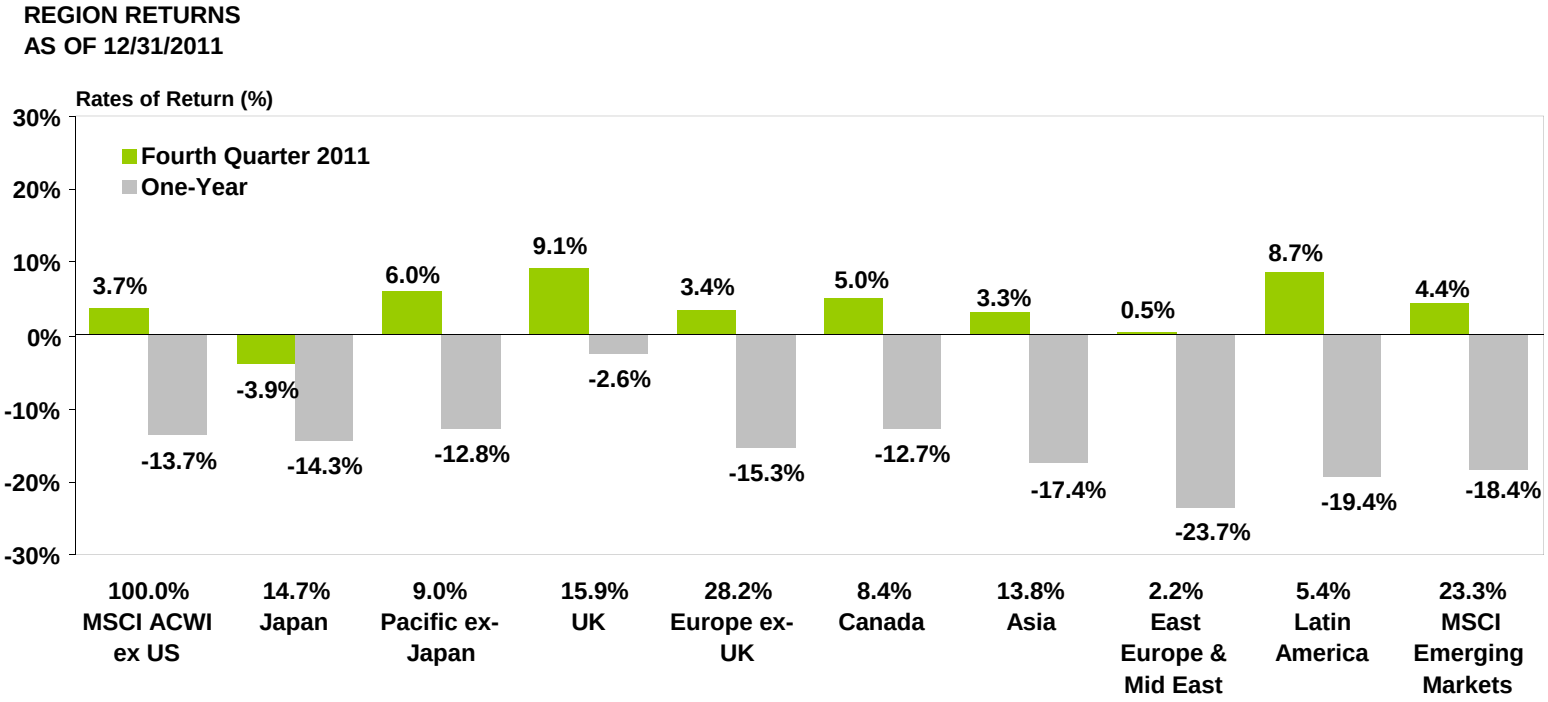
# Non-U.S. Equity Markets




- Non-U.S. equity markets gained positive momentum, originating from the U.S. market, during the fourth quarter posting a 3.7% return. All major markets (developed and emerging) posted gains during the quarter with the exception of Japan. For the year 2011, all major markets plummeted with double-digit losses, with the exception of the UK.

- Among developed markets, the UK performed the strongest, returning 9.1% for the fourth quarter. Through 2011, the UK was also the top performer, posting a mere 2.6% loss. Staying independent from the European currency union, the UK appeared to be less exposed to the European sovereign debt crisis than other major European economies.

- Among emerging markets, Peru switched swiftly from the worst market in the third quarter to the strongest one, returning 11.6% in the fourth quarter. For the year 2011, Indonesia was the only emerging market in positive territory, gaining 4.0%.



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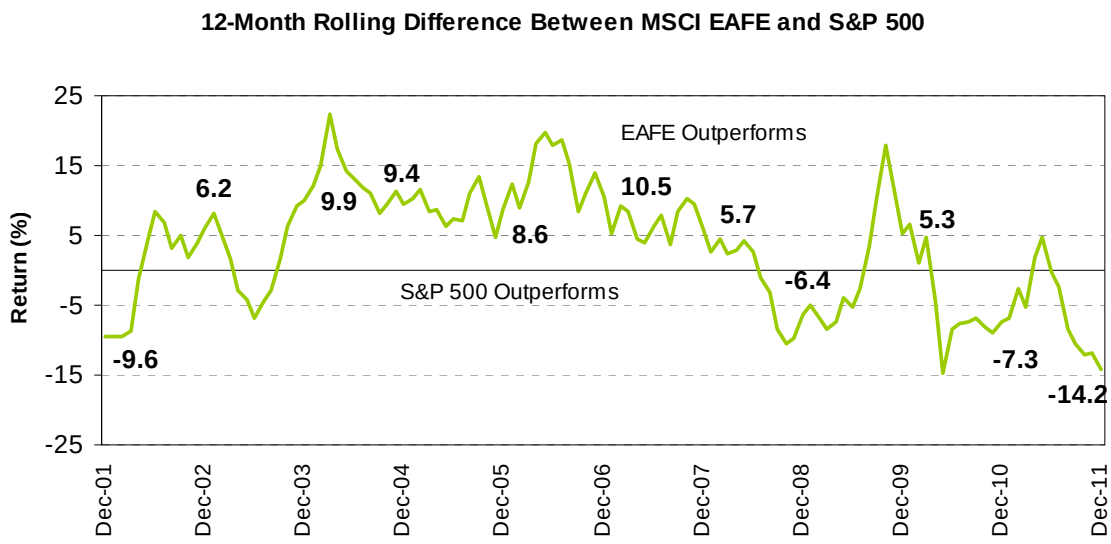
# Non-U.S. vs. U.S. Equity – Market Performance Over Time




- **2011 in Review**
  - Currency fluctuations did not have a major impact on the performance differential in 2011.
  - No single region was responsible for the performance differential (Europe -10%, Japan -14%, Australia -11%).
  - U.S. economy continues to steadily expand with outlook improving.
  - European growth prospects hampered by the sovereign debt crisis.
  - Japan's economy was destabilized by the earthquake in March in combination with a strong yen which hurt exports.
  - Australian growth prospects were lowered, due to a slowing Chinese economy and resulting drop in the demand for commodities.
  - Canadian mining companies were a drag on performance, due to lower expected commodity demand from China and Europe.

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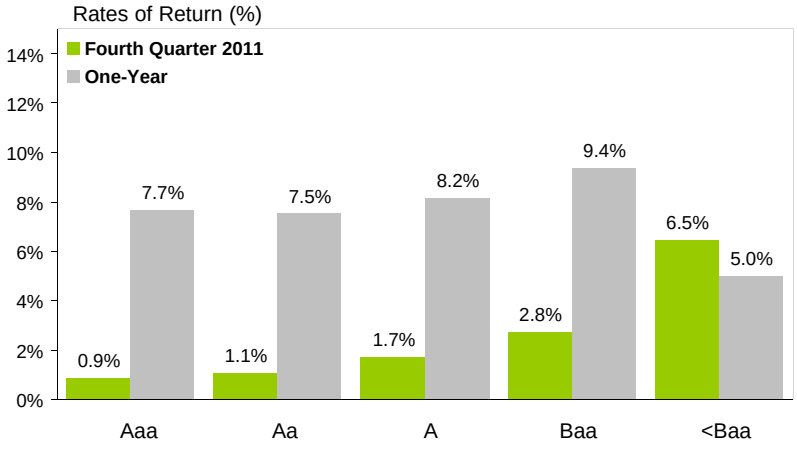
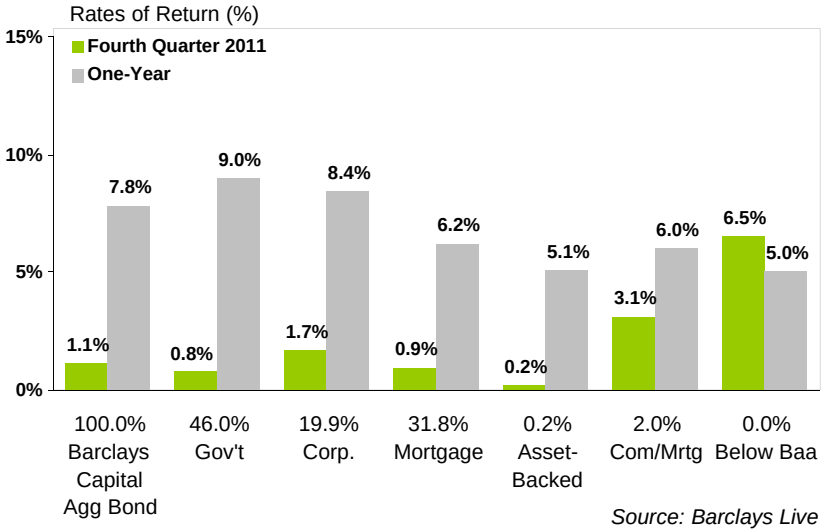
# U.S. Fixed Income Markets

**RETURNS BY QUALITY**
**AS OF 12/31/2011**




*Source: Barclays Live*

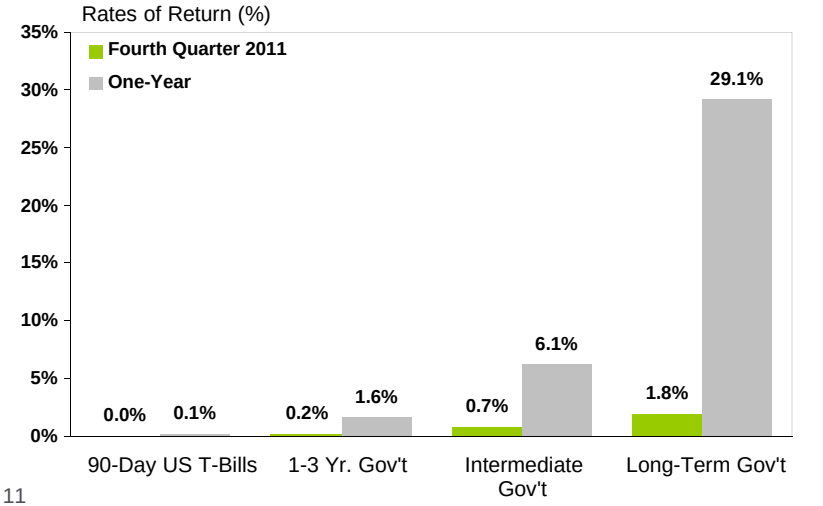
**SECTOR RETURNS**
**AS OF 12/31/2011**




*Source: Barclays Live*

- As investors increased risk appetite in October, lower credit bonds performed more strongly than higher credit bonds. Non-investment grade bonds were the top-performing sector, gaining 6.5% during the fourth quarter.
- For year 2011, Government has been the strongest sector, gaining 9.0%. Below investment-grade assets performed the worst, gaining only 5.0% in 2011.
- Along the yield curve, long-term government issues continued to outperform their short-term counterparts in the fourth quarter.
- Spreads on investment-grade, high-yield, and mortgages all tightened in the fourth quarter.

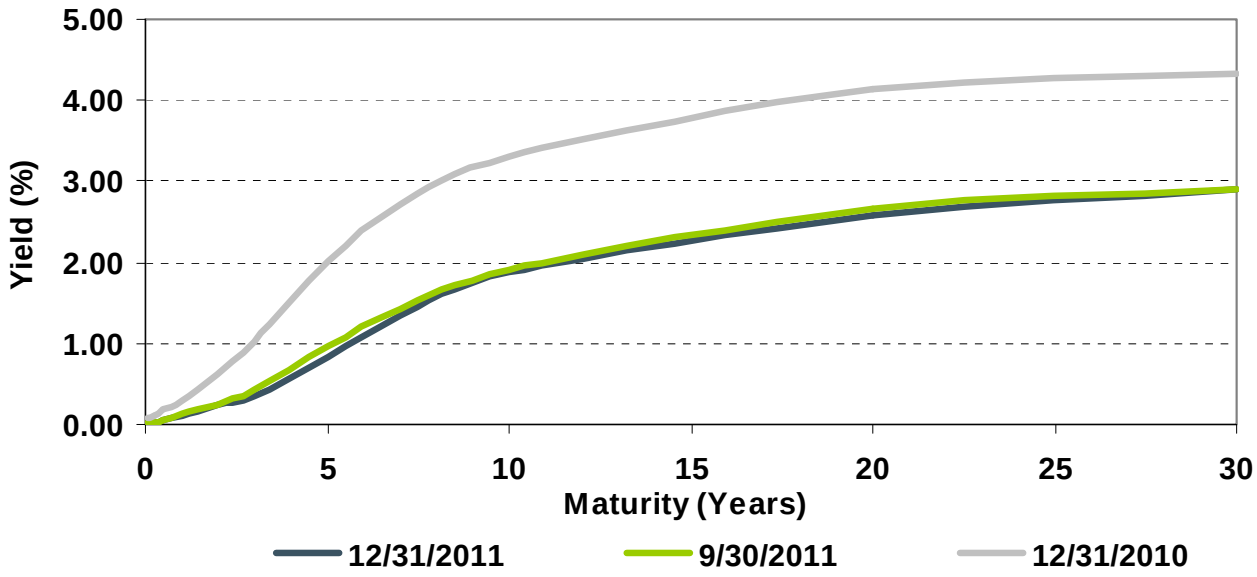
**RETURNS BY MATURITY**
**AS OF 12/31/2011**




*Source: Barclays Live*

# U.S. Fixed Income Markets

**U.S. TREASURY YIELD CURVE**




*Source: U.S. Department of Treasury*

- Prices on long-dated Treasuries rose during the last two months of 2011.
- Compared to a year ago, yields on securities with more than five years to maturity are a full percentage point lower.
- While acknowledging better than expected U.S. economic data, the Federal Open Market Committee pledged to continue to extend the maturity of its holdings and keep the federal fund rates at 0 to 0.25%.



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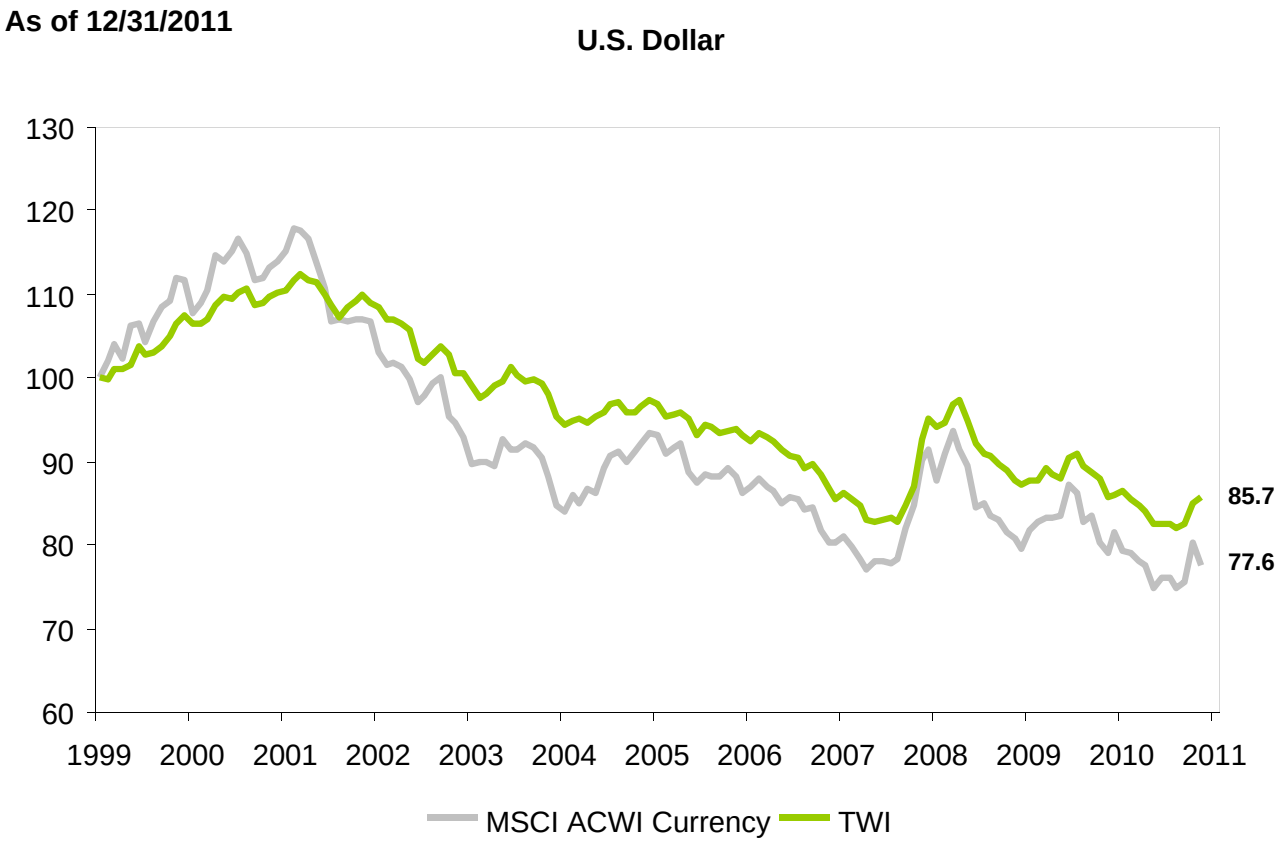
# Currency Impact




- The U.S. dollar has lost a third of its value since 2001 whether viewed from the perspective of the Trade Weighted Dollar Index (TWI) or an index comprised of currencies in an investor's typical non-U.S. equity portfolio.
- Twin deficits, as well as the more recent U.S. quantitative easing policy, have weighed on the dollar.



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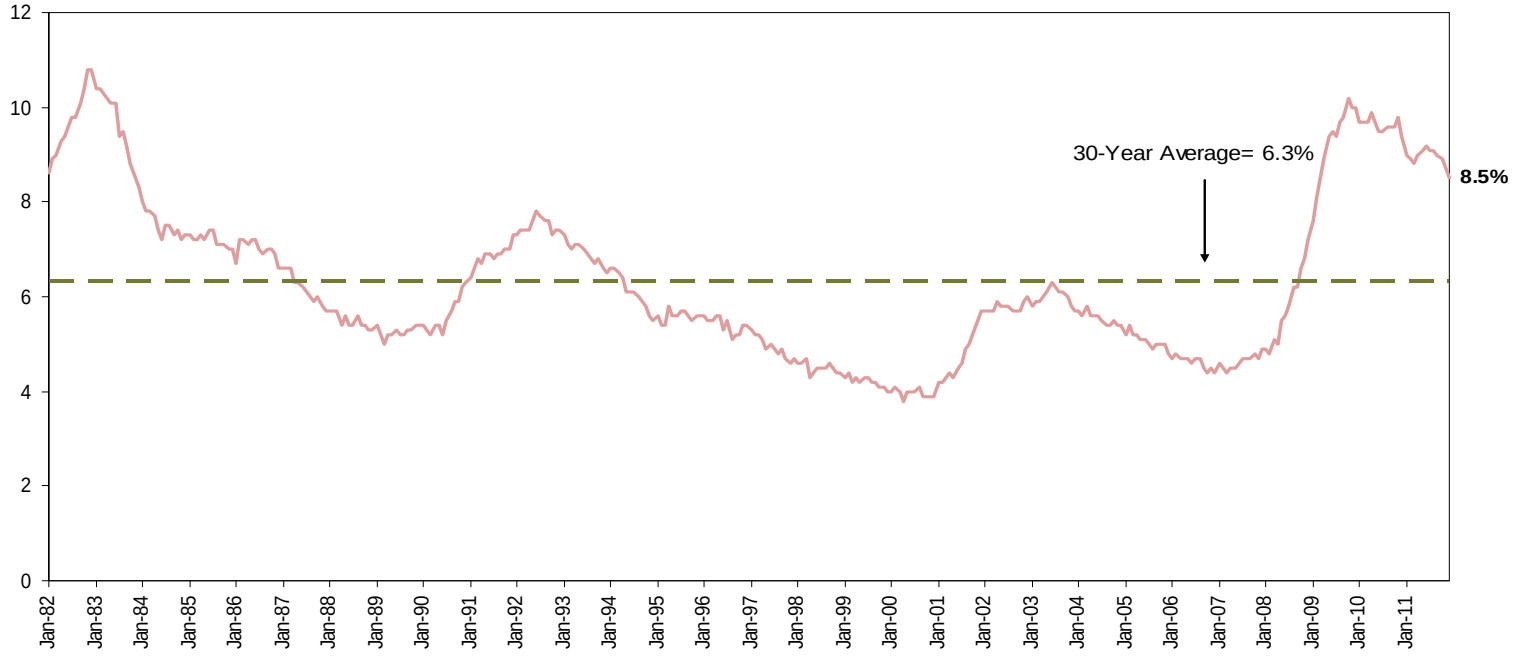
# U.S. Unemployment Rate

Unemployment Rate
As of December 2011




Source: Bureau of Labor Statistics

- During the fourth quarter, the U.S. unemployment rate declined to 8.5%, its lowest level in almost three years.
- The economy added 200,000 non-farm jobs in December, after adding 100,000 jobs in November and 80,000 in October.
- For the year, the economy has added about 1.64 million jobs, the most since 2006. The labor market still has a long way to recover the 8.75 million jobs lost in the recession that officially ended June 2009.

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# Major Mandate Investment Results
# Periods Ending 1/31/2012

| | Year-to-Date | Trailing One-Year | Trailing Three-Year | Trailing Five-Year | Trailing Ten-Year |
|---|---|---|---|---|---|
| FRS Pension Plan | 4.1% | 2.3% | 14.3% | 2.3% | 5.6% |
| *Performance Benchmark** | 4.1% | 1.7% | 13.8% | 2.0% | 5.5% |
| FRS Investment Plan | 3.4% | 3.0% | 12.4% | 2.2% | -- |
| *Total Plan Aggregate Benchmark*** | 3.1% | 2.9% | 11.8% | 1.5% | -- |
| CAT Operating Fund | 0.1% | 0.3% | 1.1% | 1.5% | 2.2% |
| *Performance Benchmark**** | 0.0% | 0.1% | 0.2% | 1.7% | 2.0% |
| CAT 2007A Fund | 0.0% | 0.3% | 0.7% | -- | -- |
| *Performance Benchmark**** | 0.0% | 0.1% | 0.2% | -- | -- |
| Lawton Chiles Endowment | 4.5% | 4.6% | 16.1% | 1.7% | 5.6% |
| *Performance Benchmark***** | 4.3% | 4.3% | 15.4% | 1.4% | 5.3% |
| Florida PRIME | 0.0% | 0.3% | 0.4% | 1.7% | 2.2% |
| *S&P AAA & AA GIP All 30 Day Net Yield Index* | 0.0% | 0.1% | 0.2% | 1.6% | 2.0% |

*A combination of the Global Equity Target, the Barclays Capital Aggregate Bond Index, the Private Equity Target, the Real Estate Investments Target, the Strategic Investments Target, and the iMoneyNet First Tier Institutional Money Market Fund Net Index.
**Aggregate benchmark returns are an average of the individual portfolio benchmark returns at their actual weights.
***A 50/50 blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Net Index.
****A combination of the custom Global Equity Target, the Barclays Capital Aggregate Bond Index, the Barclays Capital U.S. TIPS Index and the S&P U.S. AAA & AA Rated GIP 30-Day Net Index.

# State Board of Administration of Florida
# Florida Retirement System

Pension Plan Review

Fourth Quarter 2011

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# Executive Summary

- The Fund assets total $118.2 billion as of December 31, 2011, which represents a $3.8 billion increase since last quarter.
- The Pension Plan, when measured against the Performance Benchmark, underperformed for the quarter but outperformed over all longer time periods.
- Relative to the Absolute Nominal Target Rate of Return, the Pension Plan underperformed over the trailing 15-year period but outperformed over the 20- and 25-year periods.
- The Pension Plan is well-diversified across six broad asset classes, and each asset class is also well-diversified.
  - Public market asset class investments do not significantly deviate from their broad market based benchmarks, e.g., sectors, market capitalizations, global regions, credit quality, duration, and security types.
  - Private market asset classes are well-diversified by either vintage year, geography, property type, sectors, investment vehicle/asset type, and investment strategy.
  - Asset allocation is monitored on a daily basis to ensure the actual asset allocation of the plan remains close to the long-term policy targets set forth in the Investment Policy Statement.
- Hewitt EnnisKnupp and SBA staff revisit the plan design annually through informal and formal asset allocation and asset liability reviews.
- Adequate liquidity exists within the asset allocation to pay the monthly obligations of the Pension Plan consistently and on a timely basis.

# FRS Change in Market Value
# Periods Ending 12/31/2011

| Summary of Cash Flows | | |
|---|---|---|
| | **Fourth Quarter** | **Fiscal YTD*** |
| | | |
| **Beginning Market Value** | $114,463,456,426 | $128,532,863,218 |
| **+/- Net Contributions/(Withdrawals)** | ($1,368,691,680) | ($3,110,163,007) |
| **Investment Earnings** | $5,140,325,708 | ($7,187,609,757) |
| **= Ending Market Value** | $118,235,090,454 | $118,235,090,454 |
| **Net Change** | $3,771,634,028 | ($10,297,772,764) |
| | | |

*Period July 2011 - December 2011



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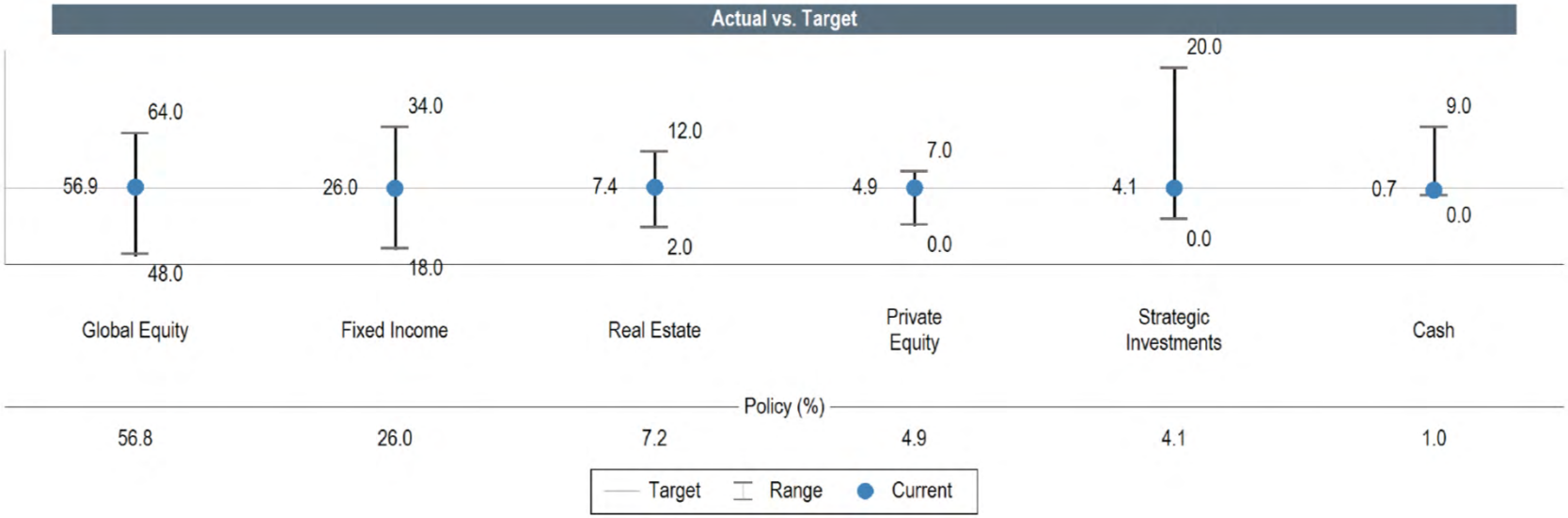
# Asset Allocation as of 12/31/2011
# Total Fund Assets = $118.2 Billion



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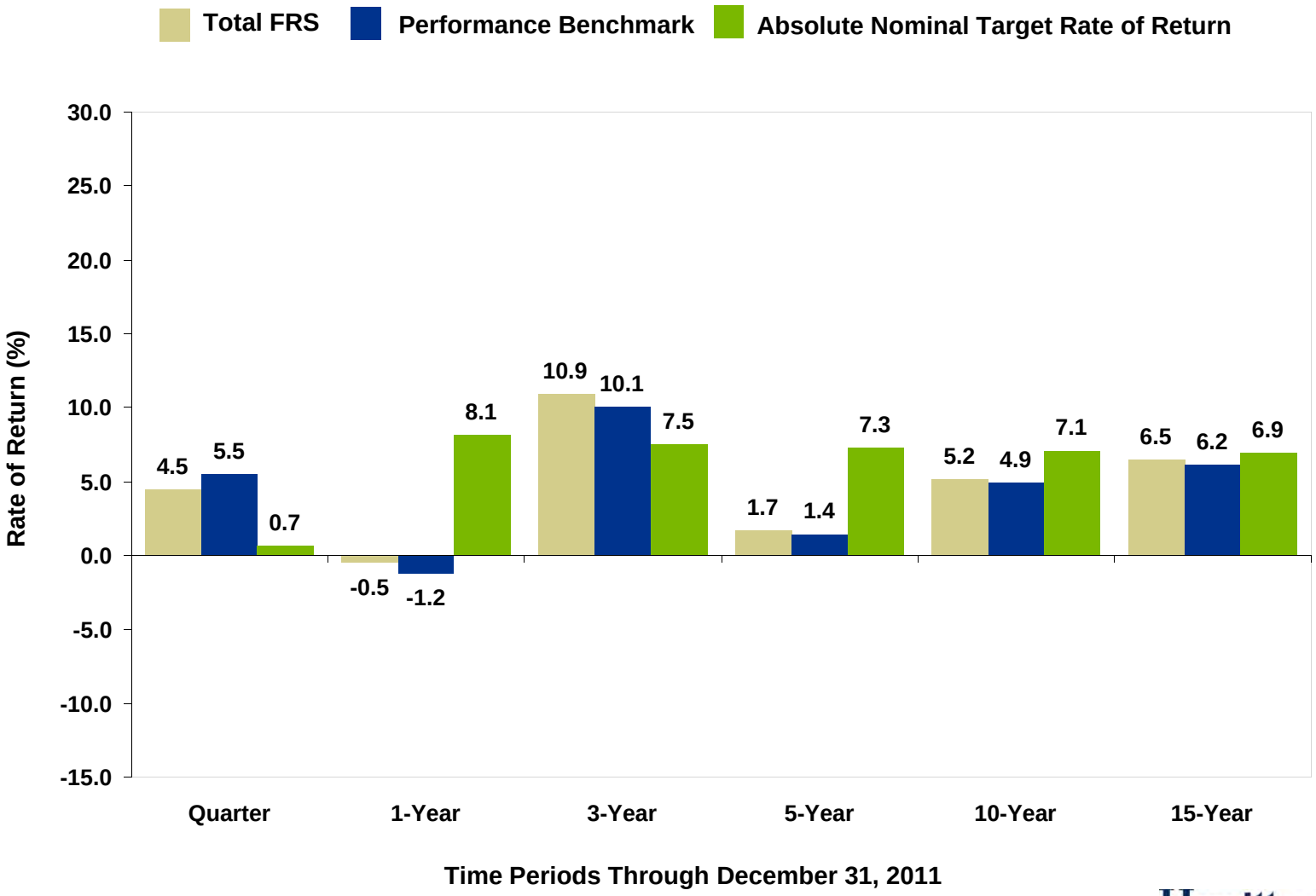
# FRS Investment Results
# Periods Ending 12/31/2011

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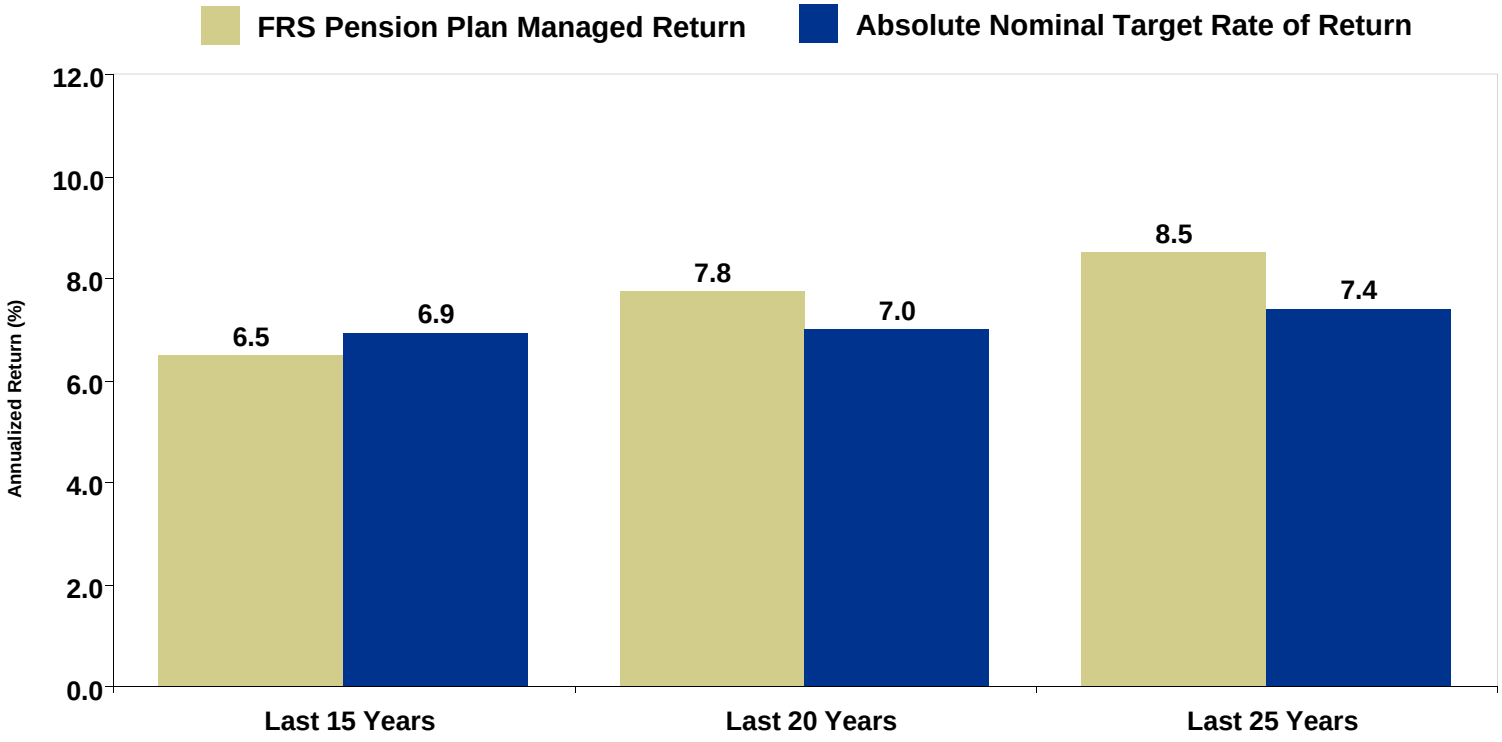
# FRS Investment Results
# Periods Ending 12/31/2011

## Long-Term FRS Pension Plan Performance Results
## vs. SBA's Long-Term Investment Objective




**Time Periods Through December 31, 2011**

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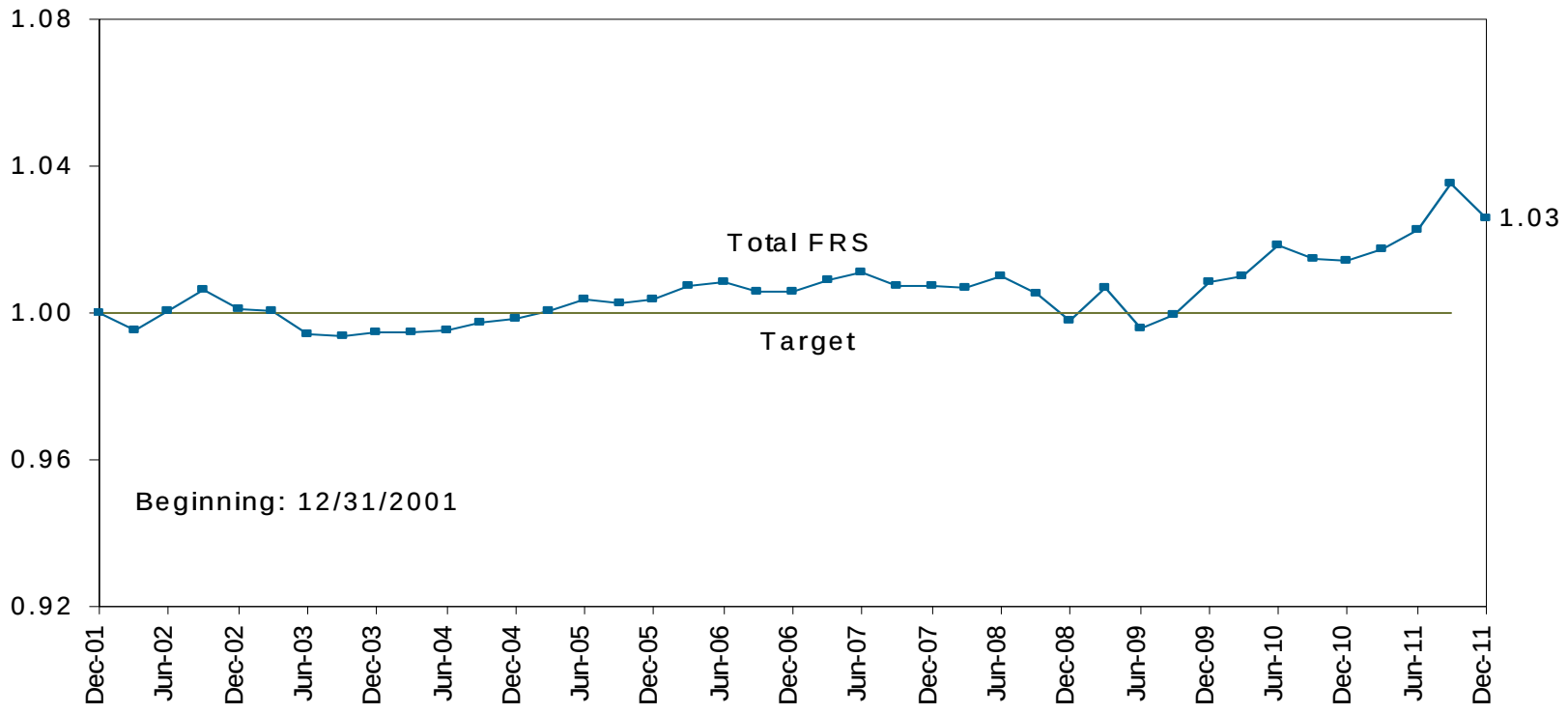
# Total FRS Cumulative Relative Performance
# 10 Years Ending 12/31/2011



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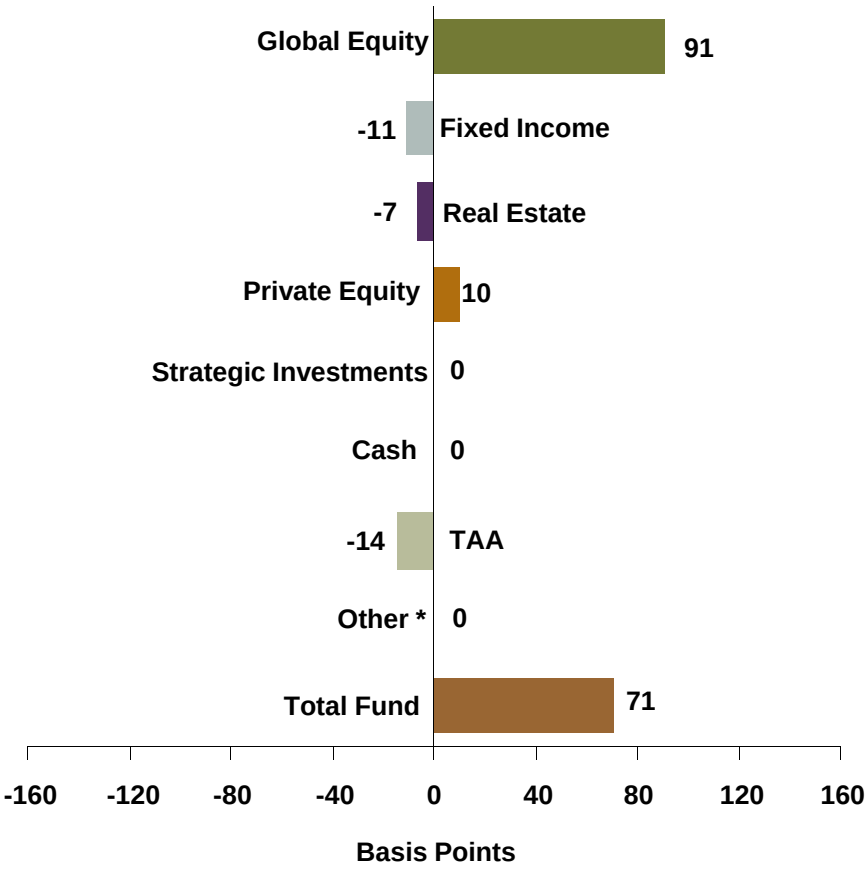
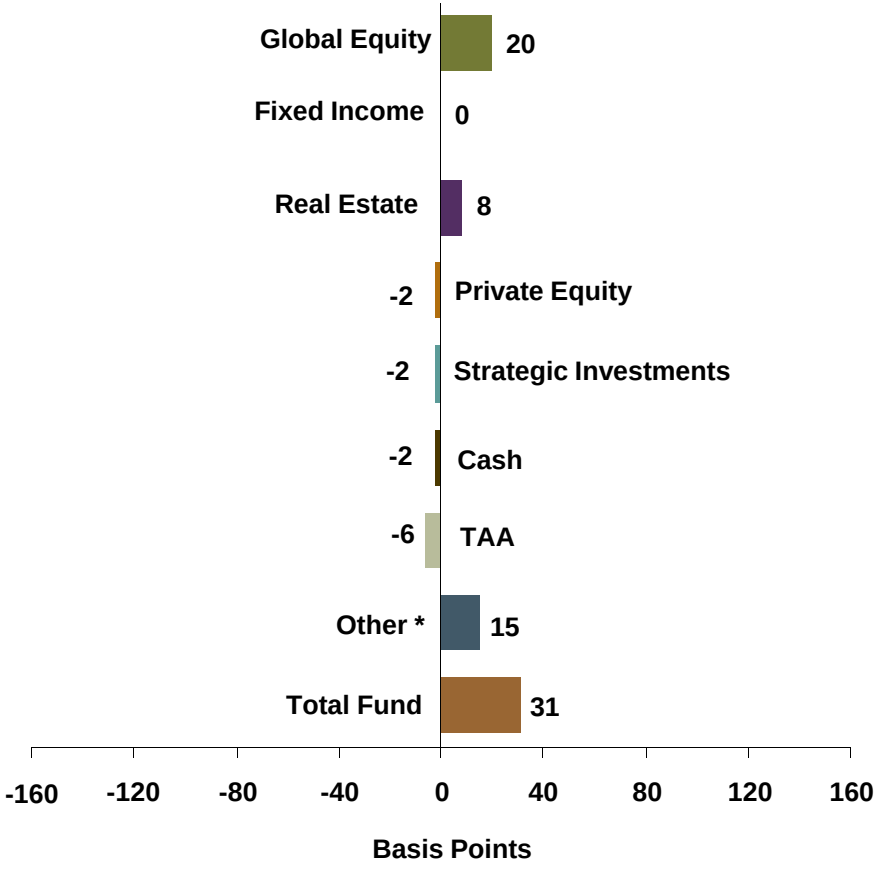
# Total FRS Attribution Analysis




1 Year Ending 12/31/2011




5 Years Ending 12/31/11

*Other includes legacy accounts, securities lending, and unexplained differences due to methodology.

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# FRS Investment Results - Trailing Period
# Periods Ending 12/31/2011

Total Fund | As of December 31, 2011 | $118,235.1 Million and 100.0% of Fund

## Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | Policy % | 2011 Q4 (%) | Rank | 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank | 10 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | Ending December 31, 2011 | | | | | | | |
| **Total Fund** | **118,235,090,454** | **100.0** | **100.0** | **4.5** | **65** | **-0.5** | **71** | **10.9** | **46** | **1.7** | **45** | **5.2** | **57** |
| *Performance Benchmark* | | | | *5.5* | *38* | *-1.2* | *84* | *10.1* | *65* | *1.4* | *57* | *4.9* | *68* |
| *Absolute Nominal Target Rate of Return* | | | | *0.7* | *99* | *8.1* | *4* | *7.5* | *95* | *7.3* | *1* | *7.1* | *8* |
| **Global Equity** | **67,296,756,644** | **56.9** | **56.8** | **7.5** | **--** | **-6.5** | **--** | **13.2** | **--** | **-1.1** | **--** | **3.9** | **--** |
| *Asset Class Target* | | | | *7.1* | *--* | *-7.9* | *--* | *12.3* | *--* | *-1.7* | *--* | *3.6* | *--* |
| **Domestic Equities** | **30,159,997,320** | **25.5** | **--** | **12.2** | **38** | **1.6** | **21** | **15.3** | **32** | **0.2** | **42** | **3.5** | **54** |
| *Asset Class Target* | | | | *12.1* | *40* | *1.0* | *30* | *14.9* | *46* | *0.0* | *52* | *3.5* | *55* |
| **Foreign Equities** | **33,880,566,859** | **28.7** | **--** | **3.6** | **54** | **-12.9** | **45** | **12.7** | **9** | **-1.5** | **7** | **7.3** | **6** |
| *Asset Class Target* | | | | *3.1* | *85* | *-14.6* | *80* | *11.5* | *22* | *-2.7* | *41* | *6.4* | *34* |
| **Global Equities** | **3,256,190,127** | **2.8** | **--** | **7.6** | **--** | **-5.7** | **--** | **11.4** | **--** | **-2.4** | **--** | **--** | **--** |
| *Benchmark* | | | | *7.4* | *--* | *-6.7* | *--* | *12.4* | *--* | *-1.6* | *--* | *--* | *--* |
| **Fixed Income** | **30,706,179,097** | **26.0** | **26.0** | **1.4** | **64** | **7.6** | **45** | **10.4** | **41** | **6.6** | **41** | **6.1** | **38** |
| *Asset Class Target* | | | | *1.1* | *81* | *7.8* | *38* | *6.8* | *95* | *6.5* | *48* | *5.9* | *46* |
| **Private Equity** | **5,783,192,360** | **4.9** | **4.9** | **-5.0** | **--** | **8.0** | **--** | **4.0** | **--** | **4.7** | **--** | **5.7** | **--** |
| *Asset Class Target* | | | | *13.9* | *--* | *4.0* | *--* | *18.3* | *--* | *4.1* | *--* | *7.9* | *--* |
| *Secondary Target** | | | | *-3.9* | *--* | *14.2* | *--* | *6.3* | *--* | *8.5* | *--* | *11.7* | *--* |
| **Real Estate** | **8,694,348,812** | **7.4** | **7.2** | **3.5** | **1** | **14.5** | **18** | **-2.4** | **46** | **0.8** | **26** | **7.7** | **25** |
| *Asset Class Target* | | | | *3.8* | *1* | *15.3* | *12* | *-4.1* | *52* | *-0.4* | *62* | *3.8* | *74* |
| **Strategic Investments** | **4,879,413,980** | **4.1** | **4.1** | **-1.8** | **--** | **5.5** | **--** | **11.9** | **--** | **--** | **--** | **--** | **--** |
| *Short-Term Target* | | | | *2.4* | *--* | *4.2* | *--* | *9.2* | *--* | *--* | *--* | *--* | *--* |
| **Cash** | **875,199,561** | **0.7** | **1.0** | **0.1** | **--** | **0.3** | **--** | **0.8** | **--** | **0.1** | **--** | **1.3** | **--** |
| *Asset Class Target* | | | | *0.0* | *--* | *0.1* | *--* | *0.3* | *--* | *1.8* | *--* | *2.2* | *--* |

* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

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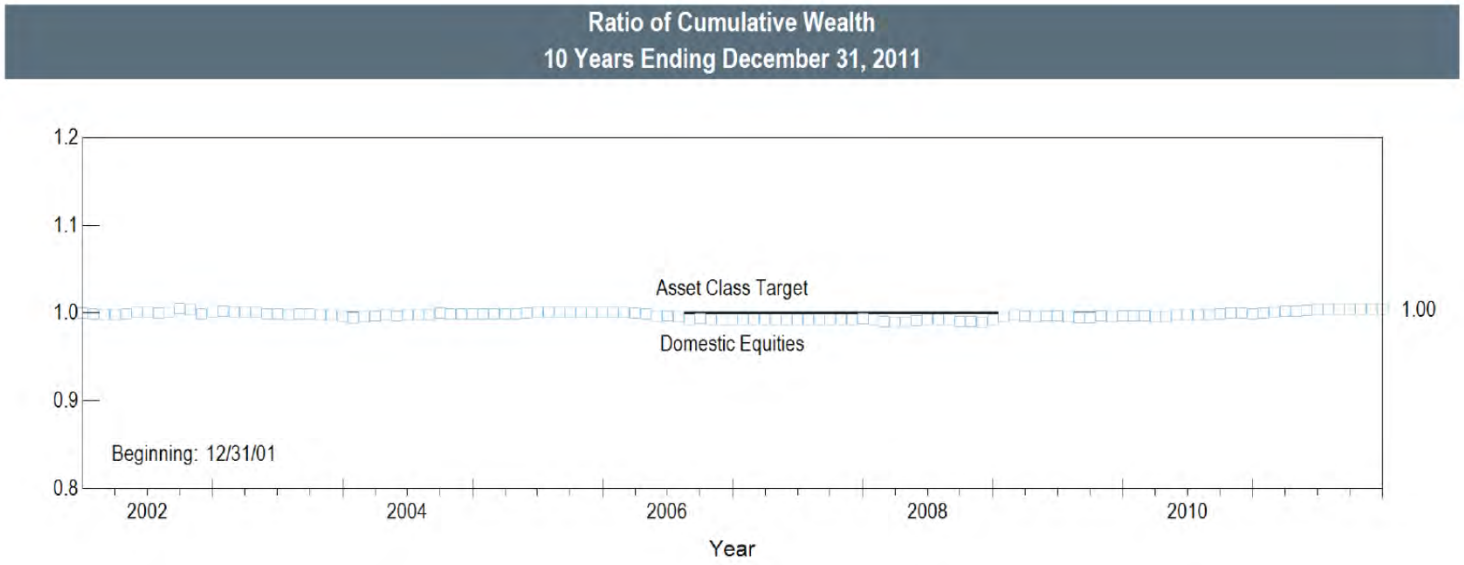
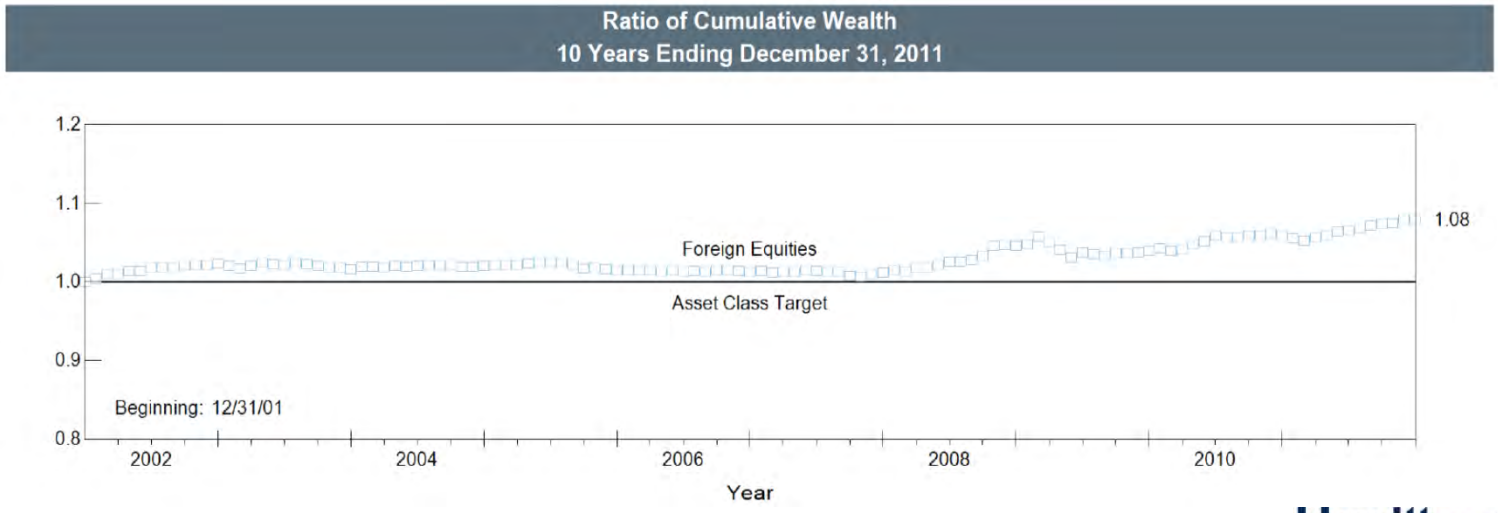
# Ratio of Cumulative Wealth
# As of 12/31/2011

**Domestic Equities**




**Foreign Equities**

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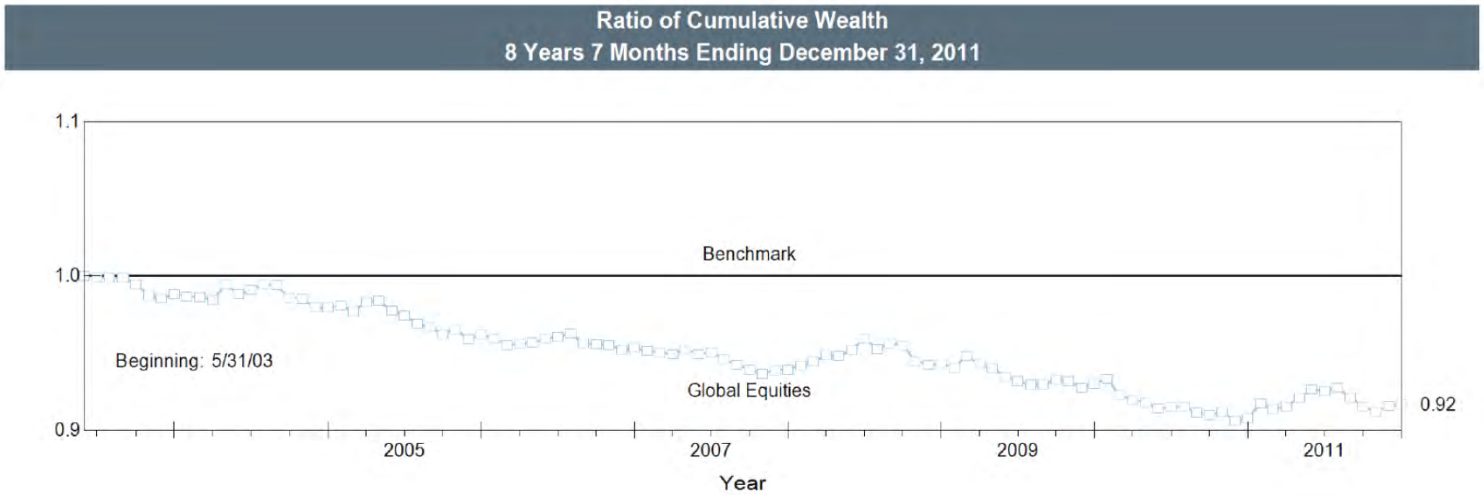
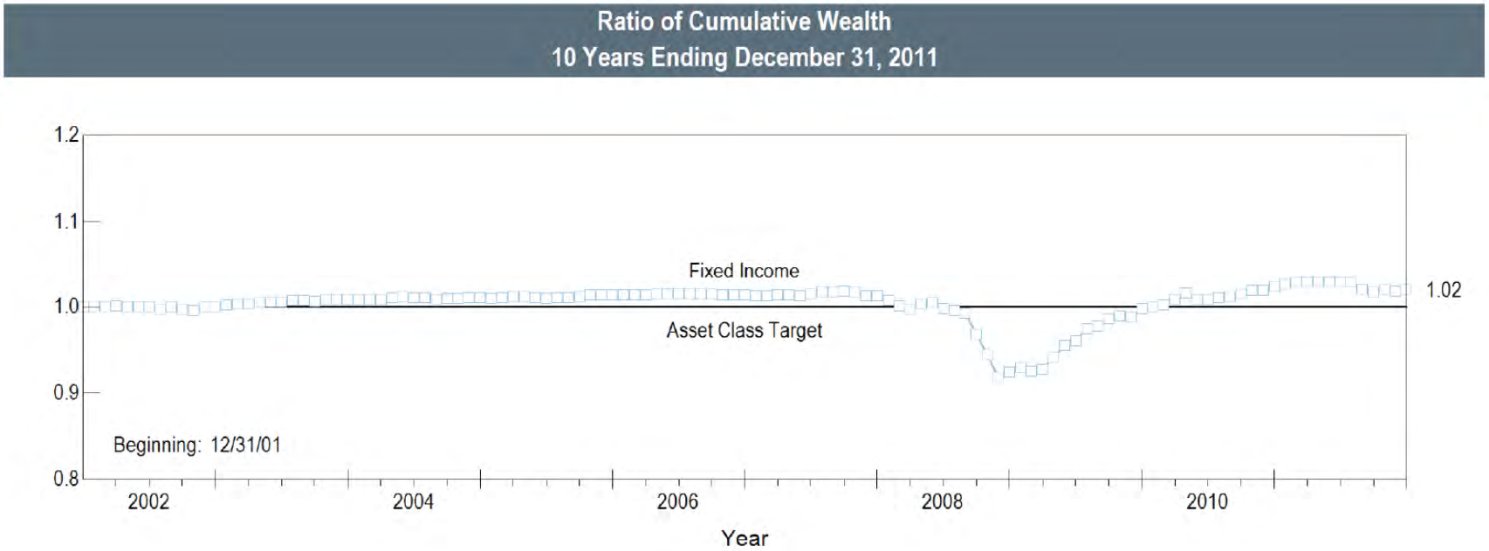
# Ratio of Cumulative Wealth
# As of 12/31/2011

**Global Equities**




**Fixed Income**

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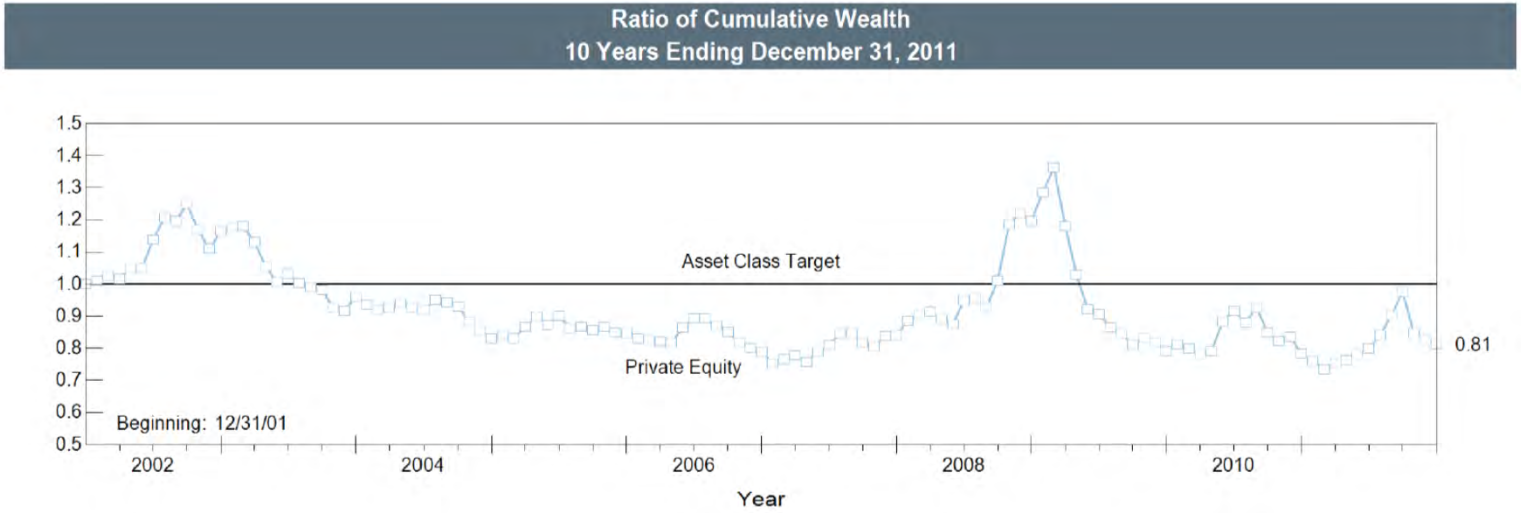
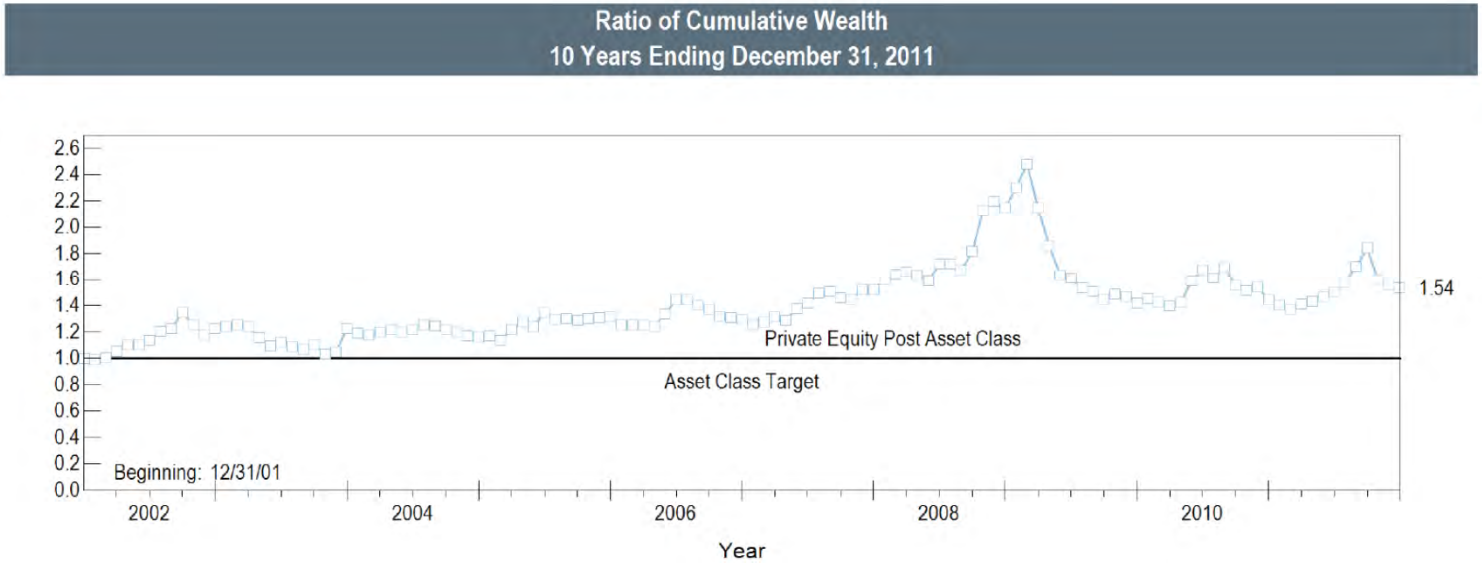
# Ratio of Cumulative Wealth
# As of 12/31/2011

**Private Equity**




**Private Equity Post Asset Class**

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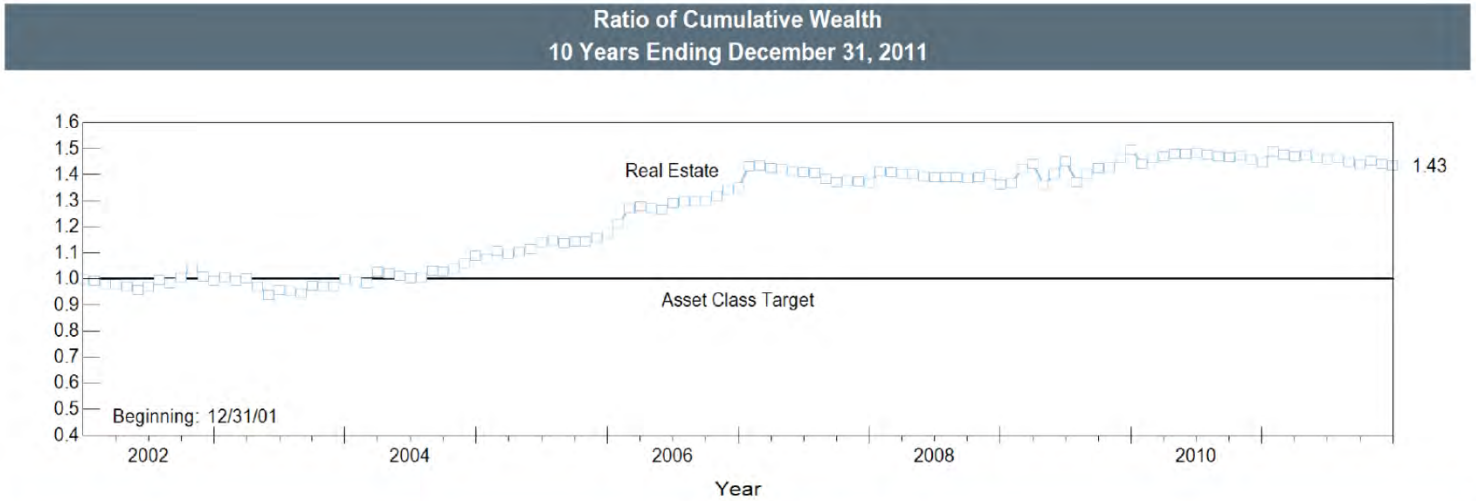
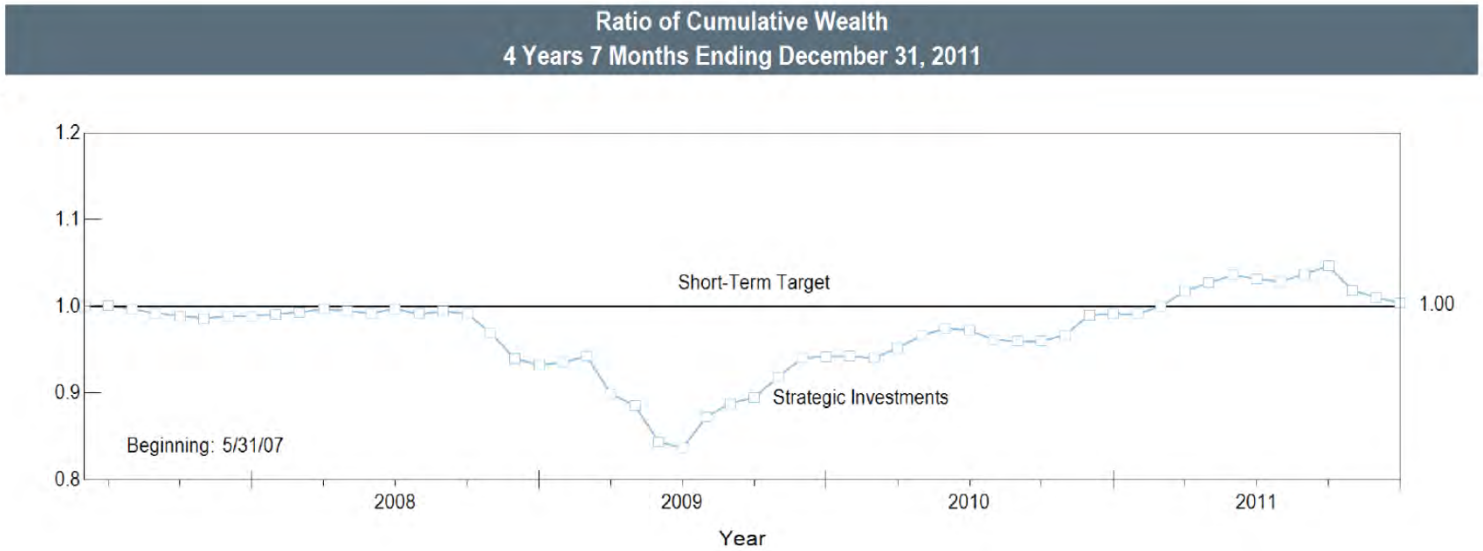
# Ratio of Cumulative Wealth
# As of 12/31/2011

**Real Estate**




**Strategic Investments**

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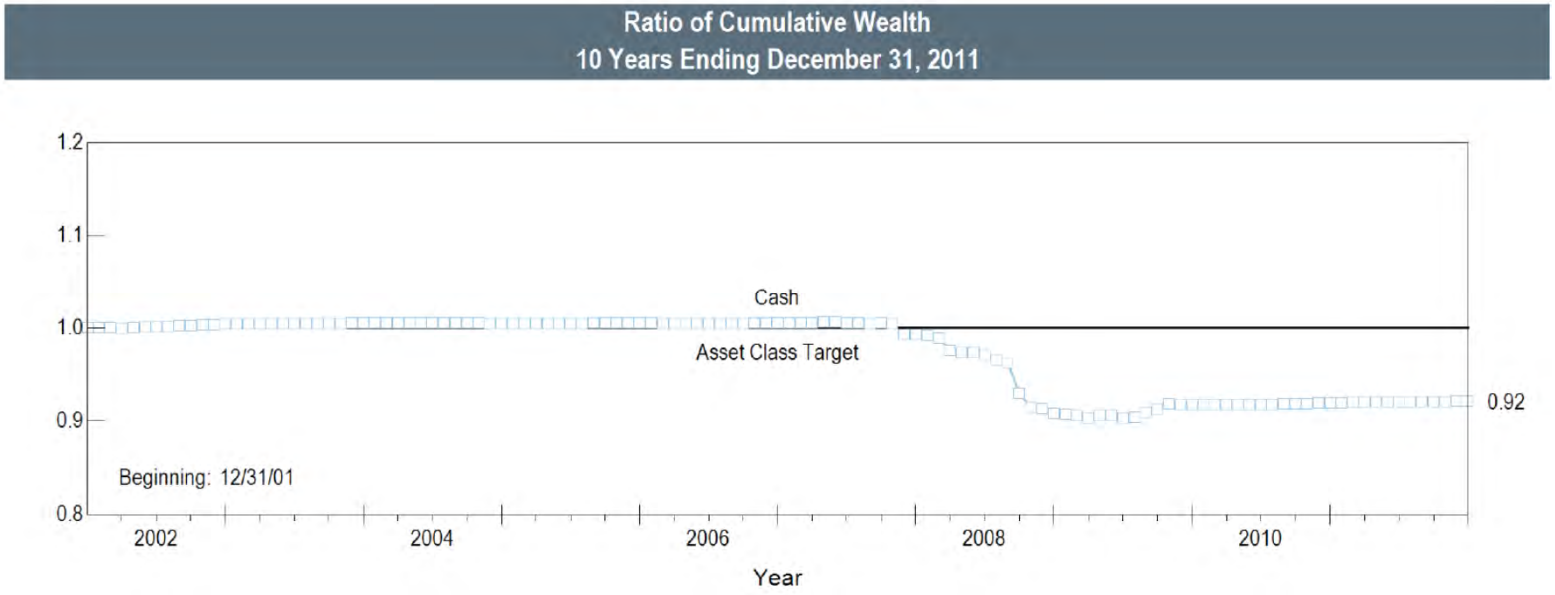
# Ratio of Cumulative Wealth
# As of 12/31/2011

**Cash**



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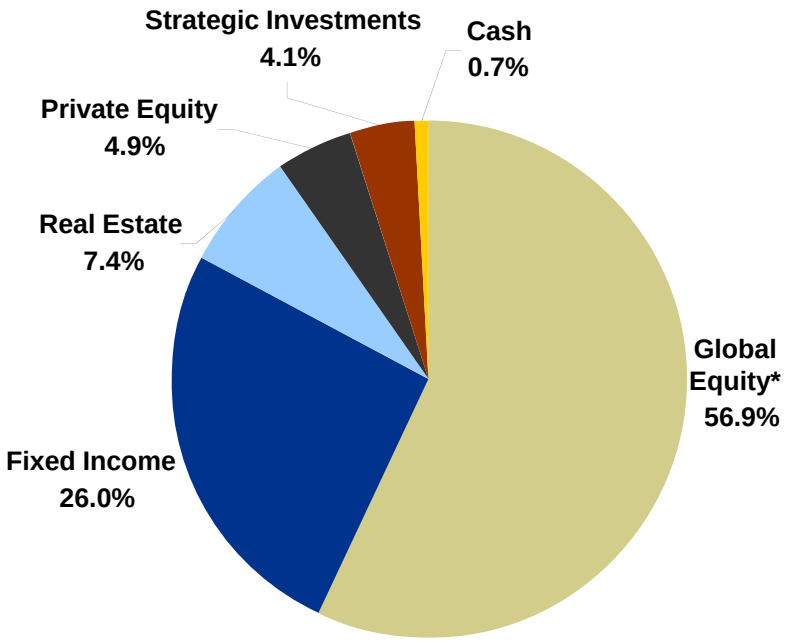
# Comparison of Asset Allocation
# As of 12/31/2011

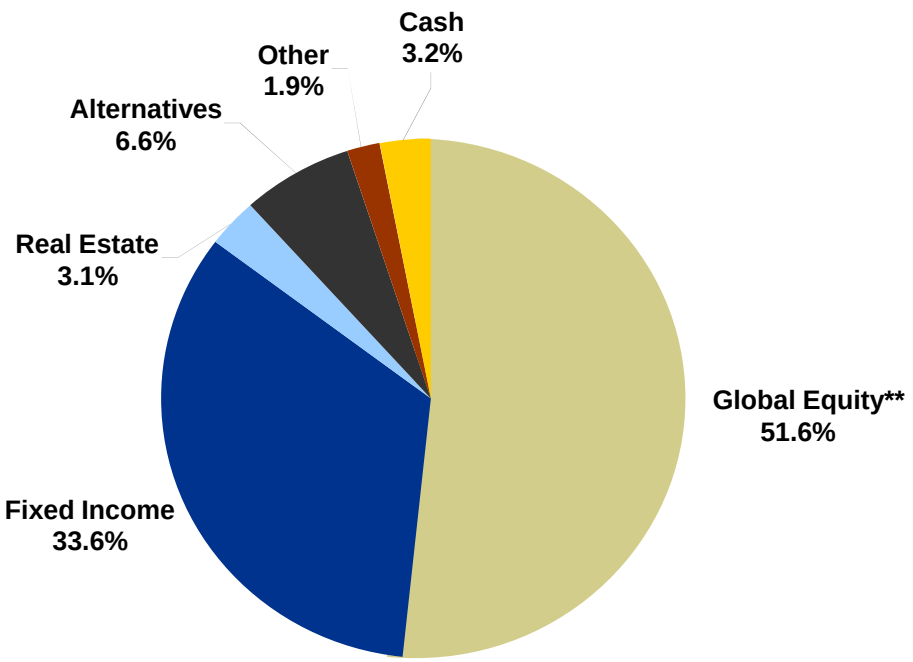
## FRS Pension Plan vs. Median Defined Benefit Plans

### FRS TOTAL FUND




*Global Equity Allocation: 25.5% Domestic Equities; 28.7% Foreign Equities; 2.8% Global Equities. Percentages are of the Total FRS Fund.

### TUCS




**Global Equity Allocation: 38.0% Domestic Equities; 13.6% Foreign Equities.

Note: The TUCS Universe is comprised of 284 defined benefit plan sponsors with $2.4 trillion in total assets. The median fund size was $948.9 million and the average fund size was $8.4 billion.

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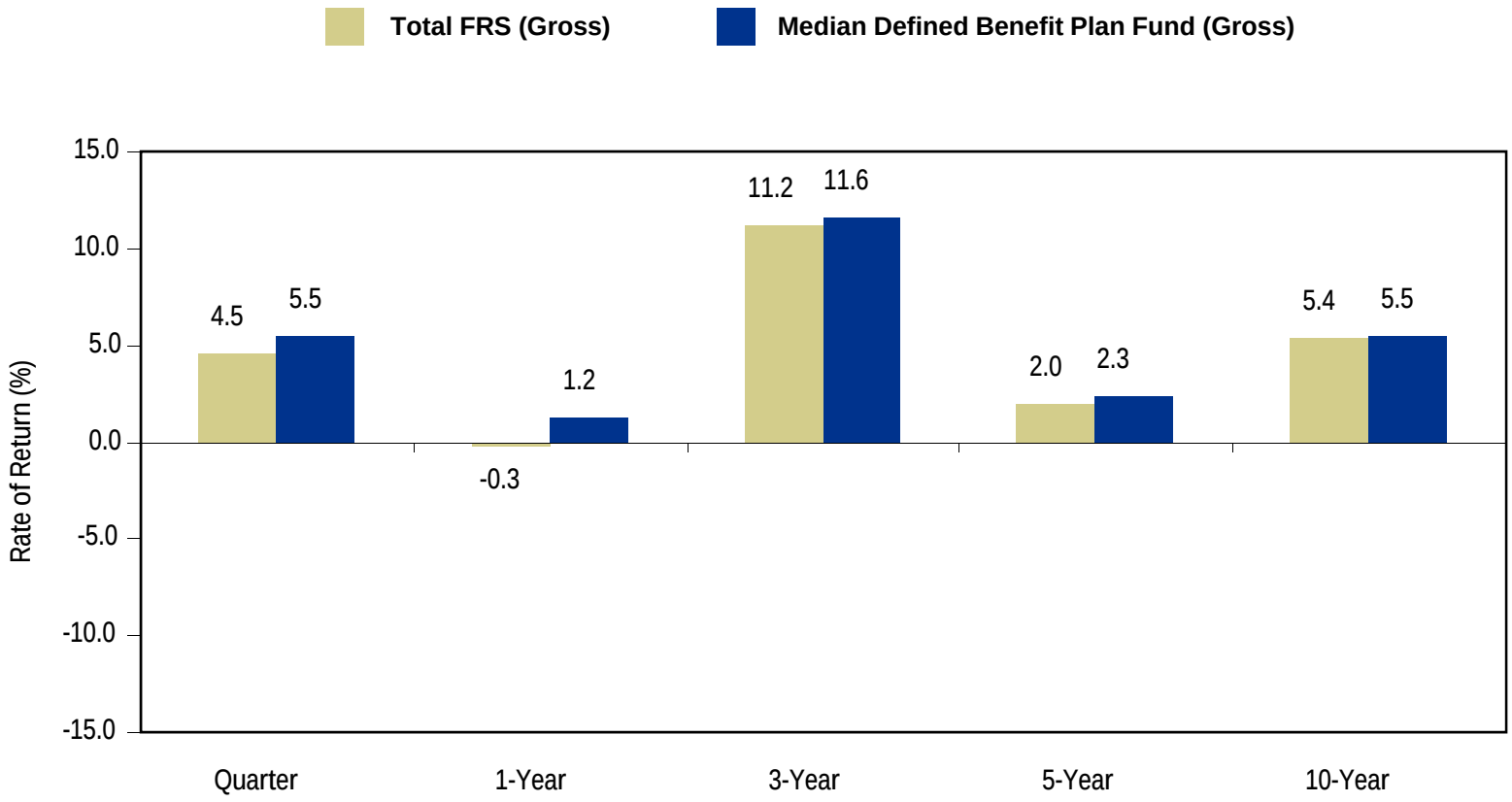
# FRS Results Relative to TUCS Universe
# Periods Ending 12/31/2011




Note: The TUCS Universe is comprised of 284 defined benefit plan sponsors with $2.4 trillion in total assets. The median fund size was $948.9 million and the average fund size was $8.4 billion.

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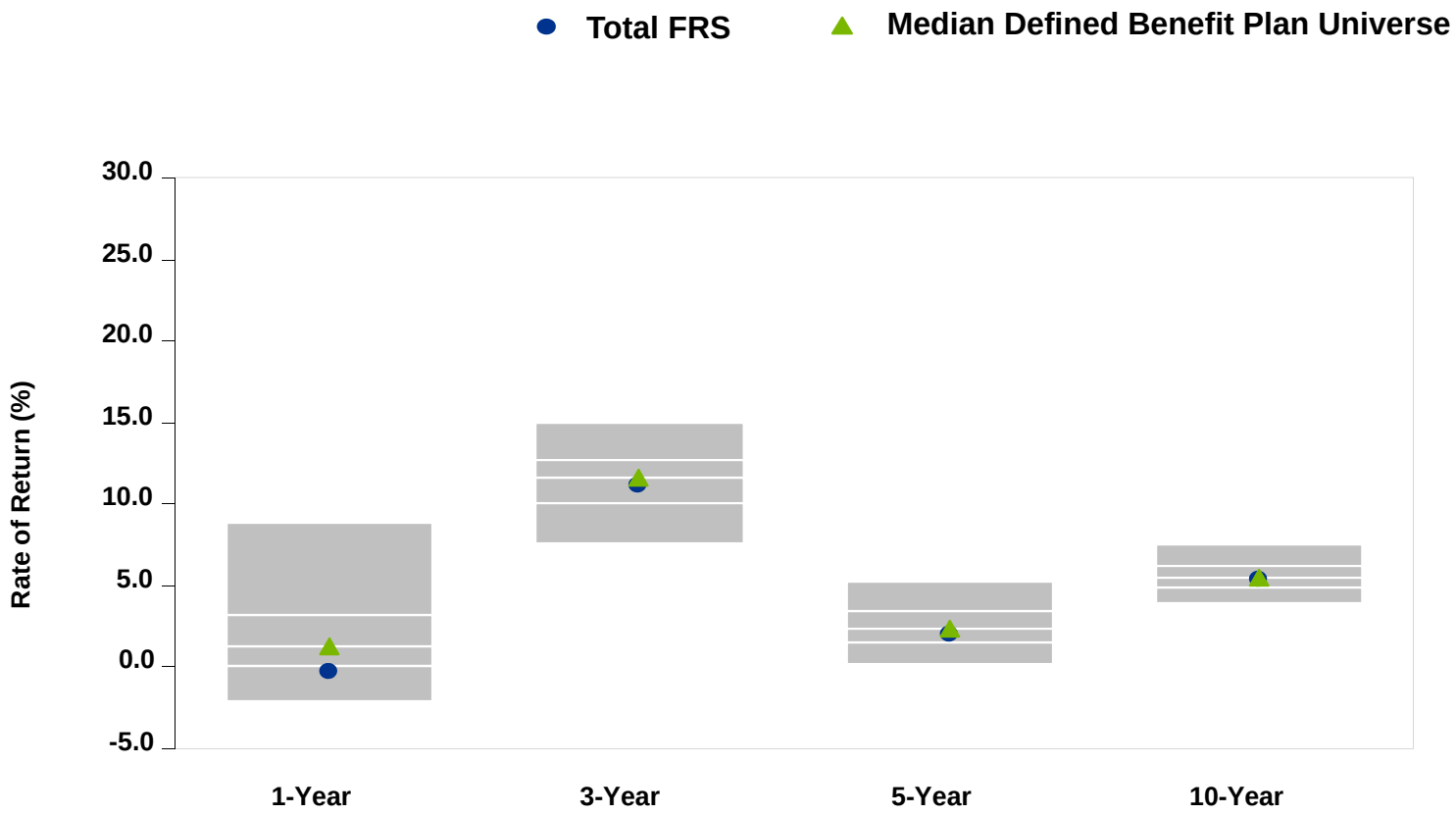
# Total FRS Universe Comparison (TUCS)
# Periods Ending 12/31/2011




| | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|
| FRS Percentile Ranking | 80 | 56 | 63 | 55 |

Note: The TUCS Universe is comprised of 284 defined benefit plan sponsors with $2.4 trillion in total assets. The median fund size was $948.9 million and the average fund size was $8.4 billion.

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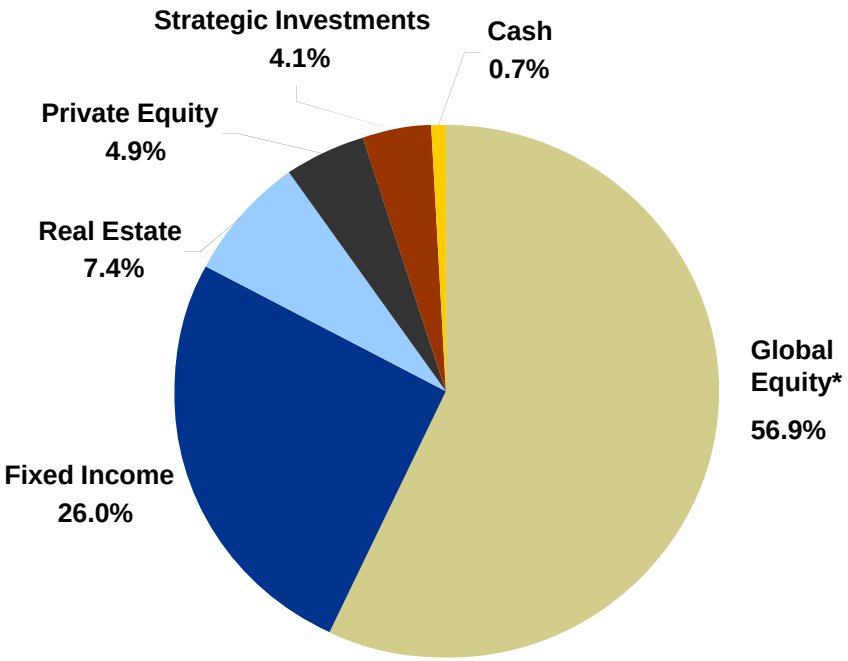
# Comparison of Asset Allocation
# As of 12/31/2011

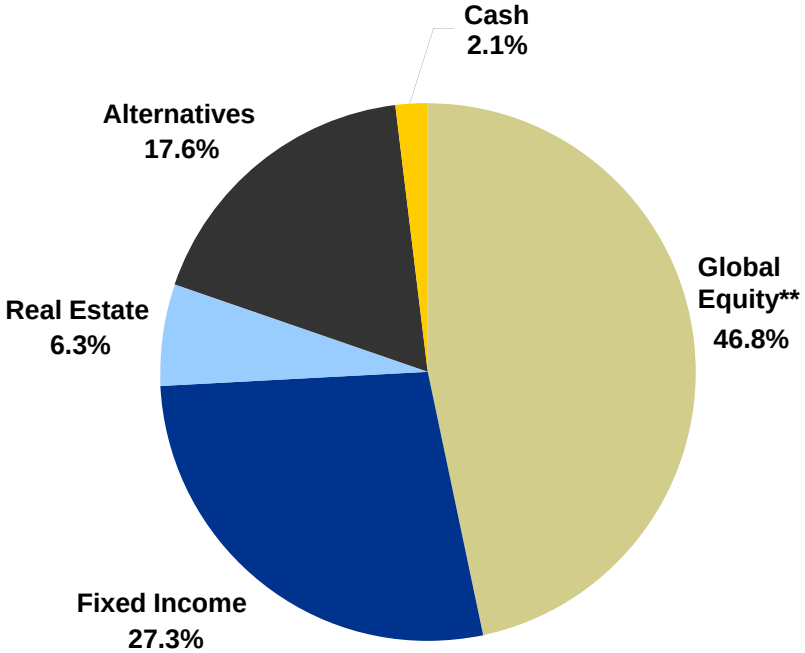
## FRS Pension Plan vs. Top Ten Defined Benefit Plans

### FRS TOTAL FUND




*Global Equity Allocation: 25.5% Domestic Equities; 28.7% Foreign Equities; 2.8% Global Equities. Percentages are of the Total FRS Fund.

### TUCS Top Ten




**Global Equity Allocation: 28.9% Domestic Equities; 17.9% Foreign Equities.

Note: The TUCS Top Ten Universe includes $1.1 trillion in total assets. The median fund size was $112.5 billion and the average fund size was $109.7 billion.

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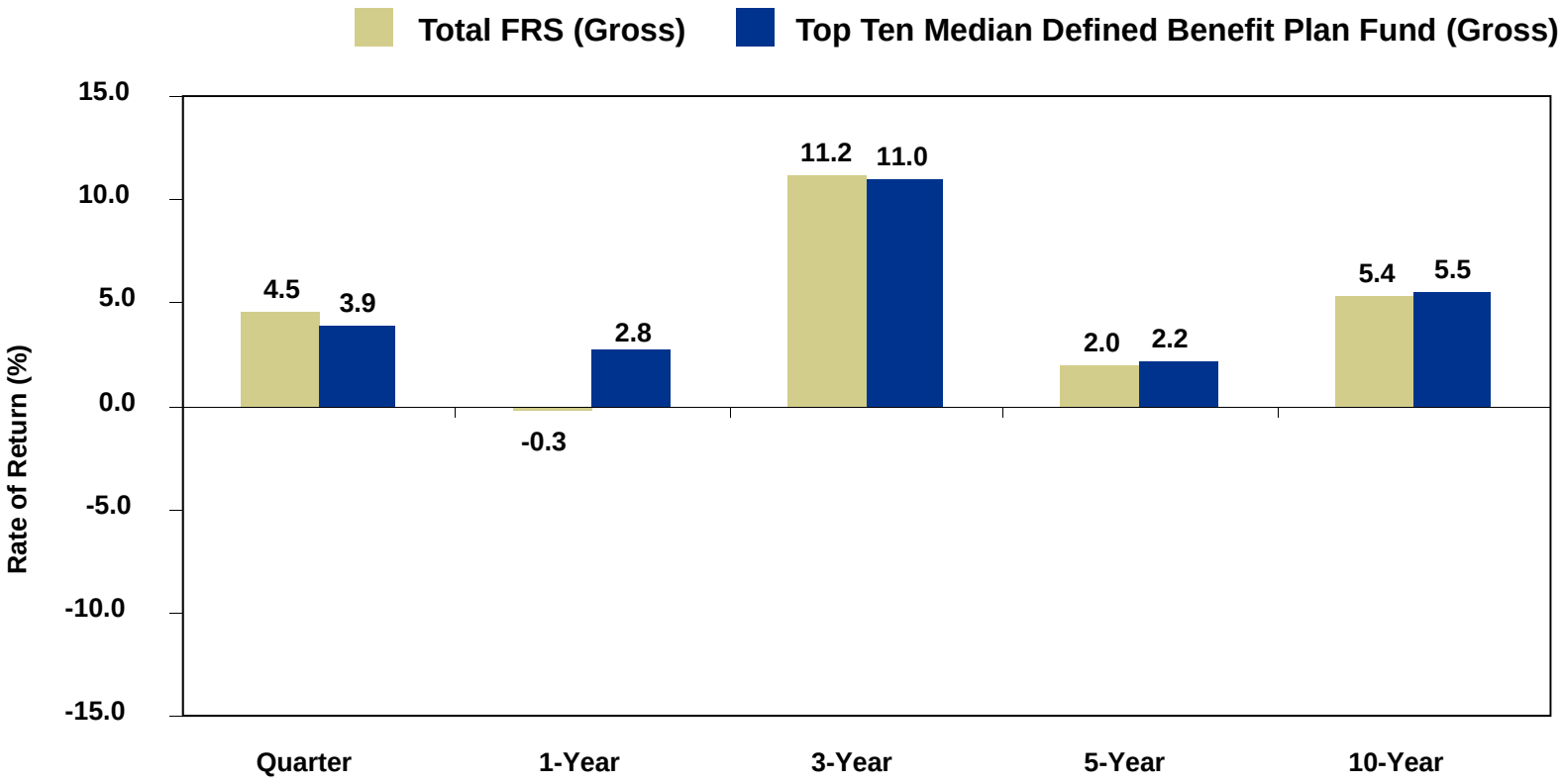
# FRS Results Relative to TUCS Top Ten Defined Benefit Plans
# Periods Ending 12/31/2011




Note: The TUCS Top Ten Universe includes $1.1 trillion in total assets. The median fund size was $112.5 billion and the average fund size was $109.7 billion.



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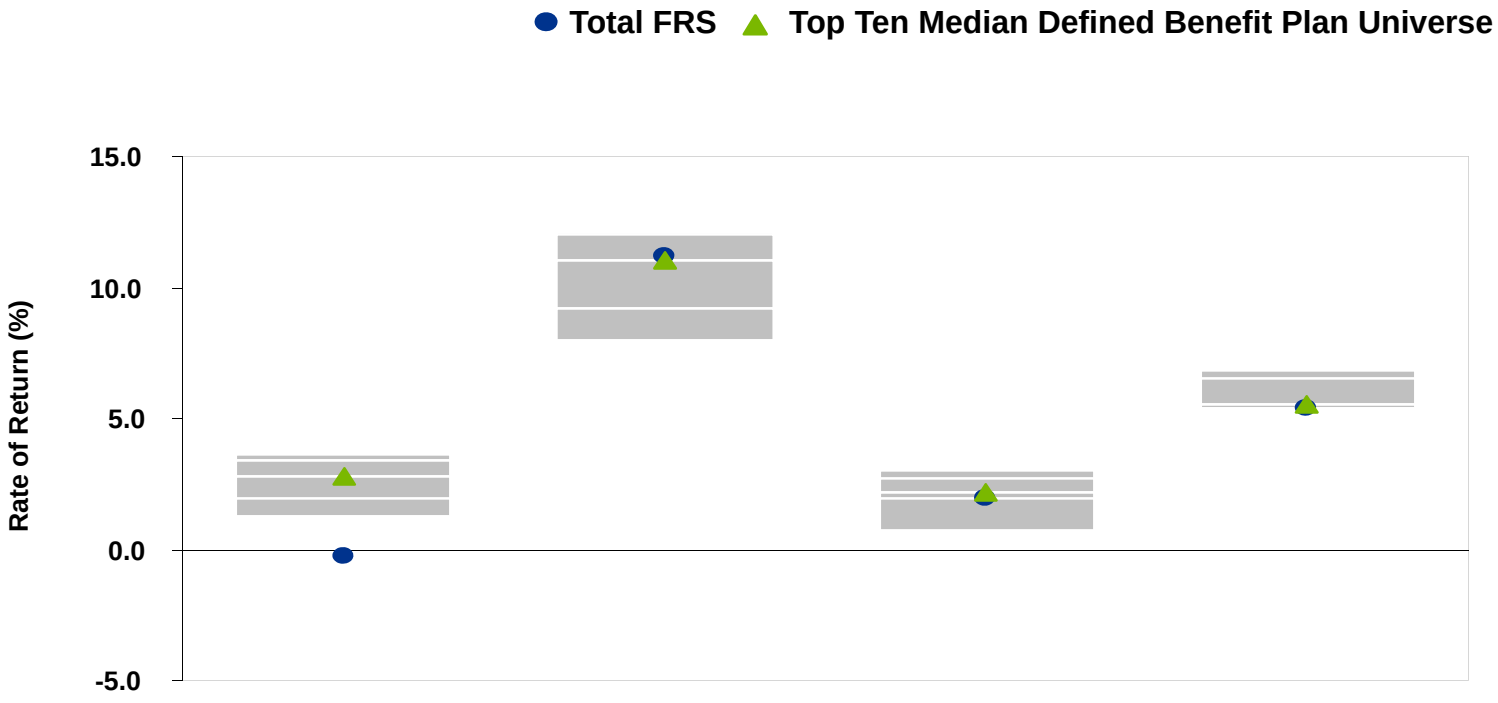
# Top Ten Defined Benefit Plans FRS Universe Comparison (TUCS)
# Periods Ending 12/31/2011




| | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|
| FRS Percentile Ranking | 100 | 37 | 75 | 99 |

Note: The TUCS Top Ten Universe includes $1.1 trillion in total assets. The median fund size was $112.5 billion and the average fund size was $109.7 billion.



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# State Board of Administration of Florida
# Florida Retirement System

Investment Plan Review

Fourth Quarter 2011

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# Executive Summary

- The FRS Investment Plan outperformed the Plan Aggregate Benchmark over the trailing three- and five-year periods with slight underperformance for the trailing one-year period. This suggests strong relative performance for the underlying fund options in which participants are investing.

- The Total Plan Expense Ratio for the FRS Investment Plan is lower, on average, when compared to a defined contribution peer group and is significantly lower than the average corporate and public defined benefit plans.

- Management fees are lower than the median as represented by Morningstar's mutual fund universe for every investment category.

- The FRS Investment Plan offers an appropriate number of fund options that span the risk and return spectrum.

- The Investment Policy Statement is revisited periodically to ensure the structure and guidelines of the Investment Plan are appropriate, taking into consideration the Plan's goals and objectives.

# Total Investment Plan Returns

**Periods Ending 12/31/2011**

| | One-Year | Three-Year | Five-Year |
|---|---|---|---|
| **FRS Investment Plan** | **0.7%** | **9.7%** | **1.8%** |
| *Total Plan Aggregate Benchmark** | 0.9 | 9.1 | 1.1 |
| *FRS Investment Plan vs. Total Plan Aggregate Benchmark* | -0.2 | 0.6 | 0.7 |

**Periods Ending 12/31/2010**

| | Five-Year Average Return | Five-Year Gross Value Added |
|---|---|---|
| **FRS Investment Plan** | **4.0%** | **1.0%** |
| *U.S. Median*** | 3.8 | 0.5 |
| *FRS Investment Plan vs. U.S. Median* | 0.2 | 0.5 |

*Aggregate benchmark returns are an average of the individual portfolio benchmark returns at their actual weights.

**Based on the CEM 2010 Survey that included 152 U.S. defined contribution plans with aggregate assets totaling $929 billion. The median DC plan in the universe had $2.3 billion in assets and the average DC plan has $6.1 billion in assets.



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# Investment Plan Change in Market Value
# Periods Ending 12/31/2011

| Summary of Cash Flows* | | |
|---|---|---|
| | **Fourth Quarter** | **Fiscal YTD**** |
| | | |
| **Beginning Market Value** | $6,371,988,738 | $6,733,758,411 |
| **+/- Net Contributions/(Withdrawals)** | ($56,394,910) | $162,386,763 |
| **Investment Earnings** | $326,727,978 | ($253,823,368) |
| **= Ending Market Value** | $6,642,321,806 | $6,642,321,806 |
| **Net Change** | $270,333,068 | ($91,436,606) |
| | | |

* Based on figures provided by the Investment Plan's Administrator as of report time.

** Period July 2011 – December 2011



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# FRS Investment Plan Results - Trailing Period
# Periods Ending 12/31/2011

FRS Investment Plan | As of December 31, 2011 | $6,642.3 Million and 100.0% of Fund

## Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|
| **FRS Investment Plan** | **6,642,321,806** | **100.0** | **5.2** | **--** | **0.7** | **--** | **9.7** | **--** | **1.8** | **--** |
| *Total Plan Aggregate Benchmark* | | | *5.2* | -- | *0.9* | -- | *9.1* | -- | *1.1* | -- |
| **Balanced Funds** | **2,833,352,104** | **42.7** | **4.2** | **--** | **1.4** | **--** | **8.8** | **--** | **1.4** | **--** |
| FRS Select Conservative Balanced Fund | 626,660,939 | 9.4 | 1.7 | -- | 3.9 | -- | 6.1 | -- | 3.7 | -- |
| *Conservative Balanced Fund Target Benchmark* | | | *1.8* | -- | *4.0* | -- | *5.8* | -- | *3.3* | -- |
| FRS Select Moderate Balanced Fund | 1,691,870,961 | 25.5 | 4.5 | -- | 1.2 | -- | 9.2 | -- | 1.3 | -- |
| *Moderate Balanced Fund Target Benchmark* | | | *4.6* | -- | *1.3* | -- | *8.8* | -- | *0.8* | -- |
| FRS Select Aggressive Balanced Fund | 514,820,204 | 7.8 | 6.2 | -- | -0.9 | -- | 10.0 | -- | -0.4 | -- |
| *Aggressive Balanced Fund Target Benchmark* | | | *6.3* | -- | *-0.8* | -- | *10.1* | -- | *-0.6* | -- |
| **Cash** | **921,202,884** | **13.9** | **0.1** | **1** | **0.2** | **1** | **0.3** | **14** | **1.7** | **20** |
| FRS Select Yield Plus Money Market Active Fund | 921,202,884 | 13.9 | 0.1 | 1 | 0.2 | 1 | 0.3 | 14 | 1.7 | 20 |
| *iMoneyNet 1st Tier Institutional Net Index* | | | *0.0* | *26* | *0.1* | *25* | *0.3* | *7* | *1.9* | *3* |
| **TIPS** | **288,104,372** | **4.3** | **2.5** | **--** | **13.6** | **--** | **10.4** | **--** | **8.0** | **--** |
| FRS Select TIPS Fund | 288,104,372 | 4.3 | 2.5 | 48 | 13.6 | 9 | 10.4 | 25 | 8.0 | 23 |
| *Barclays Capital US TIPS* | | | *2.7* | *8* | *13.6* | *9* | *10.4* | *26* | *8.0* | *26* |
| **Fixed Income** | **633,333,438** | **9.5** | **1.5** | **44** | **6.7** | **53** | **8.7** | **62** | **6.8** | **34** |
| FRS Select U.S. Bond Enhanced Index Fund | 148,002,354 | 2.2 | 1.0 | 88 | 7.9 | 75 | 7.0 | 96 | 6.8 | 64 |
| *Barclays Capital Aggregate Bond Index* | | | *1.1* | *88* | *7.8* | *76* | *6.8* | *97* | *6.5* | *66* |
| Pyramis Intermediate Duration Pool Fund | 74,251,707 | 1.1 | 1.0 | 79 | 5.9 | 70 | 8.3 | 67 | 5.7 | 70 |
| *Barclays Capital Int Aggregate* | | | *0.9* | *85* | *6.0* | *69* | *6.2* | *93* | *6.1* | *60* |
| FRS Select High Yield Fund | 133,251,345 | 2.0 | 5.8 | 51 | 6.0 | 10 | -- | -- | -- | -- |
| *Barclays Capital U.S. High Yield Ba-2% Issuer Cap* | | | *5.7* | *55* | *6.9* | *3* | -- | -- | -- | -- |
| PIMCO Total Return Fund | 277,828,032 | 4.2 | 2.2 | 11 | 4.0 | 91 | 8.7 | 61 | 7.9 | 9 |
| *Barclays Capital Aggregate Bond Index* | | | *1.1* | *68* | *7.8* | *17* | *6.8* | *87* | *6.5* | *44* |

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# FRS Investment Plan Results - Trailing Period
# Periods Ending 12/31/2011

FRS Investment Plan | As of December 31, 2011 | $6,642.3 Million and 100.0% of Fund

## Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|
| **Domestic Equity** | **1,522,296,291** | **22.9** | **12.5** | **41** | **0.3** | **36** | **16.5** | **29** | **1.1** | **29** |
| FRS Select U.S. Stock Market Index Fund | 229,260,232 | 3.5 | 12.2 | 24 | 1.0 | 44 | 15.0 | 17 | 0.1 | 28 |
| *Russell 3000 Index* | | | *12.1* | *27* | *1.0* | *44* | *14.9* | *19* | *0.0* | *30* |
| FRS Select U.S. Large Value Stock Fund | 185,075,725 | 2.8 | 12.8 | 39 | 1.6 | 27 | 12.2 | 50 | -- | -- |
| *Russell 1000 Value Index* | | | *13.1* | *32* | *0.4* | *37* | *11.5* | *60* | -- | -- |
| QMA Mid Cap Quantitative Core Fund | 256,450,202 | 3.9 | 14.8 | 13 | 0.1 | 22 | 20.8 | 22 | 3.8 | 21 |
| *S&P 400 MidCap* | | | *13.0* | *36* | *-1.7* | *35* | *19.6* | *35* | *3.3* | *25* |
| FRS Select U.S. Large Growth Stock Active Fund | 77,940,867 | 1.2 | 8.0 | 79 | 1.2 | 25 | 17.6 | 26 | 2.7 | 24 |
| *Russell 1000 Growth Index* | | | *10.6* | *27* | *2.6* | *13* | *18.0* | *20* | *2.5* | *27* |
| Pioneer Fund | 129,522,387 | 1.9 | 11.4 | 61 | -4.2 | 82 | 11.6 | 80 | -0.8 | 63 |
| *S&P 500 Index* | | | *11.8* | *38* | *2.1* | *22* | *14.1* | *32* | *-0.3* | *36* |
| Fidelity Growth Company Fund | 278,322,925 | 4.2 | 7.8 | 81 | 0.9 | 26 | 19.9 | 11 | 4.2 | 9 |
| *Russell 3000 Growth Index* | | | *10.9* | *22* | *2.2* | *18* | *18.1* | *20* | *2.5* | *28* |
| American Beacon Small Cap Value Fund | 121,542,363 | 1.8 | 18.4 | 14 | -4.0 | 52 | 17.9 | 34 | 0.9 | 47 |
| *Russell 2000 Value Index* | | | *16.0* | *54* | *-5.5* | *63* | *12.4* | *91* | *-1.9* | *92* |
| T. Rowe Price Small Cap Stock Fund | 221,369,760 | 3.3 | 16.8 | 17 | -0.1 | 29 | 22.4 | 21 | 3.7 | 19 |
| *Russell 2000 Index* | | | *15.5* | *27* | *-4.2* | *65* | *15.6* | *85* | *0.2* | *80* |
| Fidelity Low Priced Stock Fund | 22,811,831 | 0.3 | 9.4 | 95 | 0.2 | 11 | 19.1 | 36 | 2.3 | 30 |
| *Russell 2500 Value Index* | | | *15.4* | *12* | *-3.4* | *56* | *15.5* | *77* | *-0.6* | *74* |
| **International/Global Equity** | **444,032,717** | **6.7** | **4.3** | **52** | **-11.3** | **25** | **9.6** | **44** | **-2.2** | **24** |
| FRS Select Foreign Stock Index Fund | 122,600,549 | 1.8 | 3.6 | 68 | -11.8 | 31 | 8.4 | 57 | -3.8 | 45 |
| *MSCI World ex USA* | | | *3.5* | *70* | *-12.2* | *35* | *8.5* | *57* | *-4.1* | *51* |
| American Funds New Perspective Fund | 169,420,449 | 2.6 | 6.4 | 71 | -7.4 | 48 | 13.0 | 42 | 0.9 | 17 |
| *MSCI World Index* | | | *7.6* | *43* | *-5.5* | *36* | *11.1* | *63* | *-2.4* | *54* |
| American Funds Euro-Pacific Growth Fund | 152,011,720 | 2.3 | 4.6 | 48 | -13.3 | 42 | 9.9 | 26 | -1.1 | 11 |
| *MSCI All Country World ex-U.S. Index* | | | *3.8* | *73* | *-13.3* | *43* | *8.6* | *47* | *-4.0* | *45* |

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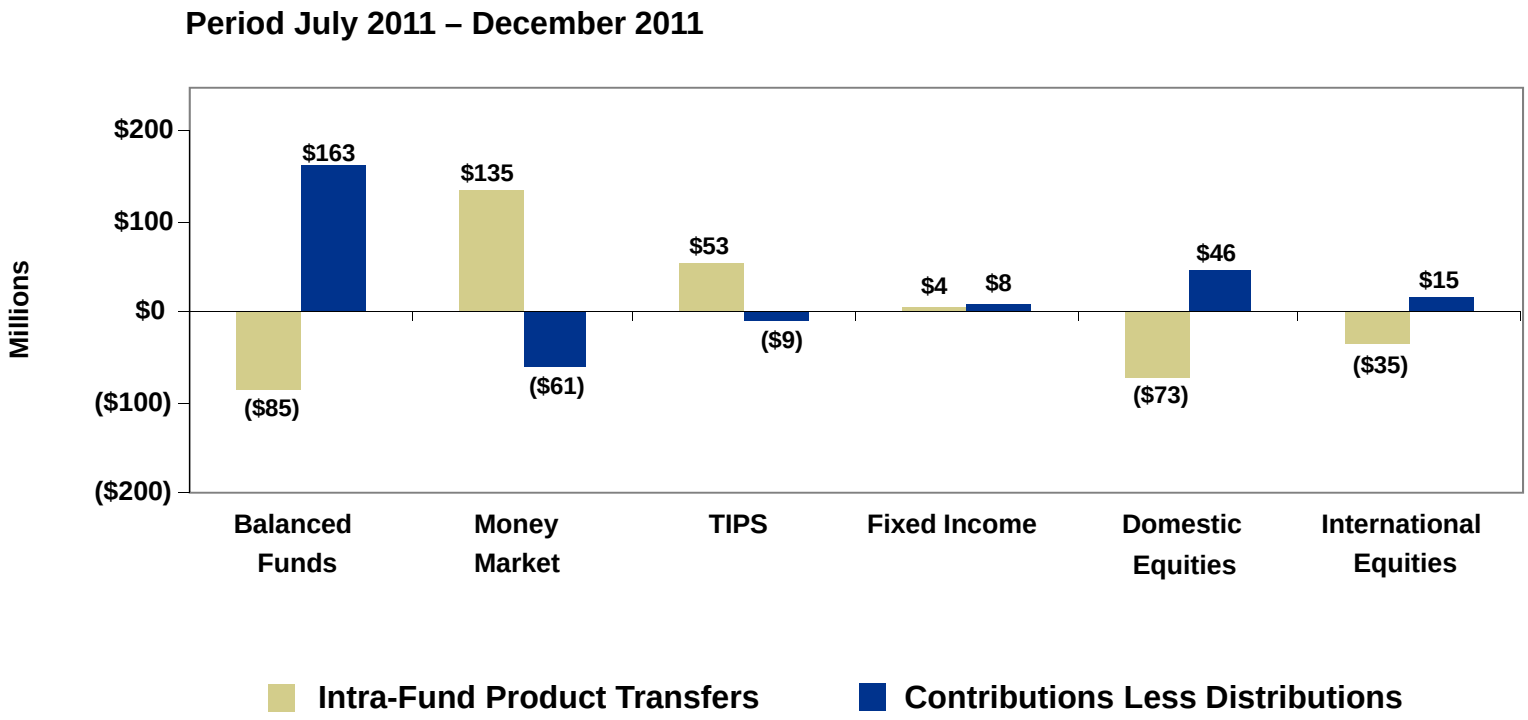
# Investment Plan Member Cash Flow by Product Type



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# Investment Plan Costs

| | |
|---|---|
| **Investment Plan Expense Ratio*** | **0.23%** |
| **Peer DC Plan Expense Ratio*** | **0.27%** |

| **DB Plan Investment Management Fees** | |
|---|---|
| **Corporate**** | **0.50%** |
| **Public Funds***** | **0.46%** |

*Source: CEM Benchmarking 2010 Report – Custom Peer Group for FSBA of 20 DC plans including corporate and public plans with assets between $1.9 - $12.4 billion.
**Source: Greenwich Associates 2010 Survey – Average fee of 80 corporate funds each with over $5 billion under management.
***Source: Greenwich Associates 2010 Survey – Average fee of 69 public funds each with over $5 billion under management.



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# Investment Plan Costs

| Investment Category | Investment Plan Fee* | Average Mutual Fund Fee** |
|---|---|---|
| Large-Cap Equity Fund | 0.27% | 0.87% |
| Mid-Cap Equity Fund | 0.55% | 0.98% |
| Small-Cap Equity Fund | 0.88% | 1.08% |
| International Equity Fund | 0.41% | 1.07% |
| Diversified Bond Fund | 0.27% | 0.55% |
| Balanced Fund | 0.05% | 0.90% |
| Money Market | 0.06% | 0.27% |

*Average Fee if Multiple Products in Category as of 12/31/2011.

**Source: Morningstar as of 12/31/2011.



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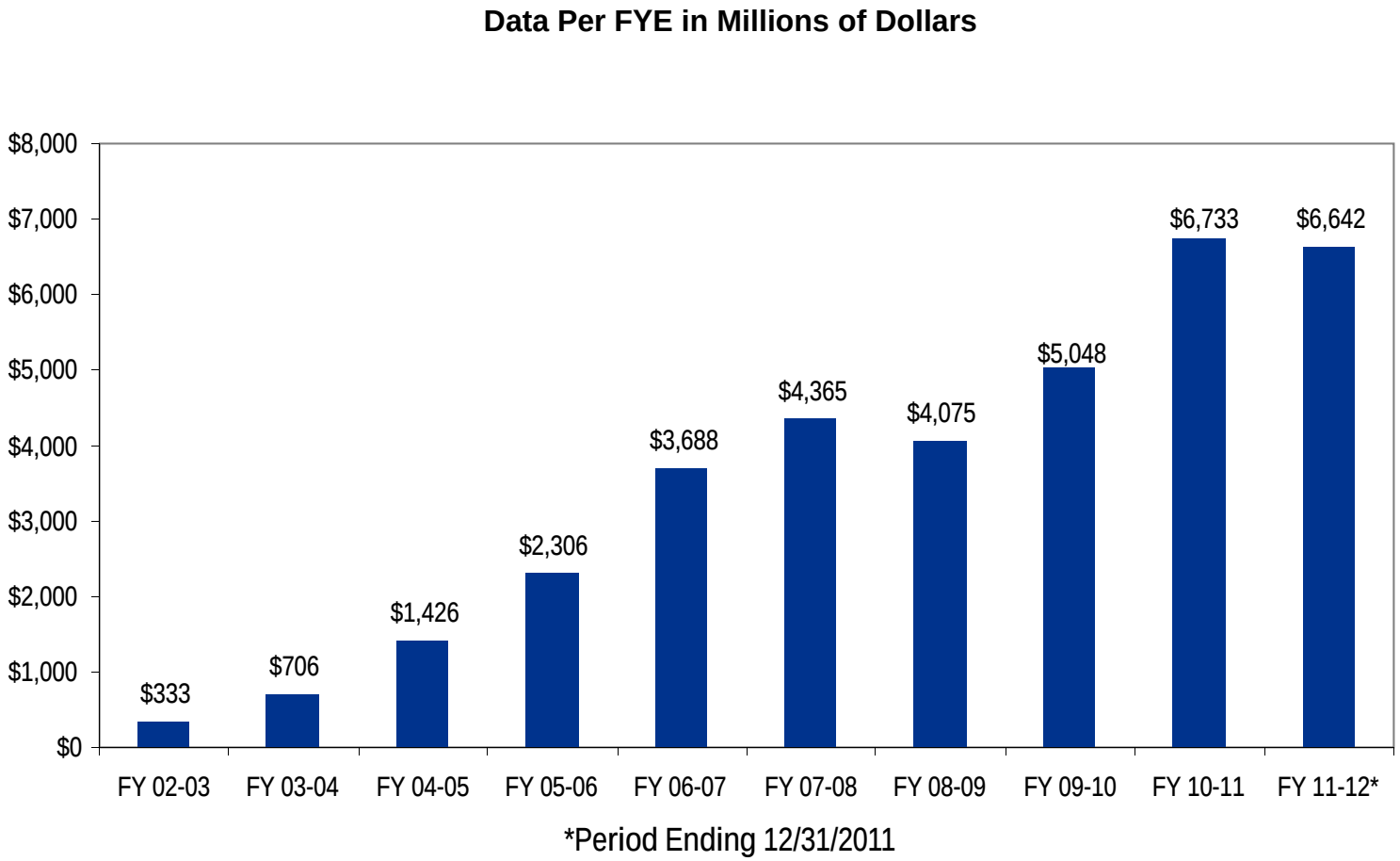
# Investment Plan Fiscal Year End Assets Under Management




Source: Aon Hewitt



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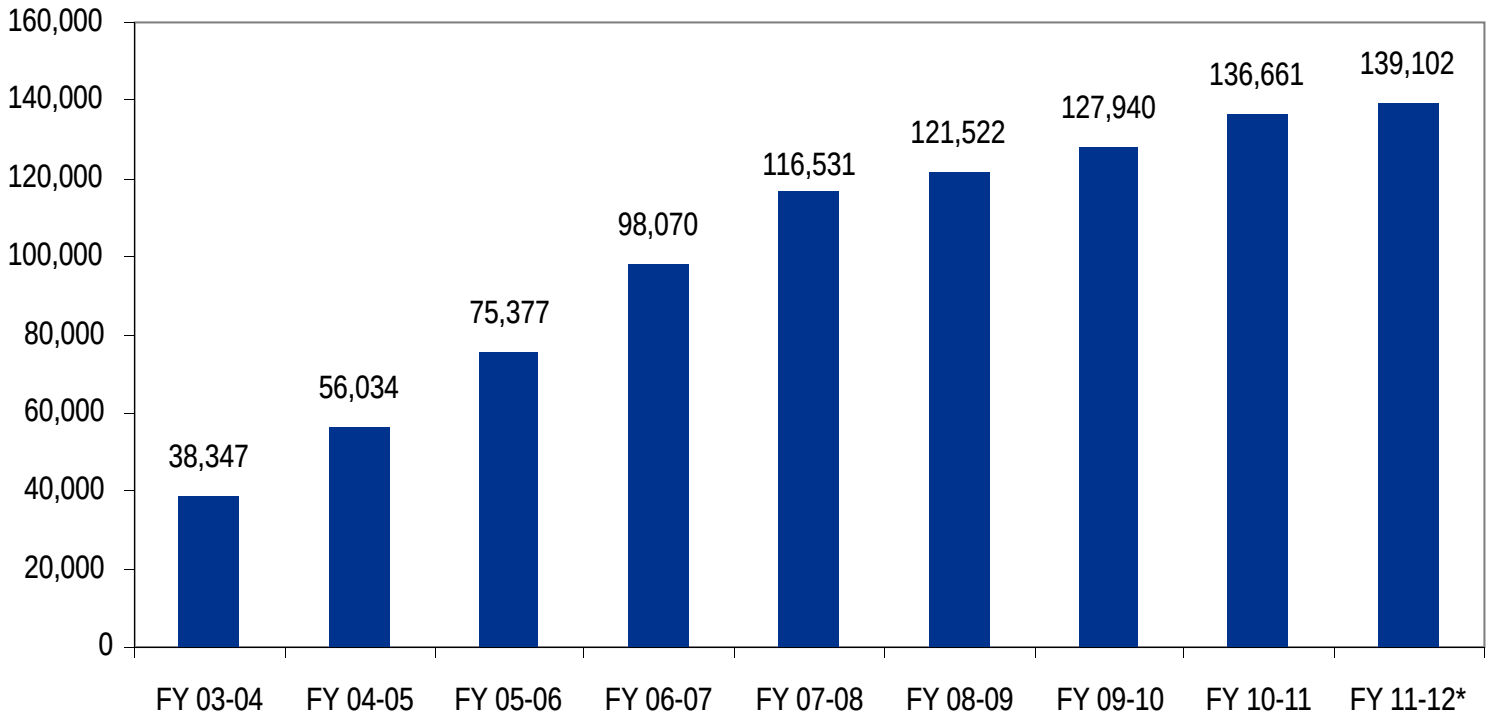
# Investment Plan Membership

**By Fiscal Year**




***Period Ending 12/31/2011**



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# State Board of Administration of Florida
# CAT Fund Review

Fourth Quarter 2011

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# Florida Hurricane Catastrophe Fund Background

- The purpose of the Florida Hurricane Catastrophe Fund (FHCF) is to provide a stable, ongoing and timely source of reimbursement to insurers for a portion of their hurricane losses.
- The State Board of Administration of Florida (SBA) manages five FHCF accounts, the CAT Fund (Operating Fund), the CAT 2006 A Fund (Post-Event Tax-Exempt Revenue Bonds), the CAT 2007 A Fund (Pre-Event Floating Rate Taxable Notes), the CAT 2008 A Fund (Post-Event Tax-Exempt Revenue Bonds), and the CAT 2010 A Fund (Post-Event Tax-Exempt Revenue Bonds).
- Both the CAT Fund (Operating Fund) and the CAT 2007 A Fund are internally managed portfolios benchmarked to a blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Net Index.
- The CAT 2006 A Fund, the CAT 2008 A Fund and the CAT 2010 A Fund are invested in State and Local Government Series (SLGS) securities.
- As of December 31, 2011, the total value of all FHCF accounts was $11.7 billion.

# Executive Summary

- Performance of the CAT Fund on both an absolute and relative basis has been strong over short- and long-term time periods. The Fund did underperform over the five-year period mostly due to poor performance during the 2008 credit crisis.
- The CAT Fund is adequately diversified across issuers within the short-term bond market.
- CAT Fund investment policy appropriately constrains the Fund to invest in short-term and high quality bonds to minimize both interest rate and credit risk.
- Adequate liquidity exists to address the cash flow obligations of the CAT Fund.
- The Investment Policy Statement is revisited periodically to ensure the structure and guidelines of the CAT Fund are appropriate, taking into consideration the Fund's goals and objectives.

# CAT Fund Change in Market Value
# Periods Ending 12/31/2011

| Summary of Cash Flows | | |
|---|---|---|
| | **Fourth Quarter** | **Fiscal YTD*** |
| **Beginning Market Value** | $6,334,131,355 | $5,916,504,386 |
| **+/- Net Contributions/(Withdrawals)** | $835,174,785 | $1,252,345,885 |
| **Investment Earnings** | $6,464,066 | $6,919,935 |
| **= Ending Market Value** | $7,175,770,206 | $7,175,770,206 |
| **Net Change** | $841,638,851 | $1,259,265,820 |

*Period July 2011 – December 2011



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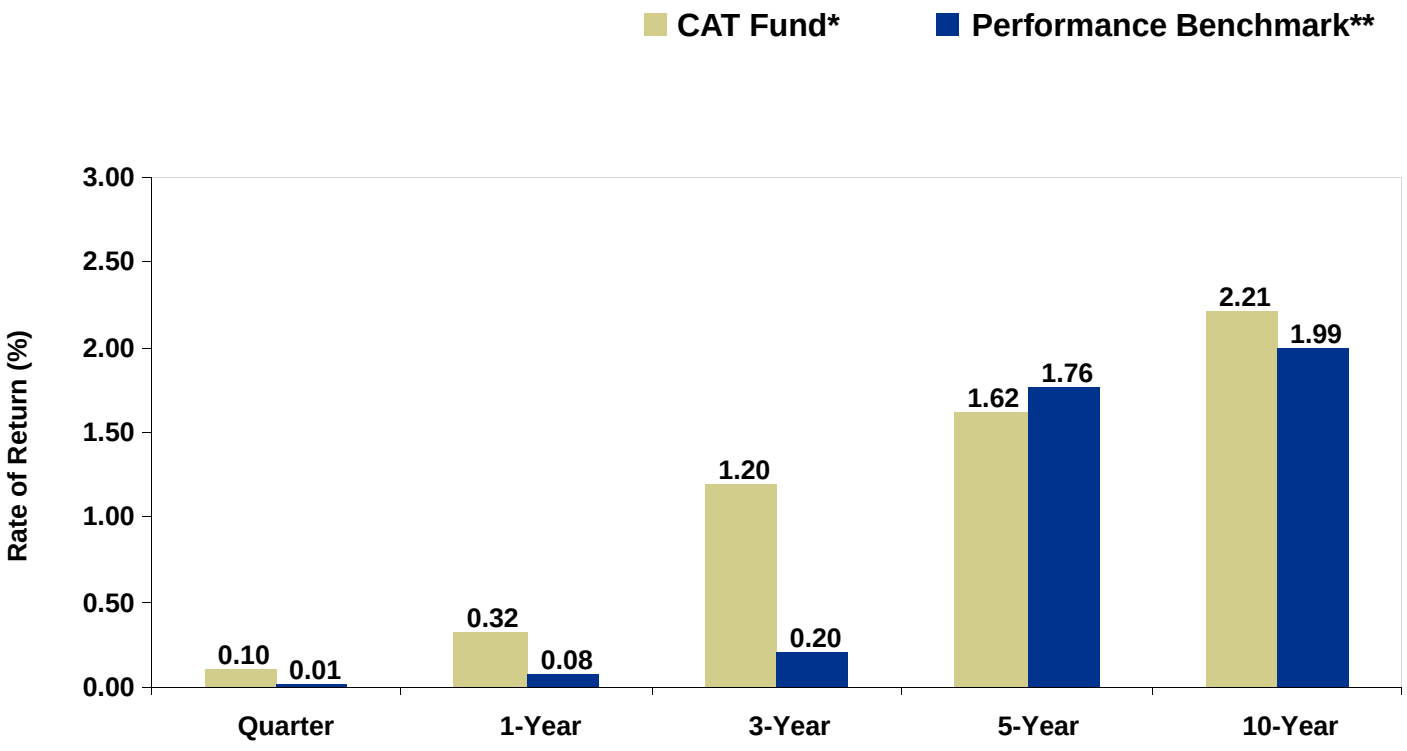
# CAT Fund Investment Results
# Periods Ending 12/31/2011




*CAT Fund: Beginning March 2008, the returns for the CAT Fund reflect marked-to-market returns. Prior to that time, cost-based returns are used.
**Performance Benchmark: The CAT Fund was benchmarked to the IBC First Tier through February 2008. From March 2008 to December 2009, it was the Merrill Lynch 1-Month LIBOR. From January 2010 to June 2010, it was a blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Gross Index. Effective July 2010, it is a blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Net Index.



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# CAT Fund Characteristics
# Period Ending 12/31/2011

| Effective Maturity Schedule | |
|---|---|
| O/N* - 14 Days | 22.5% |
| 15 - 30 Days | 13.7% |
| 31 - 60 Days | 18.9% |
| 61 - 90 Days | 8.1% |
| 91 - 120 Days | 2.3% |
| 121 - 150 Days | 2.0% |
| 151 - 180 Days | 3.3% |
| 181 - 210 Days | 4.5% |
| 211 - 240 Days | 3.2% |
| 241 - 270 Days | 0.0% |
| 271 - 300 Days | 0.8% |
| 301 - 365 Days | 3.6% |
| 366 - 732 Days | 8.2% |
| 733 - 1,098 Days | 7.3% |
| 1,099 - 1,875 Days | 1.5% |
| **Total % of Portfolio:** | **100.0%** |

| S & P Credit Quality Composition | |
|---|---|
| AAA | 51.5% |
| AA | 6.5% |
| A | 40.8% |
| BBB | 0.0% |
| Non-Investment Grade | 1.1% |
| **Total % of Portfolio:** | **100.0%** |

*O/N stands for overnight.



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# CAT 2007 A Fund Change in Market Value
# Periods Ending 12/31/2011

| Summary of Cash Flows | | |
|---|---|---|
| | **Fourth Quarter** | **Fiscal YTD*** |
| **Beginning Market Value** | $3,506,553,085 | $3,520,574,843 |
| **+/- Net Contributions/(Withdrawals)** | -- | ($15,290,037) |
| **Investment Earnings** | $3,513,643 | $4,781,922 |
| **= Ending Market Value** | $3,510,066,728 | $3,510,066,728 |
| **Net Change** | $3,513,643 | ($10,508,115) |

*Period July 2011 – December 2011



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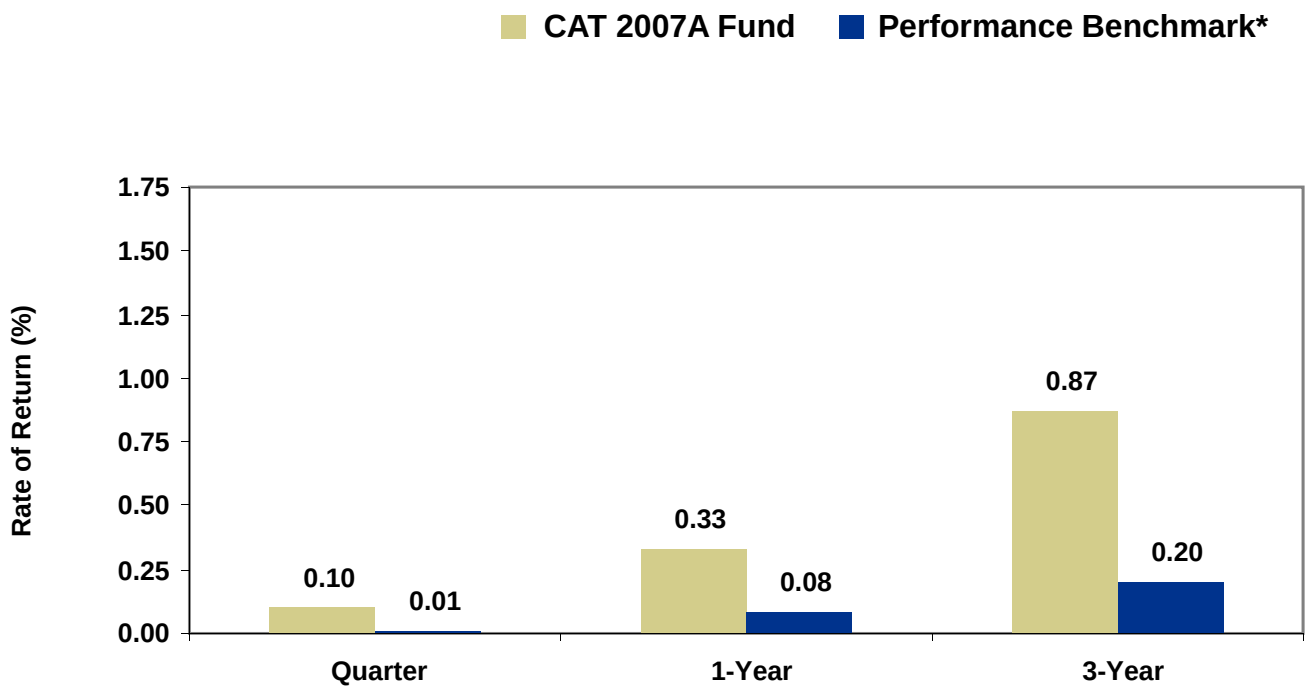
# CAT 2007 A Fund Investment Results
# Periods Ending 12/31/2011




*Performance Benchmark: The CAT 2007 A Fund was benchmarked to the Merrill Lynch 1-Month LIBOR from March 2008 to December 2009. From January 2010 to June 2010, it was a blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Gross Index. Effective July 2010, it is a blend of the average of the 3-Month Treasury Bill rate and the iMoneyNet First Tier Institutional Money Market Fund Net Index.



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# CAT 2007 A Fund Characteristics
# Period Ending 12/31/2011

| Effective Maturity Schedule | |
|---|---|
| O/N* - 14 Days | 25.1% |
| 15 - 30 Days | 13.3% |
| 31 - 60 Days | 18.4% |
| 61 - 90 Days | 3.1% |
| 91 - 120 Days | 0.8% |
| 121 - 150 Days | 3.1% |
| 151 - 180 Days | 4.1% |
| 181 - 210 Days | 5.8% |
| 211 - 240 Days | 6.2% |
| 241 - 270 Days | 1.0% |
| 271 - 300 Days | 1.1% |
| 301 - 365 Days | 3.0% |
| 366 - 732 Days | 8.6% |
| 733 - 1,098 Days | 6.4% |
| 1,099 - 1,875 Days | 0.0% |
| **Total % of Portfolio:** | **100.0%** |

| S & P Credit Quality Composition | |
|---|---|
| AAA | 51.8% |
| AA | 10.0% |
| A | 38.2% |
| BBB | 0.0% |
| Non-Investment Grade | 0.0% |
| **Total % of Portfolio:** | **100.0%** |

*O/N stands for overnight.



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# State Board of Administration of Florida
# Lawton Chiles Endowment Fund Review

Fourth Quarter 2011

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# Executive Summary

- Established in July 1999, the Lawton Chiles Endowment Fund was created to provide a source of funding for child health and welfare programs, elder programs, and research related to tobacco use.
  - Investment objective is to preserve the real value of the net contributed principal and provide annual cash flows for appropriation.
  - The Endowment's investments are diversified across various asset classes including domestic equity, foreign equity, fixed income, inflation-indexed bonds (TIPS), and cash.
- The Endowment assets totaled $738.6 million as of December 31, 2011.
  - At quarter-end, the Endowment's actual allocations were very close to the policy target.
- Over the trailing one-, three-, five-, and ten-year periods, the Endowment's return outperformed that of its target.



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# LCEF Change in Market Value
# Periods Ending 12/31/2011

| Summary of Cash Flows | | |
|---|---|---|
| | **Fourth Quarter** | **Fiscal YTD*** |
| | | |
| **Beginning Market Value** | $685,382,630 | $767,566,265 |
| **+/- Net Contributions/(Withdrawals)** | -- | -- |
| **Investment Earnings** | $53,249,035 | ($28,934,600) |
| **= Ending Market Value** | $738,631,665 | $738,631,665 |
| **Net Change** | $53,249,035 | ($28,934,600) |
| | | |

*Period July 2011 – December 2011



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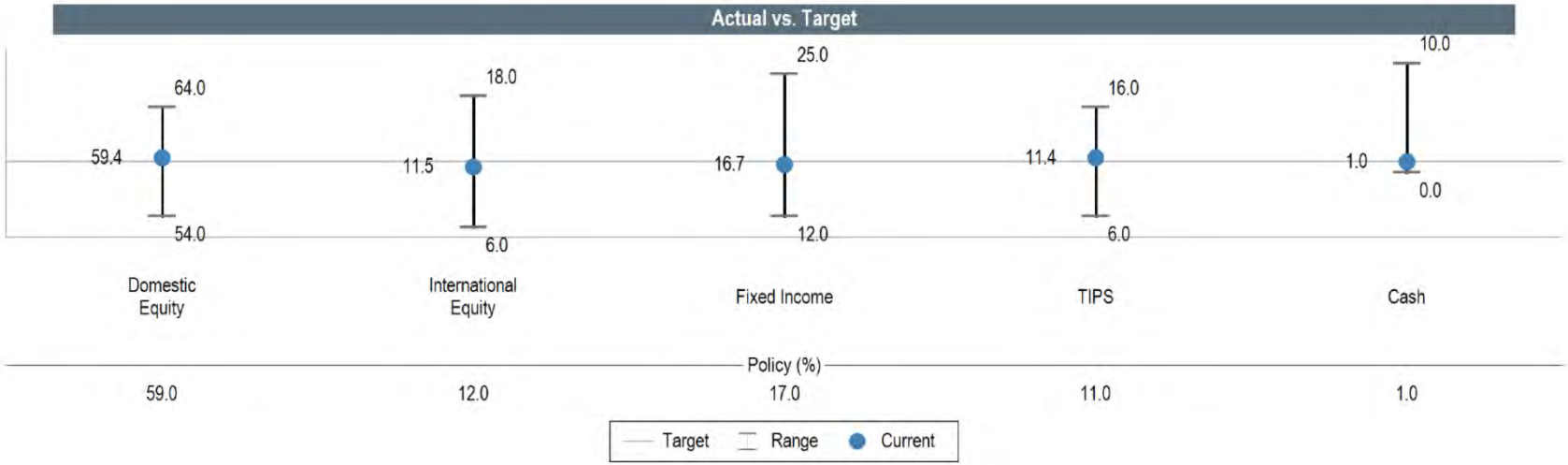
# Asset Allocation as of 12/31/2011
# Total Fund Assets = $738.6 Million



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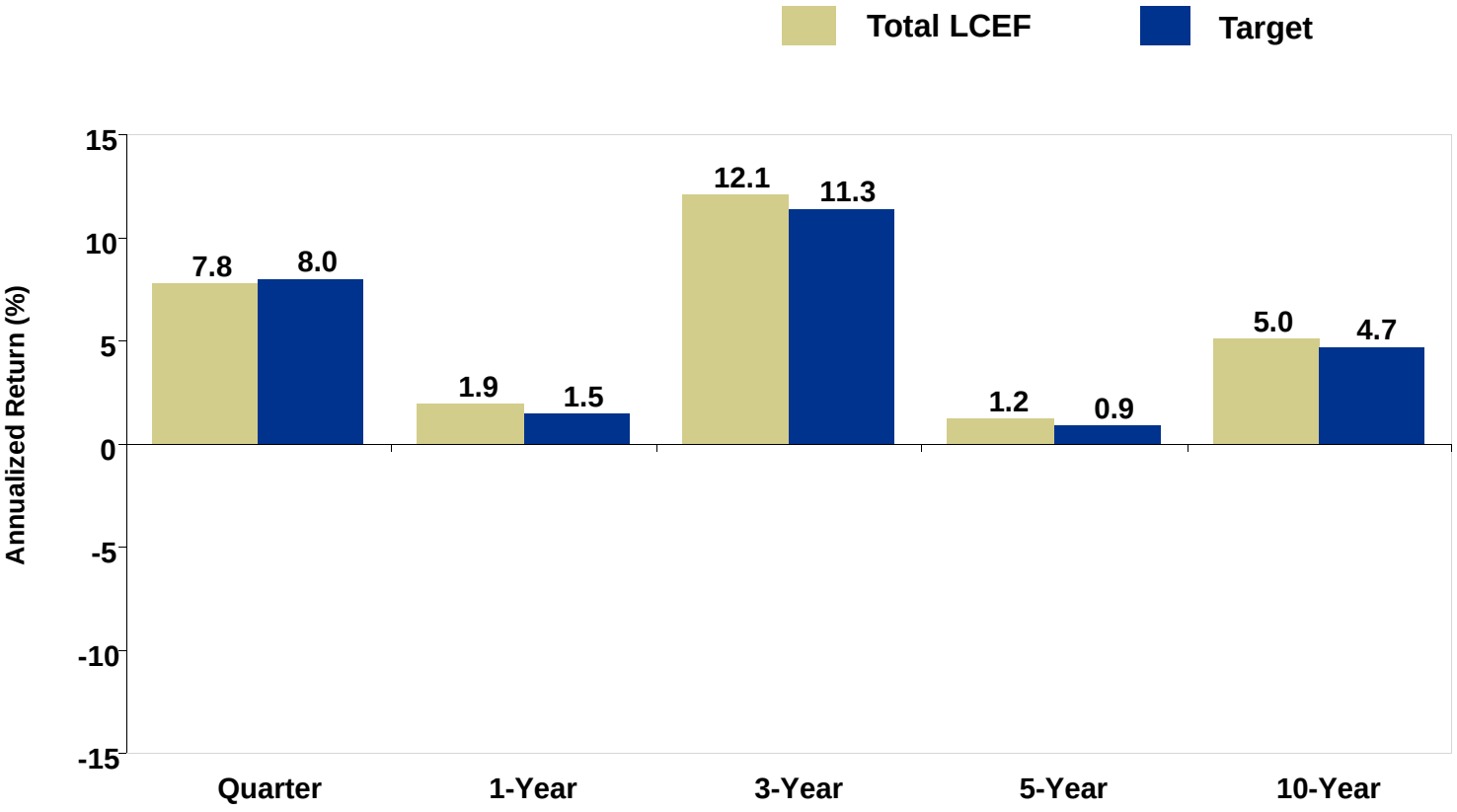
# LCEF Investment Results
# Periods Ending 12/31/2011



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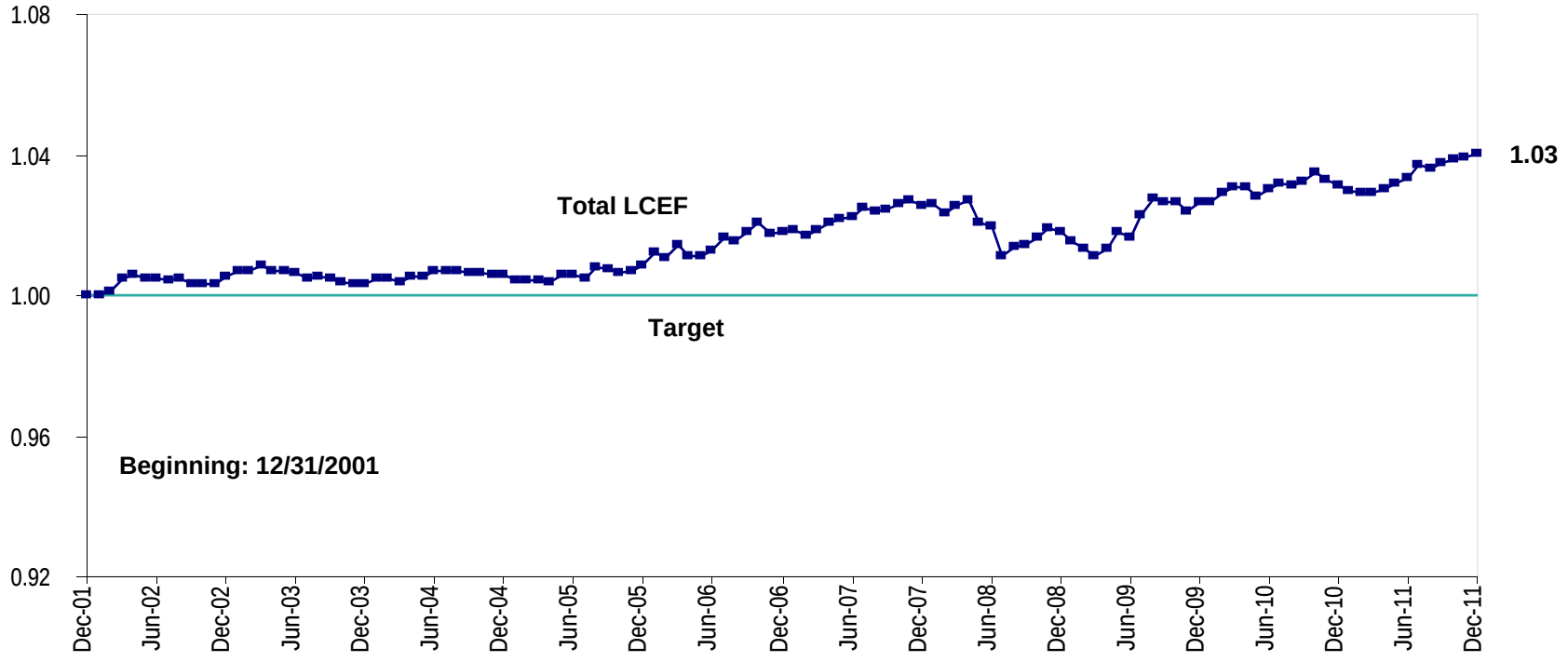
# LCEF Cumulative Relative Performance
# 10 Years Ending 12/31/2011



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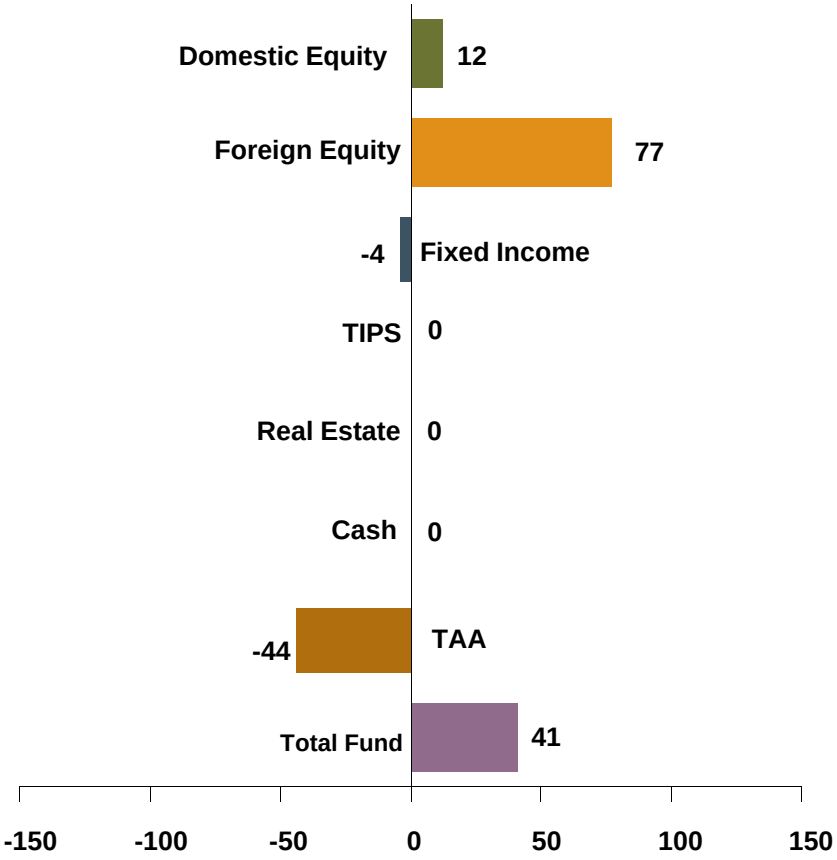
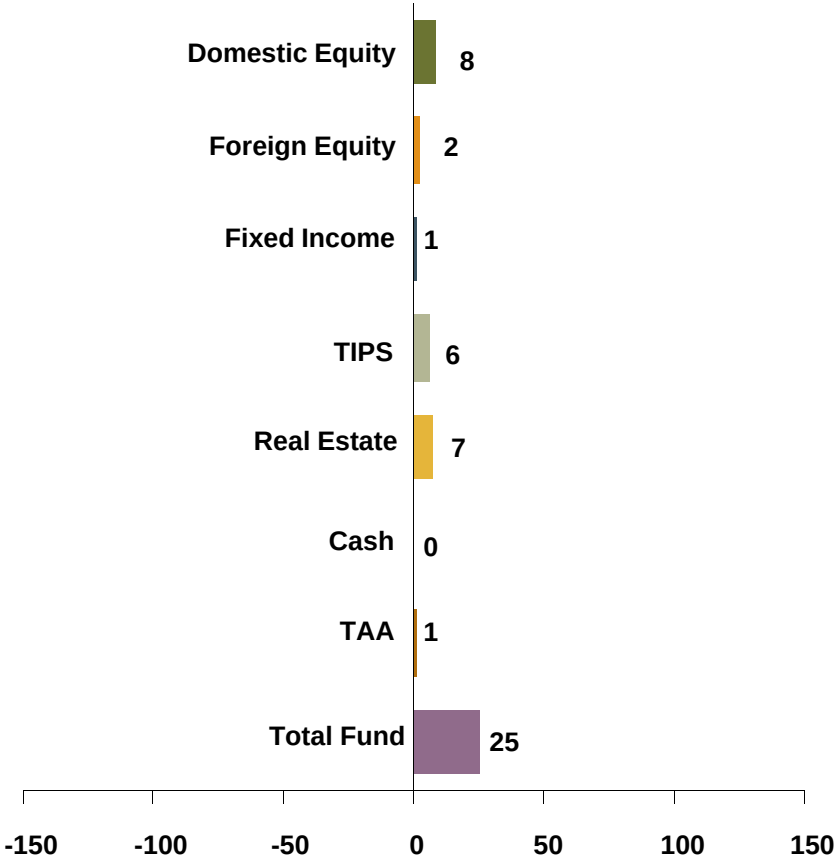
# LCEF Attribution Analysis




1 Year Ending 12/31/2011




5 Years Ending 12/31/2011

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# State Board of Administration of Florida
# Florida PRIME and Fund B Review

Fourth Quarter 2011

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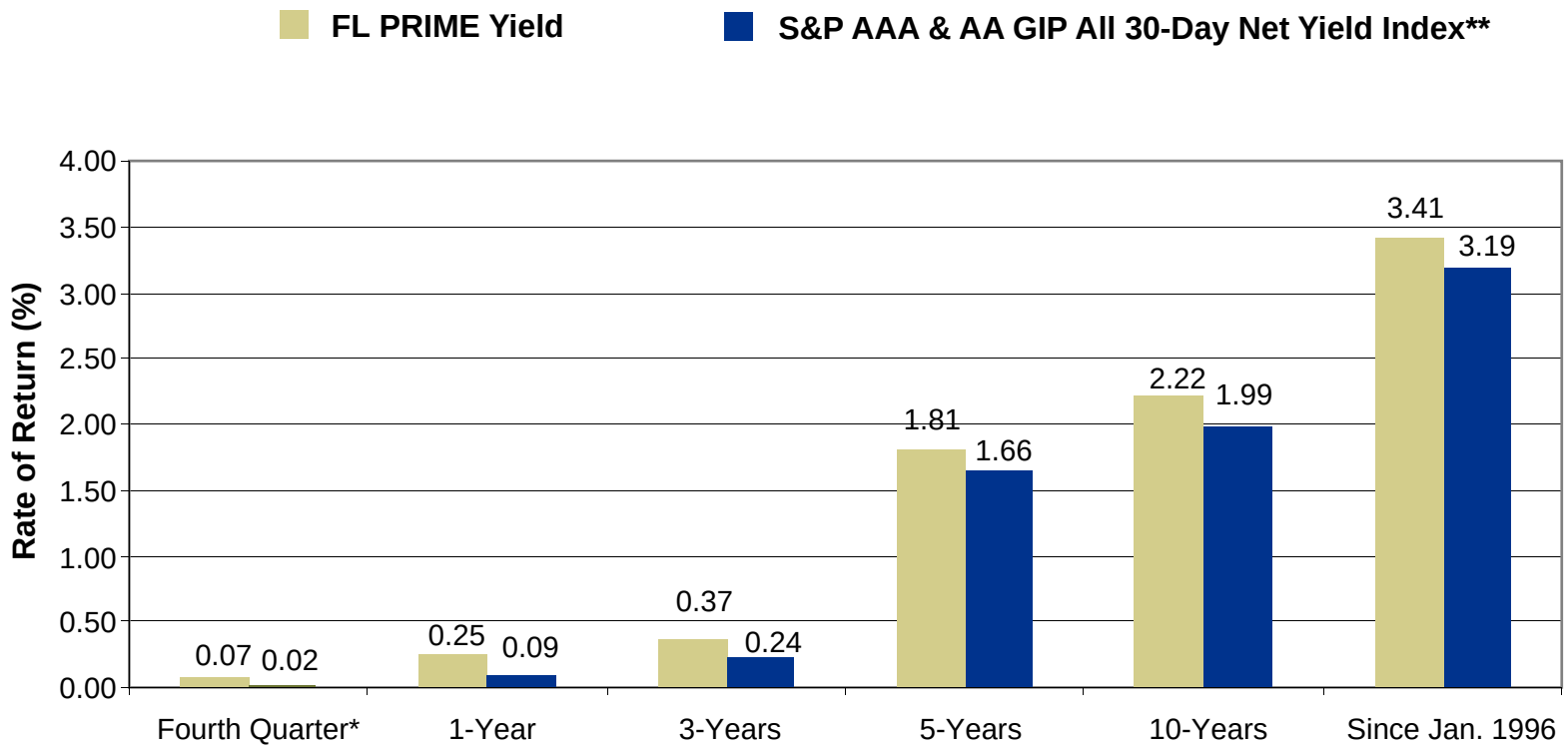
# Executive Summary

- The purpose of Florida PRIME is safety, liquidity, and competitive returns with minimal risk for participants.
- The Florida PRIME investment policy appropriately constrains the Fund to invest in short-term and high quality bonds to minimize both interest rate and credit risk.
- Florida PRIME is adequately diversified across issuers within the short-term bond market and adequate liquidity exists to address the cash flow obligations of the Fund.
- Performance of Florida PRIME on both an absolute and relative basis has been strong over short- and long-term time periods.
- As of December 31, 2011, the total market value of Florida PRIME was $7.78 billion.
- Hewitt EnnisKnupp, in conjunction with SBA staff, compiles an annual best practices report that includes a full review of the Investment Policy Statement, operational items, and investment structure for Florida PRIME.

# Florida PRIME Investment Results
# Periods Ending 12/31/2011




*Returns less than one year are not annualized.
**S&P AAA & AA GIP All 30-Day Net Yield Index for all time periods shown.



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# Florida PRIME Characteristics
# Quarter Ending 12/31/2011

| Cash Flows as of 12/31/2011 | Fourth Quarter | Fiscal YTD* |
|---|---|---|
| Opening Balance | $6,137,609,765 | $6,823,921,541 |
| Participant Deposits | $6,729,599,159 | $9,413,952,716 |
| Transfers from Fund B | $13,225,000 | $28,125,000 |
| Gross Earnings | $4,683,060 | $8,777,156 |
| Participant Withdrawals | ($5,101,619,025) | ($8,490,868,204) |
| Fees | ($403,890) | ($814,140) |
| Closing Balance (12/31/2011) | $7,783,094,067 | $7,783,094,067 |
| **Change** | **$1,645,484,302** | **$959,172,526** |

*Period July 2011 – December 2011



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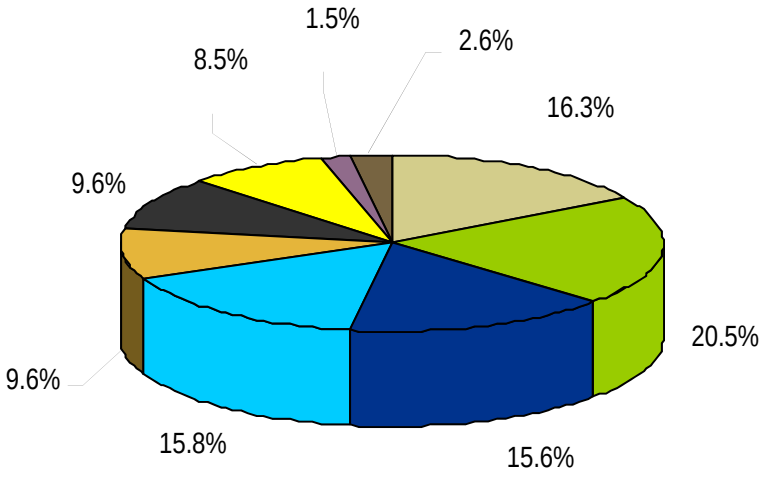
# Florida PRIME Characteristics
# Quarter Ending 12/31/2011

Portfolio Composition




- Bank Instrument - Fixed
- Repurchase Agreements
- Corporate Commercial Paper - Fixed
- Bank Instrument - Floating
- Mutual Funds - Money Market
- Asset Backed Commercial Paper - Fixed
- Corporate Notes - Floating
- Asset Backed Commercial Paper - Floating
- Corporate Commercial Paper - Floating



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# Florida PRIME Characteristics
# Period Ending 12/31/2011

| Effective Maturity Schedule | |
|---|---|
| 1-7 days | 42.9% |
| 8-30 days | 22.2 |
| 31-90 days | 28.2 |
| 91-180 days | 3.7 |
| 181+ days | 3.0 |
| **Total % of Portfolio:** | **100.0%** |

| S & P Credit Quality Composition | |
|---|---|
| A-1+ | 55.4% |
| A-1 | 44.6 |
| **Total % of Portfolio:** | **100.0%** |



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# Fund B Change in Market Value
# Period Ending 12/31/2011

| Cash Flows as of 12/31/2011 | Fourth Quarter | Fiscal YTD* |
|---|---|---|
| Opening Balance | $241,621,423 | $263,794,745 |
| Participant Distributions | ($13,225,000) | ($28,125,000) |
| Expenses Paid | ($103,764) | ($138,195) |
| Price Change | $6,395,177 | $843,714 |
| Closing Balance | $234,687,836 | $234,687,836 |
| **Change** | **($6,933,587)** | **($29,106,909)** |

*Period July 2011 – December 2011

- As of December 2011, 84.8% of the original principal in Fund B has been returned to participants.



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# State Board of Administration of Florida

# FRS Pension Plan

Fourth Quarter 2011

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# Market Environment

## Fourth Quarter 2011

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# Market Highlights

| Returns of the Major Capital Markets | | | | | |
|---|---|---|---|---|---|
| | | Annualized Periods Ending 12/31/2011 | | | |
| | Fourth Quarter | 1-Year | 3-Year | 5-Year | 10-Year |
| **Domestic Stock Indices** | | | | | |
| Russell 3000 Index | 12.1% | 1.0% | 14.9% | 0.0% | 3.5% |
| Dow Jones U.S. Total Stock Market Index | 12.1% | 1.1% | 15.2% | 0.2% | 3.9% |
| S&P 500 Index | 11.8% | 2.1% | 14.1% | -0.3% | 2.9% |
| Russell 2000 Index | 15.5% | -4.2% | 15.6% | 0.2% | 5.6% |
| **Domestic/Foreign Bond Indices** | | | | | |
| Barclays Capital Aggregate Bond Index | 1.1% | 7.8% | 6.8% | 6.5% | 5.8% |
| Barclays Capital Long Gov't Index | 1.8% | 29.1% | 7.5% | 10.8% | 8.9% |
| Barclays Capital Long Credit Index | 3.2% | 17.1% | 14.8% | 8.6% | 8.1% |
| Barclays Capital Long Gov't/Credit Index | 2.6% | 22.5% | 11.2% | 9.7% | 8.5% |
| SSB Non-U.S. WGBI | -0.5% | 5.2% | 4.9% | 7.2% | 8.4% |
| **Foreign/Global Stock Indices** | | | | | |
| MSCI All Country World IMI Index | 7.2% | -7.9% | 12.8% | -1.6% | 4.9% |
| MSCI All Country World ex-U.S. IMI Index | 3.3% | -14.3% | 11.5% | -2.7% | 7.0% |
| MSCI EAFE Index | 3.3% | -12.1% | 7.6% | -4.7% | 4.7% |
| MSCI Emerging Markets Index | 4.4% | -18.4% | 20.1% | 2.4% | 13.9% |

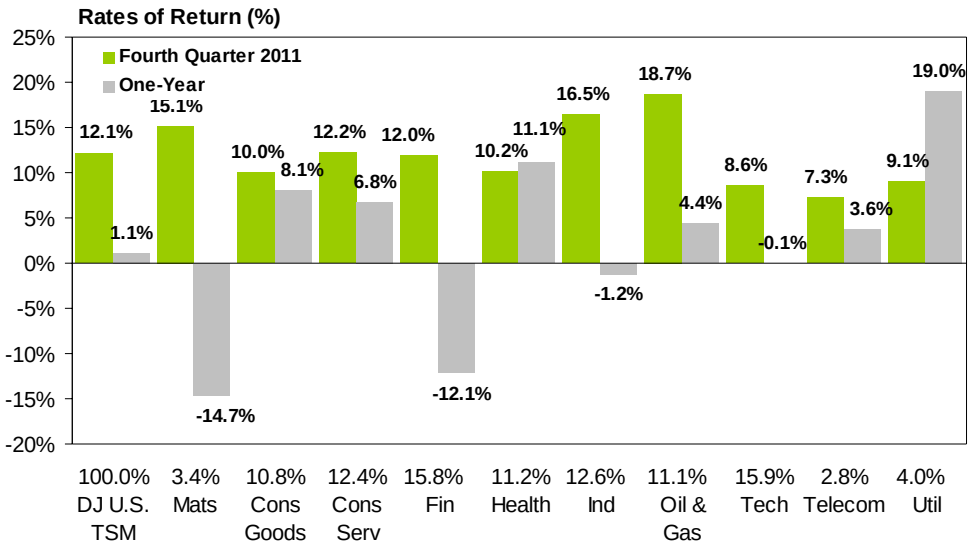
- Performance across capital markets was broadly positive during the fourth quarter. U.S. equities significantly outperformed non-U.S. markets over the quarter and full year. The rally in the U.S. equity markets during the fourth quarter was only enough to offset the losses over the prior three quarters, leaving most U.S. equity indices virtually flat for 2011. Better than expected economic data in the U.S. led to a strong “Santa’s Rally” which began in October.

- Concerns over the European debt crisis and slowing growth in emerging countries weighed on non-U.S. equities. These markets ended 2011 with double-digit negative returns.

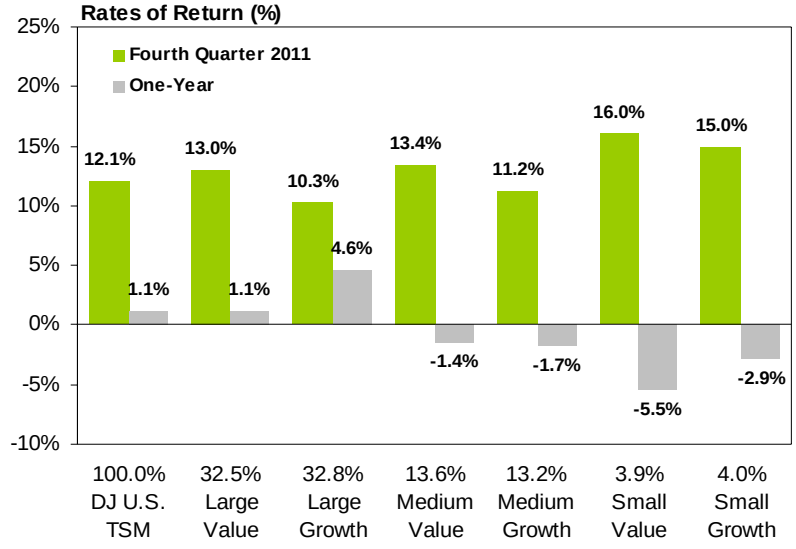
- For the year, fixed income markets generally produced strong positive returns. Higher quality, long-dated securities were rewarded. The Barclays Capital Long Government Index, consisting primarily of long duration U.S. Treasury bonds, finished the year with a 29.1% return, topping all asset classes.

# U.S. Equity Markets

**SECTOR RETURNS**
**AS OF 12/31/2011**




**STYLE RETURNS**
**AS OF 12/31/2011**




- Better than expected consumer spending data, increased manufacturing activities, as well as favorable labor market data injected a much desired level of optimism into the U.S. equity market during the fourth quarter.
- The Dow Jones Total Stock Market Index soared 12.1% during the quarter.
- All sectors within the Dow Jones Total Stock Market Index posted strong gains in the fourth quarter. Cyclical sectors outperformed defensive sectors. Oil & gas, industrials, and materials were among the top-performing sectors returning 18.7%, 16.5%, and 15.1%, respectively.
- During the fourth quarter, risk appetite returned to the market. All areas within the market capitalization spectrum produced positive results.



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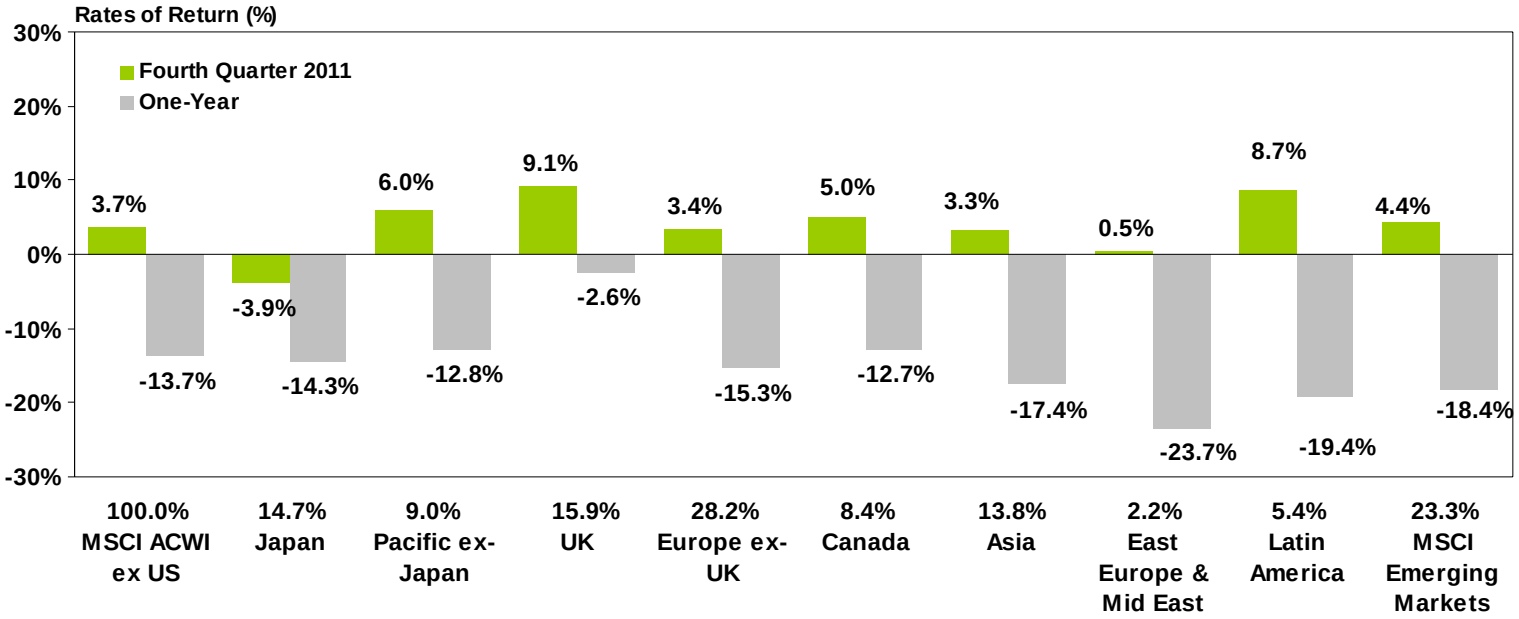
# Non-U.S. Equity Markets

**REGION RETURNS**
**AS OF 12/31/2011**




- Non-U.S. equity markets gained positive momentum, originating from the U.S. market, during the fourth quarter posting a 3.7% return. All major markets (developed and emerging) posted gains during the quarter with the exception of Japan. For the year 2011, all major markets plummeted with double digits losses, with the exception of the UK.

- Among developed markets, the UK performed the strongest, returning 9.1% for the fourth quarter. Through 2011, the UK was also the top performer, posting a mere 2.6% loss. Staying independent from the European currency union, the UK appeared to be less exposed to the European sovereign debt crisis than other major European economies.

- Among emerging markets, Peru switched swiftly from the worst market in the third quarter to the strongest one, returning 11.6% in the fourth quarter. For the year 2011, Indonesia was the only emerging market in positive territory, gaining 4.0%.



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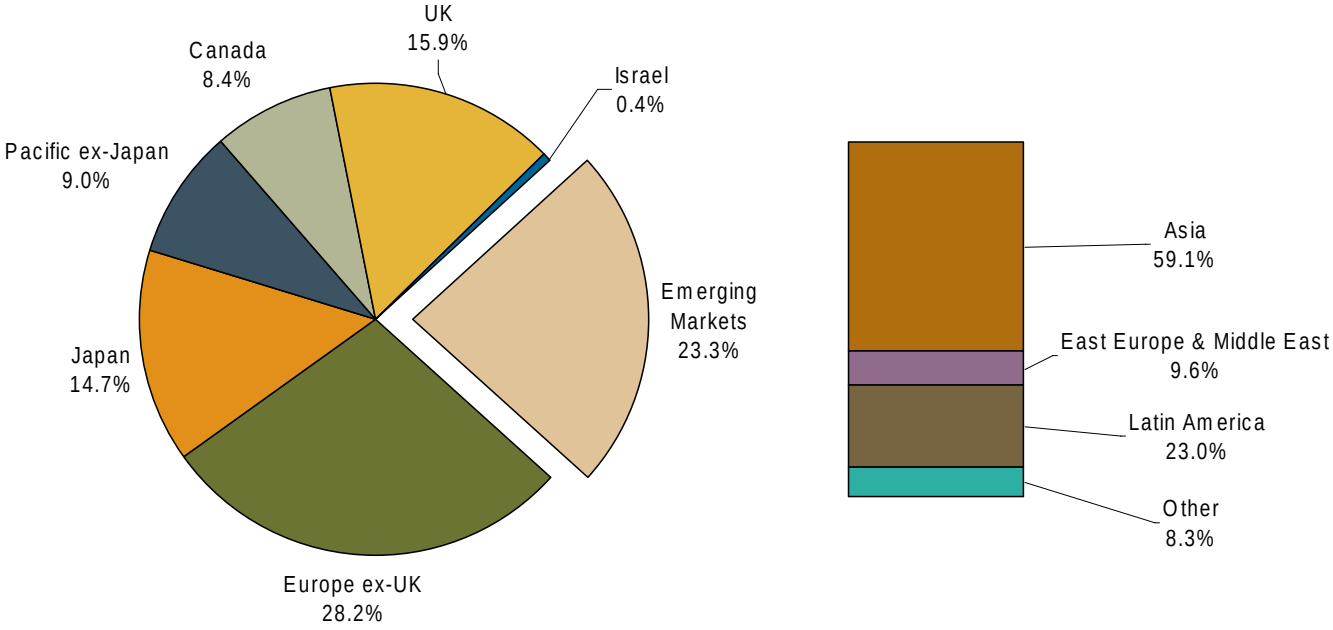
# Non-U.S. Equity Markets

**MSCI ALL COUNTRY WORLD EX-U.S. INDEX**
**GEOGRAPHIC ALLOCATION AS OF 12/31/2011**




- The exhibit above illustrates the percent each region represents of the non-U.S. stock market as measured by the MSCI All Country World ex-U.S. Index.
- Note on Other: Includes South Africa, Egypt, and Morocco.



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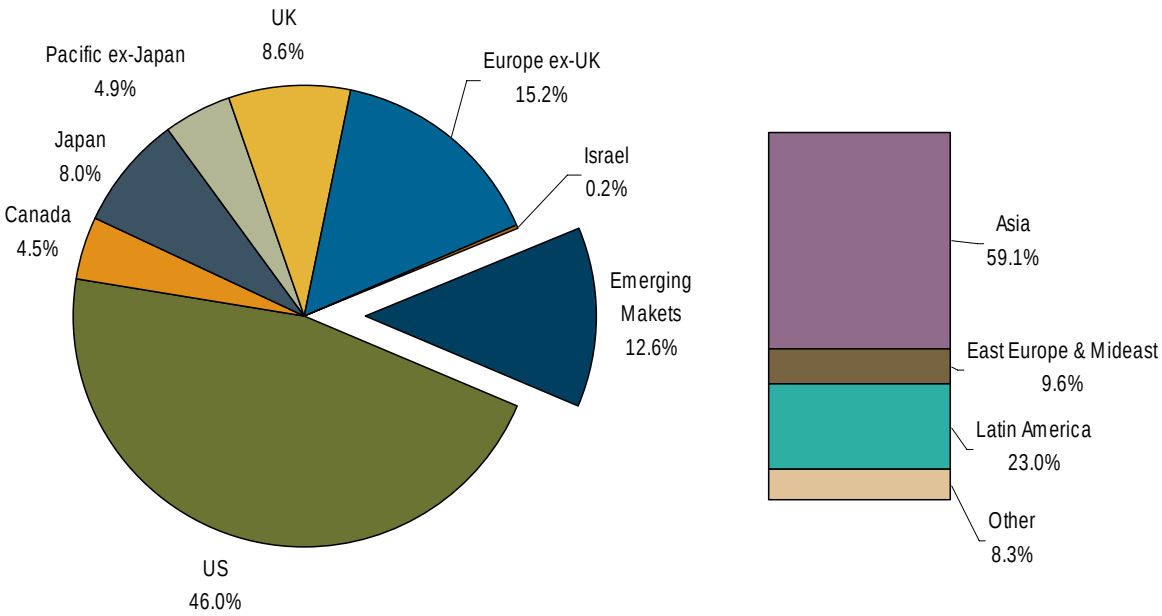
# Global Stock Markets

**MSCI ALL COUNTRY WORLD INDEX**
**GEOGRAPHIC ALLOCATION AS OF 12/31/2011**




- The MSCI All Country World Index is a capitalization-weighted index of stocks representing 24 developed stock markets and 21 emerging stock markets around the world. The graph above shows the allocation to each region at quarter-end.
- Note on Other: Includes South Africa, Egypt, and Morocco.



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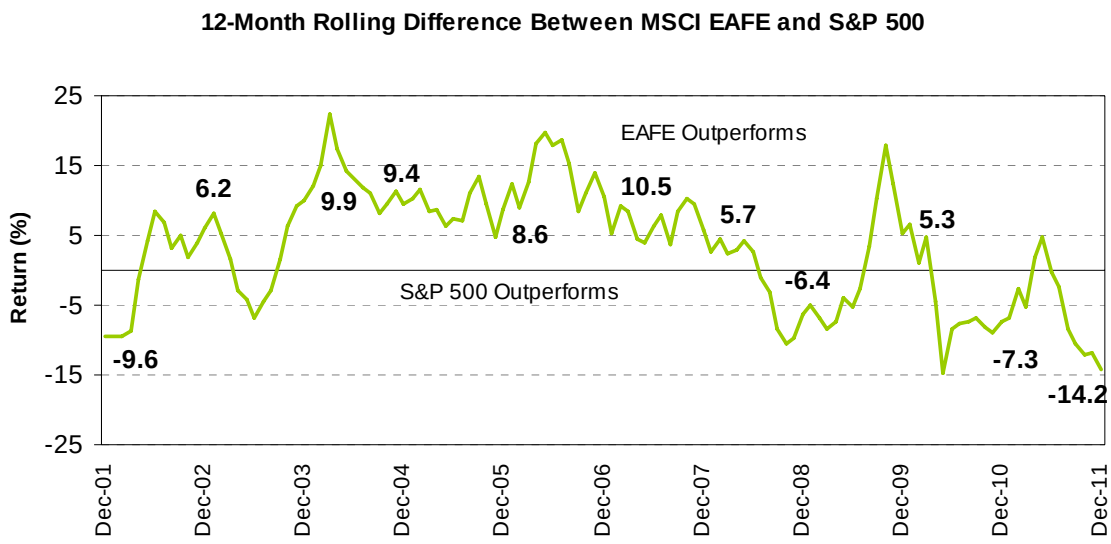
# Non-U.S. vs. U.S. Equity – Market Performance Over Time




**2011 in Review**

- Currency fluctuations did not have a major impact on the performance differential in 2011.
- No single region was responsible for the performance differential (Europe -10%, Japan -14%, Australia -11%).
- U.S. economy continues to steadily expand with outlook improving.
- European growth prospects hampered by the sovereign debt crisis.
- Japan's economy was destabilized by the earthquake in March in combination with a strong yen which hurt exports.
- Australian growth prospects were lowered, due to a slowing Chinese economy and resulting drop in the demand for commodities.
- Canadian mining companies were a drag on performance, due to lower expected commodity demand from China and Europe.



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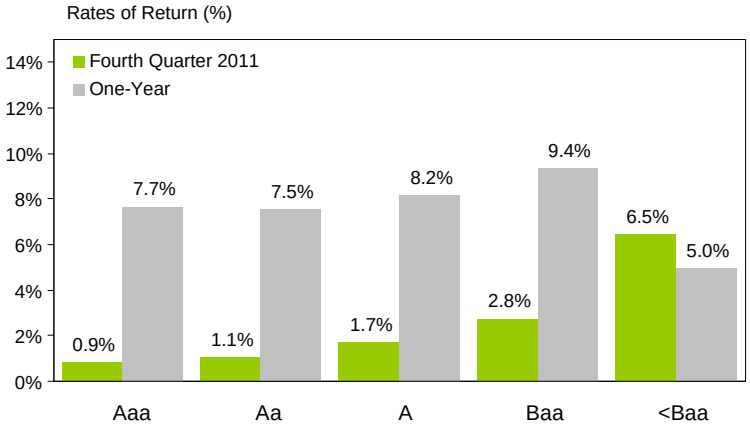
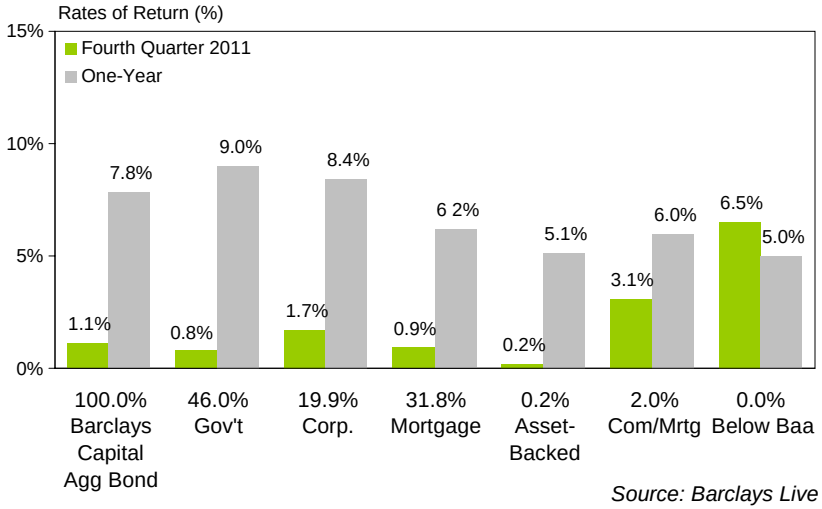
# U.S. Fixed Income Markets

**RETURNS BY QUALITY**
**AS OF 12/31/2011**




*Source: Barclays Live*

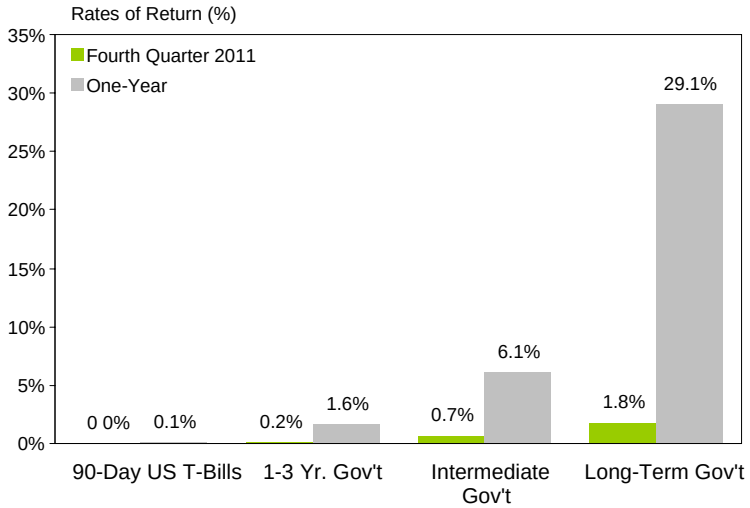
**SECTOR RETURNS**
**AS OF 12/31/2011**




*Source: Barclays Live*

- As investors increased risk appetite in October, lower credit bonds performed more strongly than higher credit bonds. Non-investment grade bonds were the top-performing sector, gaining 6.5% during the fourth quarter.
- For year 2011, Government has been the strongest sector, gaining 9.0%. Below investment-grade assets performed the worst, gaining only 5.0% in 2011.
- Along the yield curve, long-term government issues continued to outperform their short-term counterparts in the fourth quarter.
- Spreads on investment-grade, high-yield, and mortgages all tightened in the fourth quarter.

**RETURNS BY MATURITY**
**AS OF 12/31/2011**




*Source: Barclays Live*



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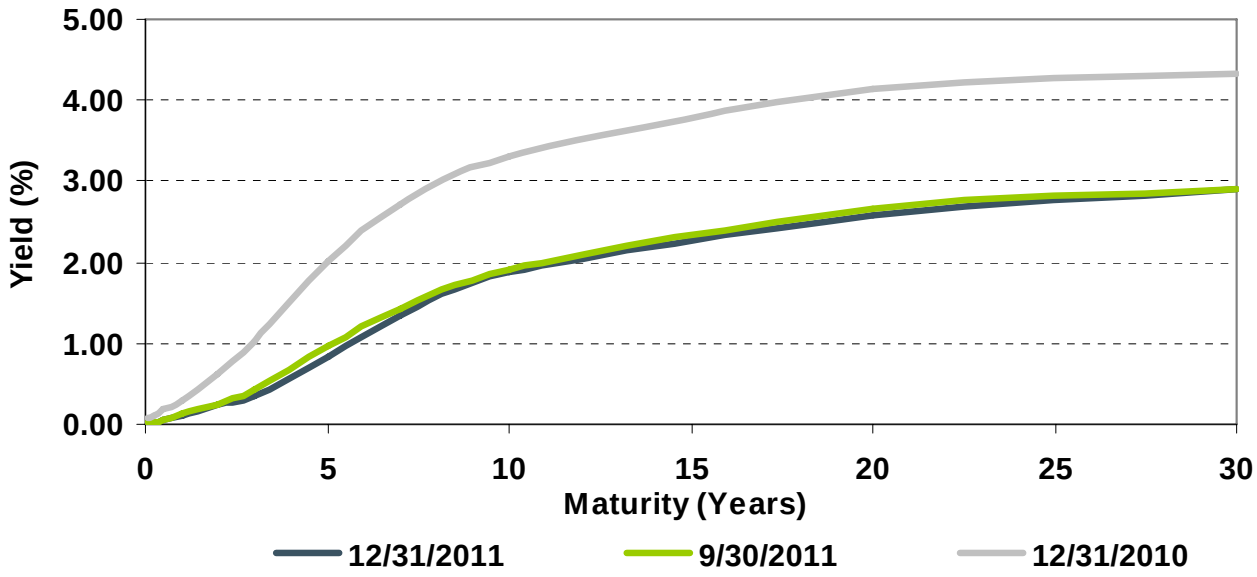
# U.S. Fixed Income Markets

**U.S. TREASURY YIELD CURVE**




*Source: U.S. Department of Treasury*

- Prices on long-dated Treasuries rose during the last two months of 2011.
- Compared to a year ago, yields on securities with more than five years to maturity are a full percentage point lower.
- While acknowledging better than expected U.S. economic data, the Federal Open Market Committee pledged to continue to extend the maturity of its holdings and keep the federal fund rates at 0 to 0.25%.



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# Credit Spreads

**AS OF 12/31/2011**

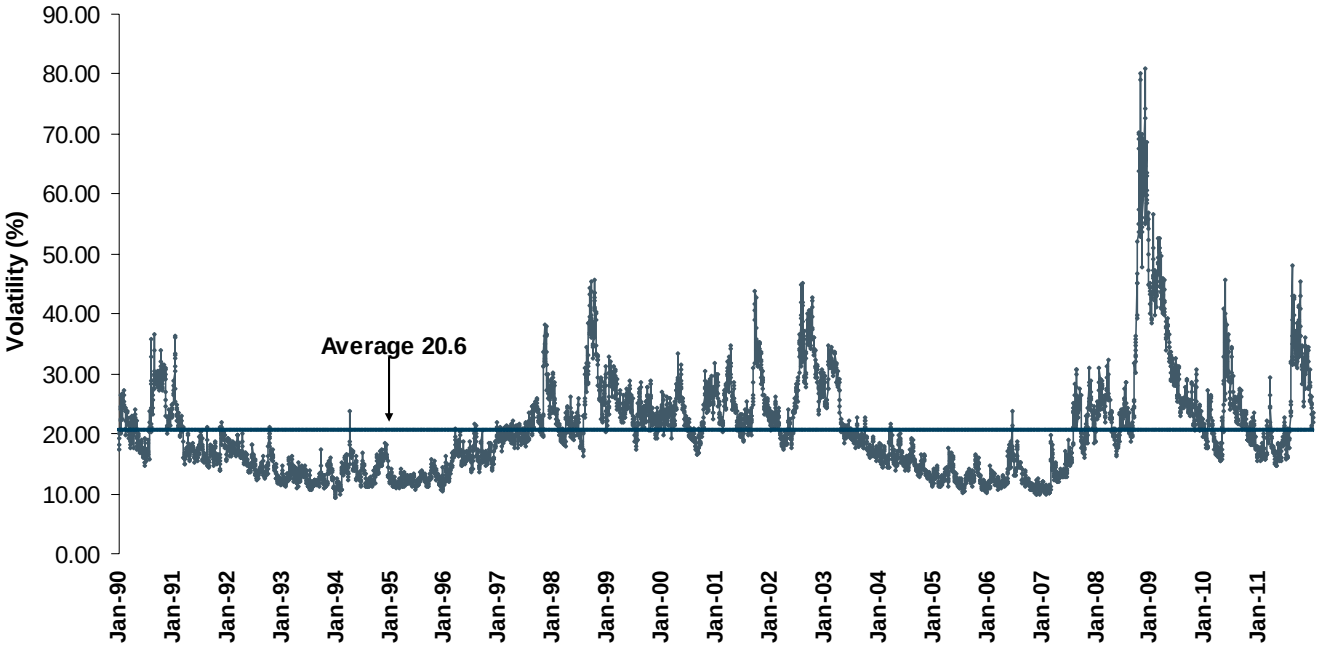
| Spread (bps) | 12/31/2011 | 9/30/2011 | 12/31/2010 | Quarterly Change (bps) | 1-Year Change (bps) |
|---|---|---|---|---|---|
| U.S. Aggregate | 87 | 90 | 56 | -3 | 31 |
| Long Gov't | 6 | 5 | 4 | 1 | 2 |
| Long Credit | 239 | 246 | 173 | -7 | 66 |
| Long Gov't/Credit | 131 | 132 | 99 | -1 | 32 |
| MBS | 77 | 82 | 41 | -5 | 36 |
| CMBS | 308 | 351 | 254 | -43 | 54 |
| ABS | 99 | 77 | 82 | 22 | 17 |
| Corporate | 234 | 238 | 156 | -4 | 78 |
| High Yield | 699 | 807 | 526 | -108 | 173 |
| Global Emerging Markets | 464 | 495 | 298 | -31 | 166 |

*Source: Barclays Live*

- During the fourth quarter, credit spreads narrowed across all segments, except for Long Government and ABS, due to investors' renewed appetite for risk beginning in October.
- Credit spreads across all segments are higher now than a year ago.
- Over the year, high yield and global emerging markets bonds have seen their credit spreads widen by 173 bps and 166 bps, respectively.

# Market Volatility

**Historical Daily VIX Closing Prices**
**Since Inception through December 31, 2011**




Source: CBOE

- Volatility at the end of 2011 approached its long-term average.
- As economic data turned more positive during the fourth quarter, there was a corresponding decrease in the VIX.



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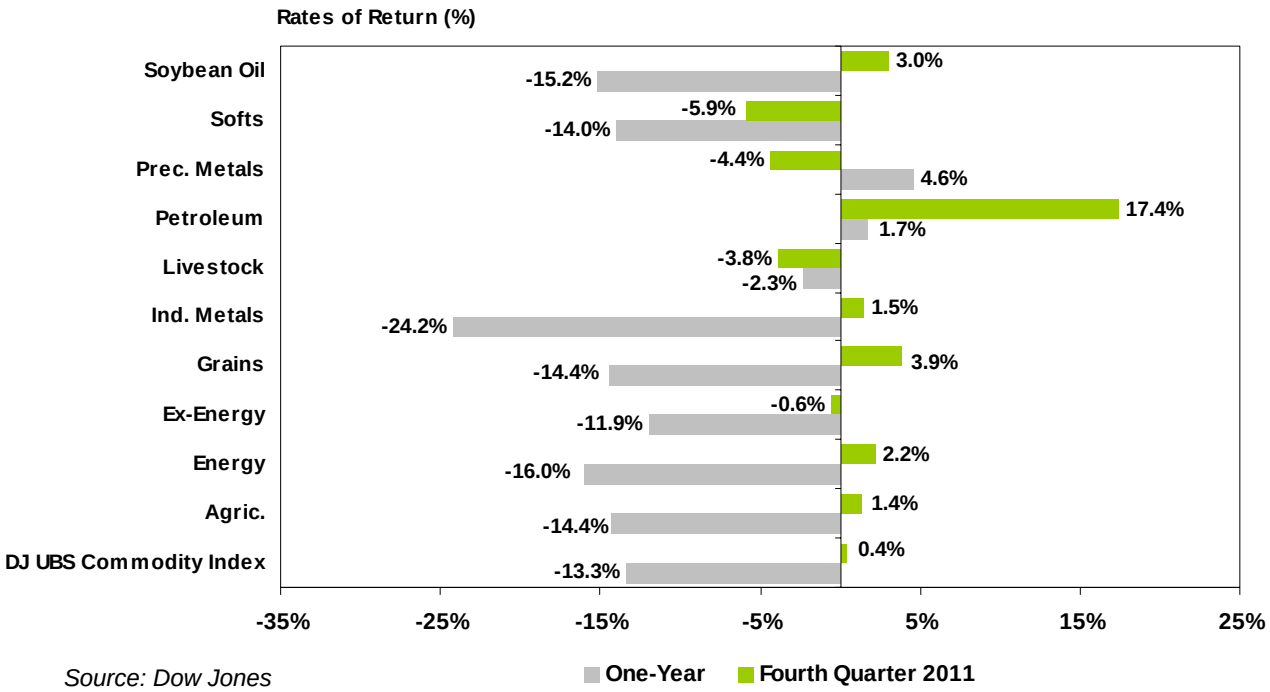
# Commodities

**COMMODITY SECTOR RETURNS**
**AS OF 12/31/2011**




*Source: Dow Jones*

- During the fourth quarter, commodity markets recovered modestly as the Dow Jones UBS Commodity Index gained 0.4%.
- Petroleum was the best performing sector, posting a gain of 17.4% for the quarter, while gold lost much of its glitter during the quarter.
- During 2011, commodity prices plummeted due to the worries over reduced global demand.



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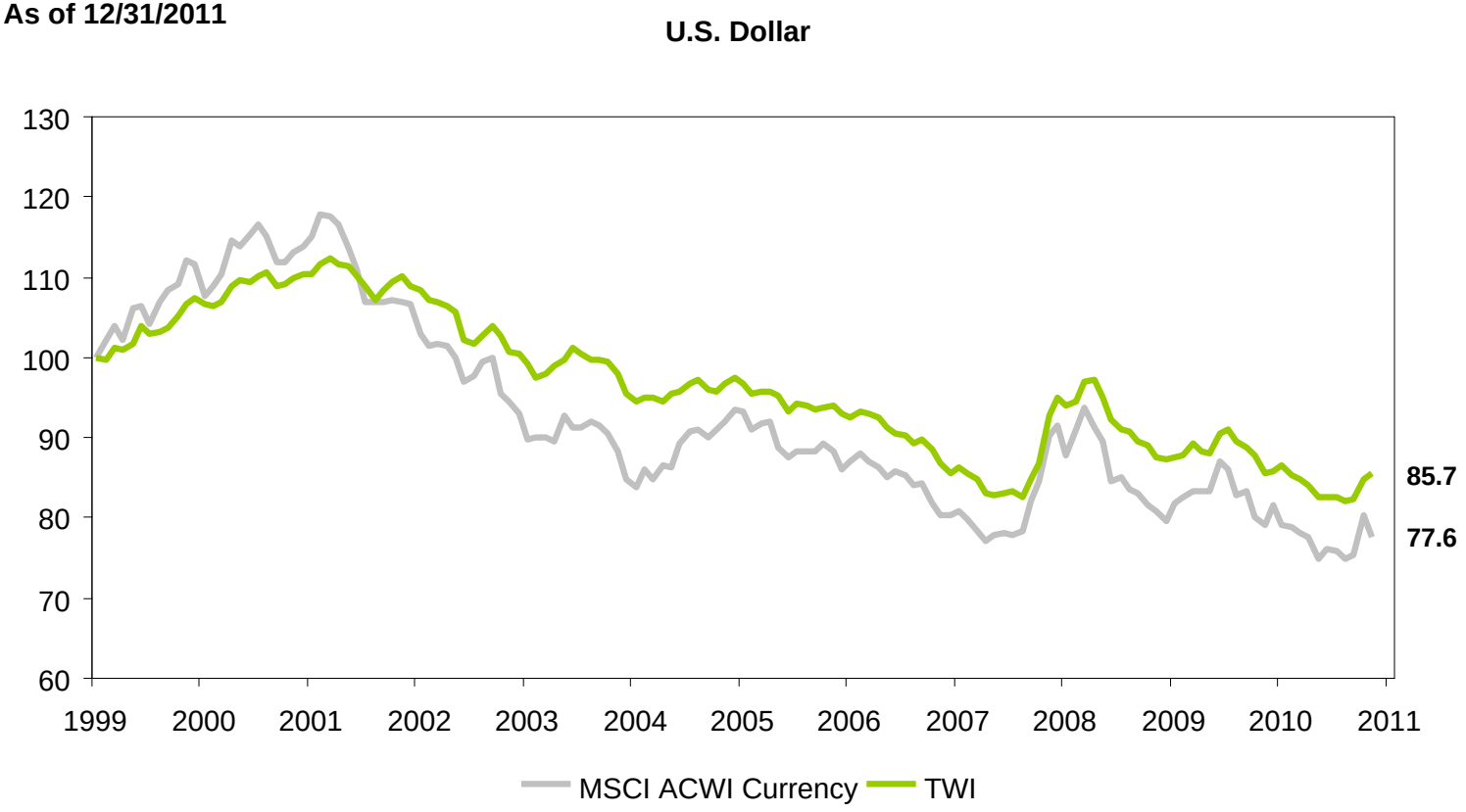
# Currency Impact

**As of 12/31/2011**




- The U.S. dollar has lost a third of its value since 2001 whether viewed from the perspective of the Trade Weighted Dollar Index (TWI) or an index comprised of currencies in an investor's typical non-U.S. equity portfolio.
- Twin deficits, as well as the more recent U.S. quantitative easing policy, have weighed on the dollar.



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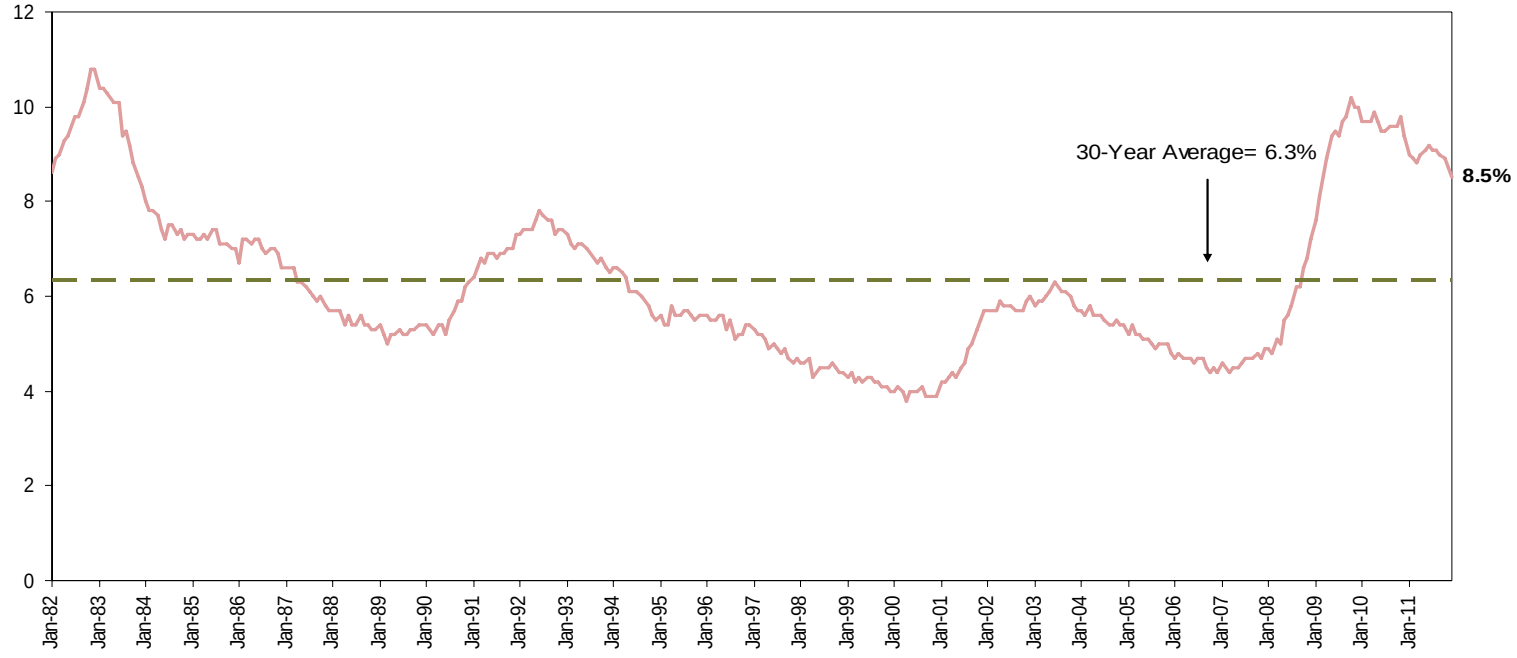
# U.S. Unemployment Rate

Unemployment Rate
As of December 2011




Source: Bureau of Labor Statistics

- During the fourth quarter, the U.S. unemployment rate declined to 8.5%, its lowest level in almost three years.
- The economy added 200,000 non-farm jobs in December, after adding 100,000 jobs in November and 80,000 in October.
- For the year, the economy has added about 1.64 million jobs, the most since 2006. The labor market still has a long way to recover the 8.75 million jobs lost in the recession that officially ended June 2009.



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# Active Manager Report Card[1]

| Peer Group/Index | Median Return [2] | | Index Return | | Index Return [1] | |
|---|---|---|---|---|---|---|
| | Qtr | 1 Year | Qtr | 1 Year | Qtr | 1 Year |
| All Cap Equity/ Russell 3000 Index | 11.3% | -0.6% | 12.1% | 1.0% | 39th Percentile | 35th Percentile |
| Large Cap Equity/ Russell 1000 Index | 11.4% | 1.0% | 11.8% | 1.5% | 39th Percentile | 44th Percentile |
| Small Cap Equity/ Russell 2000 Index | 15.0% | -2.6% | 15.5% | -4.2% | 43rd Percentile | 65th Percentile |
| Non-U.S. Equity/ MSCI ACWI ex-US | 5.0% | -12.9% | 3.7% | -13.7% | 68th Percentile | 59th Percentile |
| Global Equity/ MSCI ACWI | 7.3% | -6.7% | 7.2% | -7.4% | 56th Percentile | 55th Percentile |
| Core Fixed Income/ Barclays Aggregate | 1.3% | 7.7% | 1.1% | 7.8% | 75th Percentile | 47th Percentile |

- Over the fourth quarter, active management performance relative to passive management is mixed. The median returns of active managers in Core Fixed Income, Non-U.S. Equity, and Global Equity exceeded their respective index returns.
- Active management in Non-U.S. Equity significantly outperformed the index during the quarter. Passive management in All Cap, Large Cap, and Small Cap Equity outperformed the median active managers over the fourth quarter.
- For the year 2011, active management in Small Cap, Non-U.S. Equity, and Global Equity outperformed their passive peers.

[1] Actual peer group performance reported in client reports may vary based on constituent peer group utilized (e.g., mutual fund universe, separate account universe). Percentile rankings are based on a system in which 1=best and 99=worst.
[2] Based on preliminary peer group information as of December 31, 2011, provided by eVestment Alliance. Data was aggregated on January 09, 2012. Information is presented net of fees.

# U.S. Commercial Real Estate Sector Update

**The Three Pillars of Commercial Real Estate:**
Fundamentals continue to stabilize, but risks remain

Demand

- High unemployment and lackluster job growth continue to restrain net new demand for space.

Supply

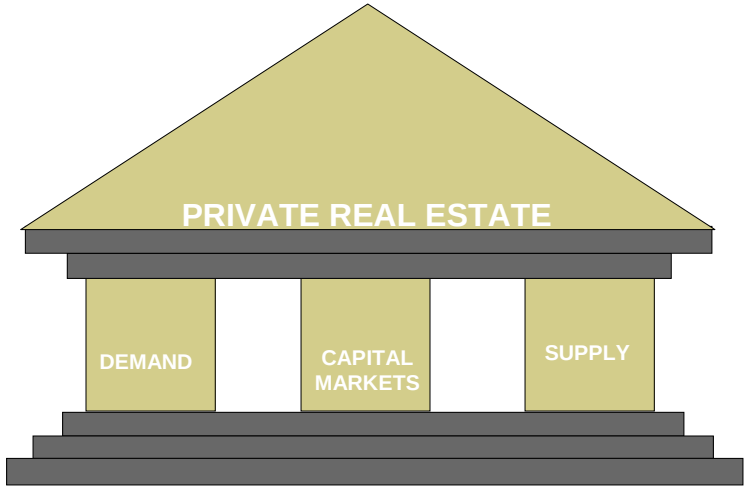
- New supply remains low due to tightened construction financing and lack of positive economics.
- Vacancies on existing supply remain high but are improving.

Capital Markets

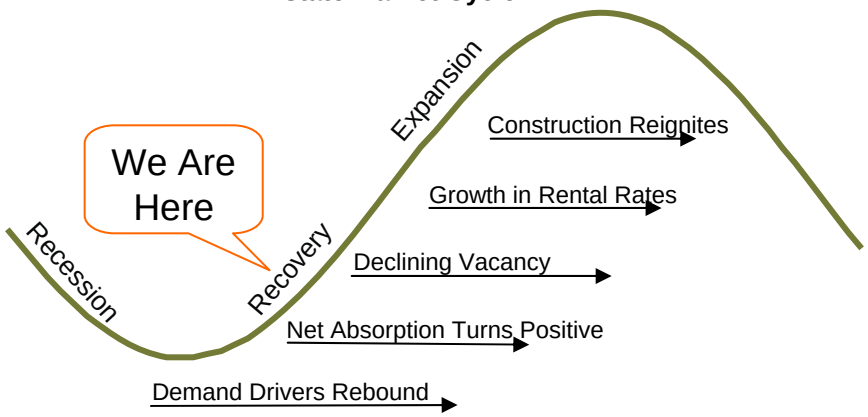
- Positive leverage still available for Core properties.
- Investor appetite for real estate is strong with capital waiting on the sidelines to be invested.

**Sector Fundamentals**

- Improvement in fundamentals slowed during the quarter in most property types due to widespread enhanced economic uncertainty.
- Downward pressure on net operating income in most markets remains as leases expire and re-sign at today's lower rates.
- Transaction activity slowed in all property types and regions; activity has more recently spread to secondary CBD locations in an effort to enhance yields.




**Stages of Fundamental Recovery in the Real Estate Market Cycle**



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# What's New in U.S. Real Estate in 3Q 2011?

Sector rebound moderated over the quarter as economic uncertainty increased

- NCREIF Property Index (NPI) registered 3.30% in Q3 driven by lower appreciation, down from 3.94% in 2Q; the trailing 1-year gross total return is 16.1%.
- FTSE NAREIT Equity REIT Index fell -14.7% over the quarter, registering only a 1.0% gain for the year ending September 30, 2011; multiples also declined but remain above long run average.
- Transactions totaled $49.8 billion, down from nearly $60 billion the prior quarter. While the pullback was widespread, volumes still represent a 38% increase from 3Q 2010.
- Fund closings declined 16% during the quarter and 13% compared to the same quarter last year.

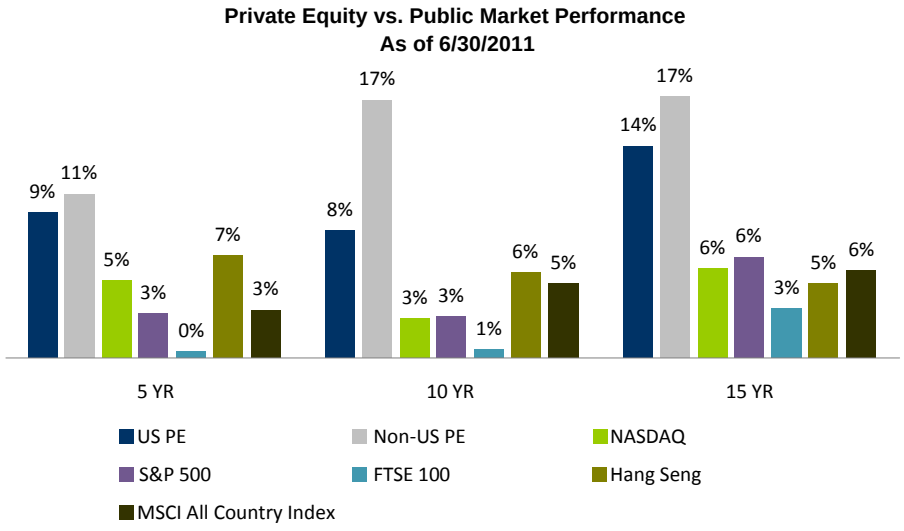
Further improvement in fundamentals is needed to continue the sector's rally

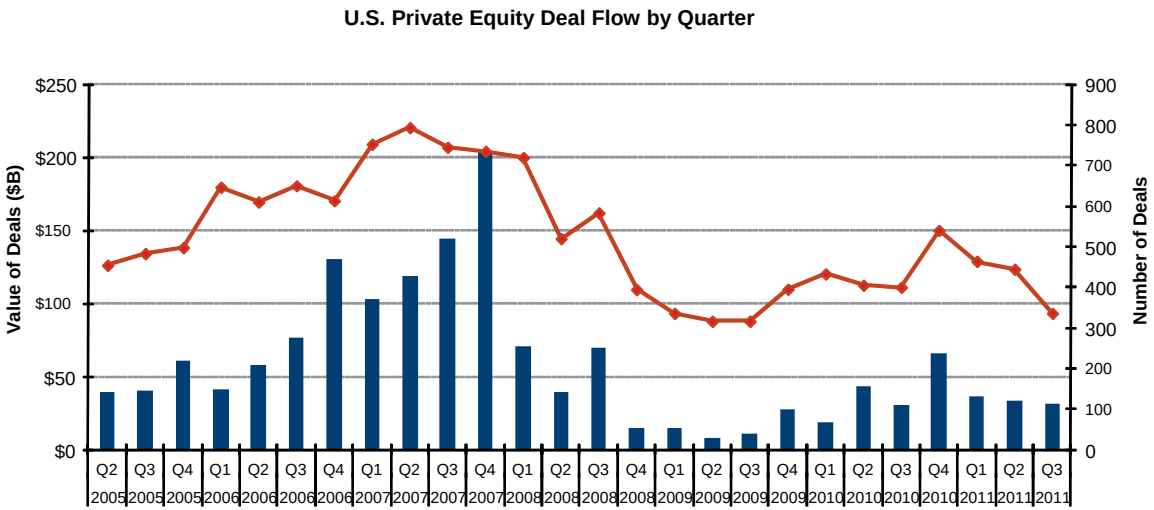
- Occupancy has firmed; but recovery is still highly bifurcated. Stalling employment growth is a major concern for the sector.
- Trends in net absorption slowed in many property types over the summer as confidence took a step back due to extensive global and domestic structural concerns.
- Rent and net operating income growth remain challenged for several property types and regions; this will be the last fundamental to display strength.

Distress remains, but resolutions are increasing

- New additions to distress dropped significantly during the quarter. When combined with new resolutions, total outstanding distress was reduced by $5.7 billion, illustrating an increasing willingness of lenders to address problems rather than "extend and pretend."
- One bright spot for owners is a loosening of lender's underwriting standards from the trough's strictness; financing for non-core investments is also expanding slowly.

# Private Equity Market Overview




Source: Thomson Reuters and S&P LCD. Deal flow excludes venture capital.

- **Fundraising:** All sectors significantly below pre-crisis levels.
- **Buyout:** A 23% decrease over Q2; scarcity of leveraged debt financing has led to sharp decline in activity in Europe; small to medium sized deals comprise 75% of transactions; purchase price multiples continue to increase; equity currently comprising ~39% of the purchase price.
- **Venture capital:** YTD investment increased; median pre-money valuations increased across all stages; exits slowing with 41 IPOs and 101 M&A transactions YTD.
- **Mezzanine:** Situation in Europe continues to favor mezzanine lenders as CLOs have limited cash to re-invest and European banks are dealing with capital constraints.
- **Distressed Debt:** Default rates remain at historically low levels; investment slow since 2009 & 2010, but potential opportunities strong 2013 & 2014 due to refinancing risk and capital constraints.
- **Secondaries:** $20 billion of transactions for 2011 YTD, on pace to exceed 2010; pricing remains at a small discount to NAV.
- **Infrastructure:** Deal activity decreased from the 2Q2011 as 36 deals were transacted in the 3Q2011; healthy pipeline of deal activity for remainder of 2011.



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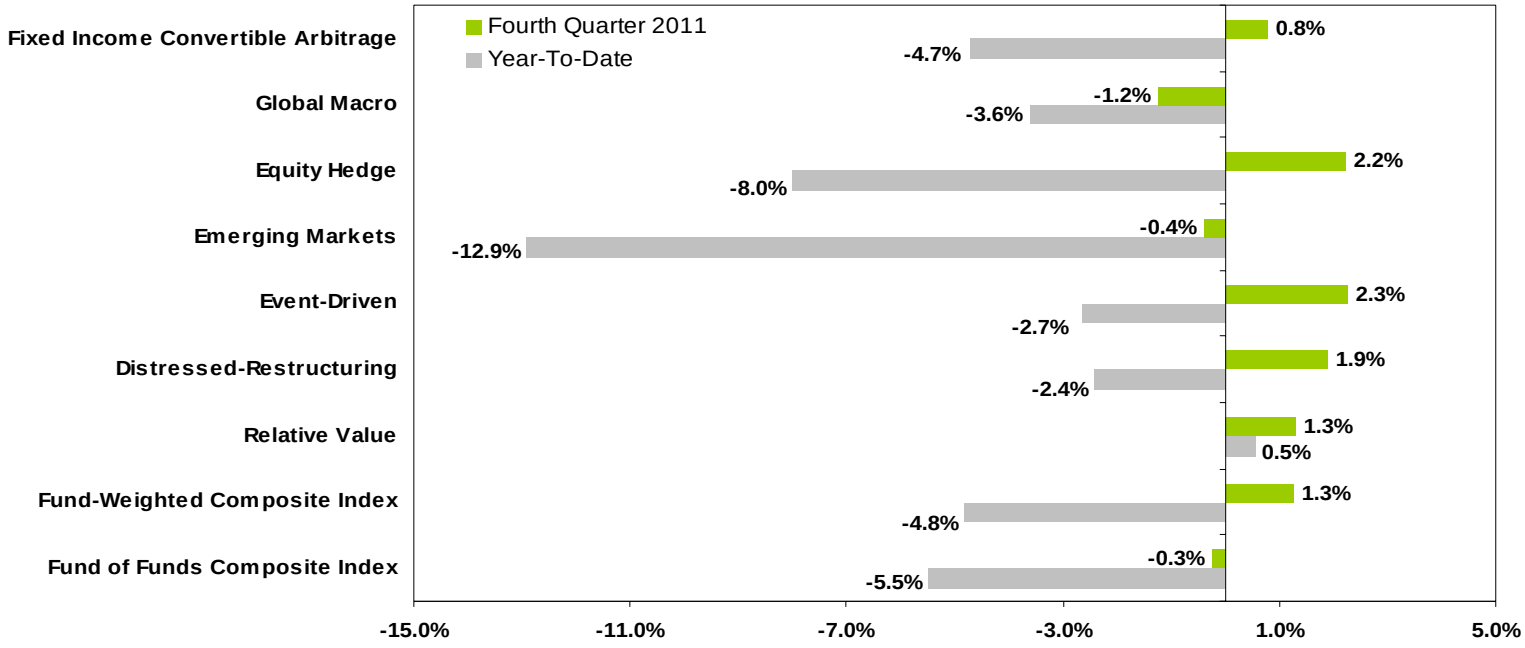
# Hedge Fund Markets Overview

**HEDGE FUND SECTOR PERFORMANCE**
**AS OF 12/31/2011**




- Hedge fund markets rebounded from the previous quarter with the majority of strategies posting positive returns. Favorable results were mostly driven by the market rally that occurred in October. Event-driven and equity hedge strategies experienced the largest gains during the quarter, while global macro managers were the bottom performers.

- 2011 proved to be a challenging year for hedge funds, as on average they declined 4.8% during the year. Hedge funds struggled with political and global economic uncertainty that plagued the markets during the majority of the year, as macro factors mostly dominated fundamentals. Only relative value strategies managed to post gains, returning 0.5% for the year.

# Total Fund

# Highlights

**Executive Summary**

- Performance of the Pension Plan when measured against the Performance Benchmark and Long-Term Target has been strong over short- and long-term time periods.
- Performance relative to peers is also competitive over short- and long-term time periods.
- The Pension Plan is well-diversified across six broad asset classes, and each asset class is also well-diversified.
- Public market asset class investments do not significantly deviate from their broad market based benchmarks, e.g., sectors, market capitalizations, global regions, credit quality, duration, and security types.
- Private market asset classes are well-diversified by either vintage year, geography, property type, sectors, investment vehicle/asset type, or investment strategy.
- Asset allocation is monitored on a daily basis to ensure the actual asset allocation of the plan remains close to the long-term policy targets set forth in the Investment Policy Statement.
- Hewitt EnnisKnupp and SBA staff revisit the plan design annually through informal and formal asset allocation and asset liability reviews.
- Adequate liquidity exists within the asset allocation to pay the monthly obligations of the Pension Plan consistently and on a timely basis.

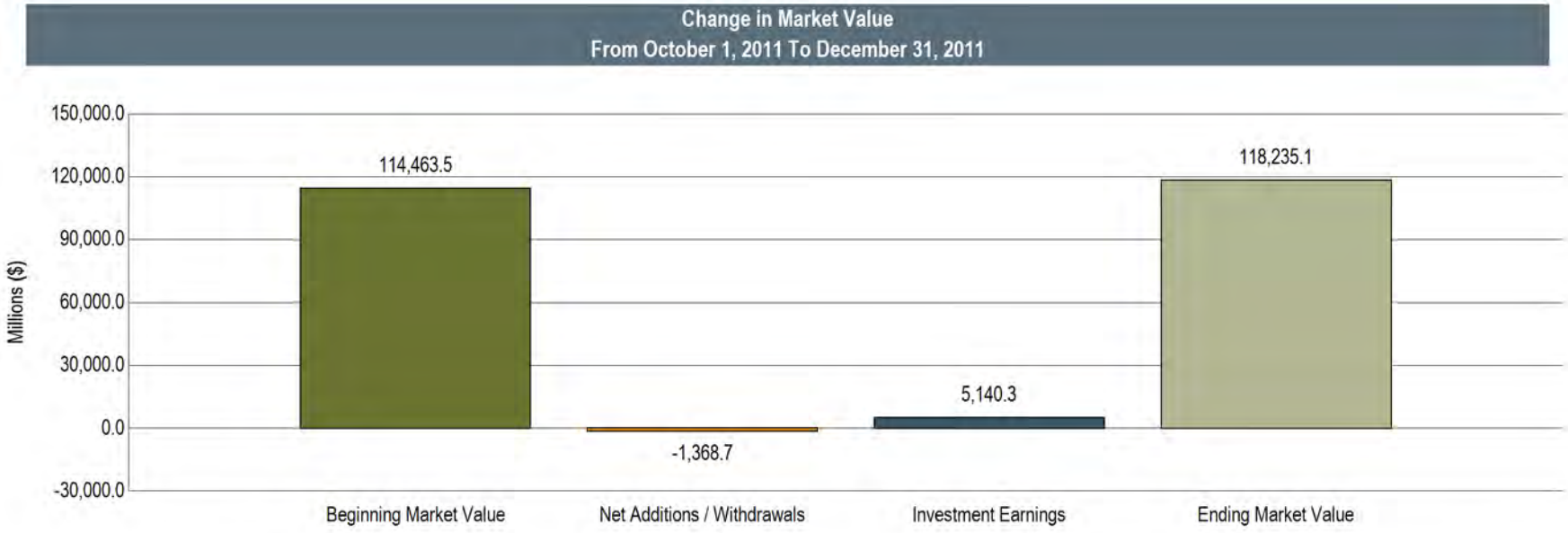
**Performance Highlights**

- Over the trailing one-, three-, five-, and ten-year periods, the Total Fund outperformed the Performance Benchmark. During the fourth quarter, the Fund returned 4.5% and underperformed its Benchmark by 0.97 percentage points.

**Asset Allocation**

- The Fund assets total $118.2 billion as of December 31, 2011, which represents a $3.8 billion increase since last quarter.
- Actual allocations for all asset classes were within their respective policy ranges at quarter-end.
- The Fund was slightly overweight global equity and real estate with corresponding marginal underweight to cash at quarter-end.

# Plan Summary




## Summary of Cash Flows

| Sources of Portfolio Growth | Fourth Quarter | Fiscal YTD* |
|---|---|---|
| Beginning Market Value | $114,463,456,426 | $128,532,863,218 |
| Net Additions/Withdrawals | -$1,368,691,680 | -$3,110,163,007 |
| Investment Earnings | $5,140,325,708 | -$7,187,609,757 |
| Ending Market Value | $118,235,090,454 | $118,235,090,454 |

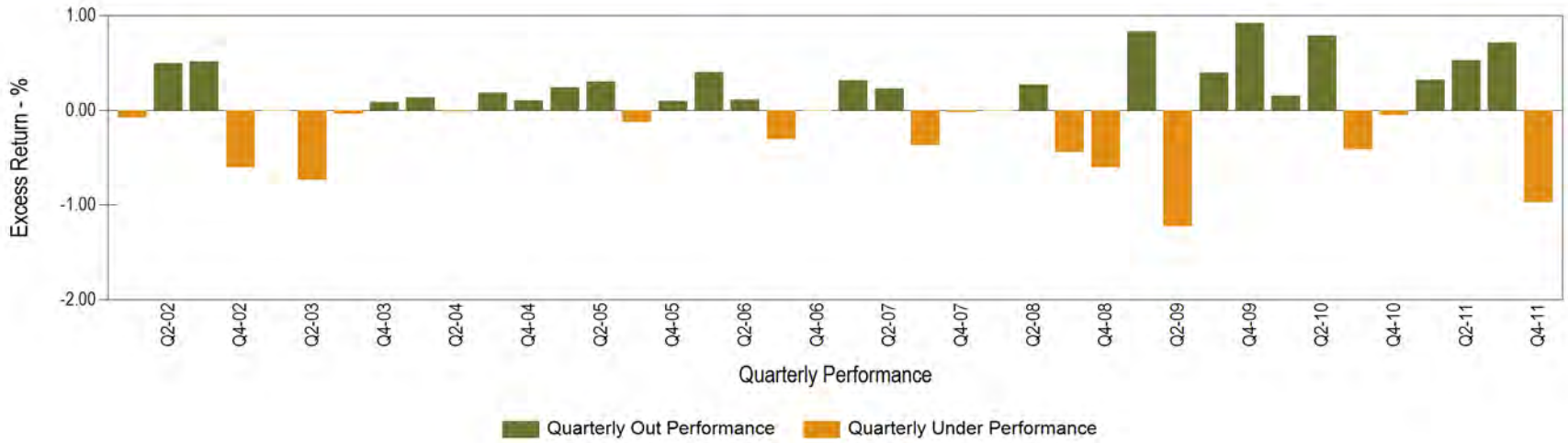
*Period July 2011 - December 2011

# Plan Performance

Benchmark: Performance Benchmark

## Return Summary

## Quarterly Excess Performance



# Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | Policy % | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank | 10 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Total Fund** | **118,235,090,454** | **100.0** | **100.0** | **4.5** | **65** | **-0.5** | **71** | **10.9** | **46** | **1.7** | **45** | **5.2** | **57** |
| *Performance Benchmark* | | | | *5.5* | *38* | *-1.2* | *84* | *10.1* | *65* | *1.4* | *57* | *4.9* | *68* |
| *Absolute Nominal Target Rate of Return* | | | | *0.7* | *99* | *8.1* | *4* | *7.5* | *95* | *7.3* | *1* | *7.1* | *8* |
| **Global Equity** | **67,296,756,644** | **56.9** | **56.8** | **7.5** | **--** | **-6.5** | **--** | **13.2** | **--** | **-1.1** | **--** | **3.9** | **--** |
| *Asset Class Target* | | | | *7.1* | *--* | *-7.9* | *--* | *12.3* | *--* | *-1.7* | *--* | *3.6* | *--* |
| **Domestic Equities** | **30,159,997,320** | **25.5** | **--** | **12.2** | **38** | **1.6** | **21** | **15.3** | **32** | **0.2** | **42** | **3.5** | **54** |
| *Asset Class Target* | | | | *12.1* | *40* | *1.0* | *30* | *14.9* | *46* | *0.0* | *52* | *3.5* | *55* |
| **Foreign Equities** | **33,880,566,859** | **28.7** | **--** | **3.6** | **54** | **-12.9** | **45** | **12.7** | **9** | **-1.5** | **7** | **7.3** | **6** |
| *Asset Class Target* | | | | *3.1* | *85* | *-14.6* | *80* | *11.5* | *22* | *-2.7* | *41* | *6.4* | *34* |
| **Global Equities** | **3,256,190,127** | **2.8** | **--** | **7.6** | **--** | **-5.7** | **--** | **11.4** | **--** | **-2.4** | **--** | **--** | **--** |
| *Benchmark* | | | | *7.4* | *--* | *-6.7* | *--* | *12.4* | *--* | *-1.6* | *--* | *--* | *--* |
| **Fixed Income** | **30,706,179,097** | **26.0** | **26.0** | **1.4** | **64** | **7.6** | **45** | **10.4** | **41** | **6.6** | **41** | **6.1** | **38** |
| *Asset Class Target* | | | | *1.1* | *81* | *7.8* | *38* | *6.8* | *95* | *6.5* | *48* | *5.9* | *46* |
| **Private Equity** | **5,783,192,360** | **4.9** | **4.9** | **-5.0** | **--** | **8.0** | **--** | **4.0** | **--** | **4.7** | **--** | **5.7** | **--** |
| *Asset Class Target* | | | | *13.9* | *--* | *4.0* | *--* | *18.3* | *--* | *4.1* | *--* | *7.9* | *--* |
| *Secondary Target** | | | | *-3.9* | *--* | *14.2* | *--* | *6.3* | *--* | *8.5* | *--* | *11.7* | *--* |
| **Real Estate** | **8,694,348,812** | **7.4** | **7.2** | **3.5** | **1** | **14.5** | **18** | **-2.4** | **46** | **0.8** | **26** | **7.7** | **25** |
| *Asset Class Target* | | | | *3.8* | *1* | *15.3* | *12* | *-4.1* | *52* | *-0.4* | *62* | *3.8* | *74* |
| **Strategic Investments** | **4,879,413,980** | **4.1** | **4.1** | **-1.8** | **--** | **5.5** | **--** | **11.9** | **--** | **--** | **--** | **--** | **--** |
| *Short-Term Target* | | | | *2.4* | *--* | *4.2* | *--* | *9.2* | *--* | *--* | *--* | *--* | *--* |
| **Cash** | **875,199,561** | **0.7** | **1.0** | **0.1** | **--** | **0.3** | **--** | **0.8** | **--** | **0.1** | **--** | **1.3** | **--** |
| *Asset Class Target* | | | | *0.0* | *--* | *0.1* | *--* | *0.3* | *--* | *1.8* | *--* | *2.2* | *--* |

Benchmark and universe descriptions can be found in the Appendix.

* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

# Calendar Year Performance

| Name | 2011 (%) | Rank | 2010 (%) | Rank | 2009 (%) | Rank | 2008 (%) | Rank | 2007 (%) | Rank | 2006 (%) | Rank | 2005 (%) | Rank | 2004 (%) | Rank | 2003 (%) | Rank | 2002 (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Total Fund** | **-0.5** | **71** | **13.5** | **37** | **20.8** | **36** | **-26.7** | **49** | **9.1** | **28** | **14.6** | **33** | **7.8** | **40** | **12.0** | **47** | **23.8** | **40** | **-11.2** | **90** |
| *Performance Benchmark* | *-1.2* | *84* | *12.9* | *52* | *19.5* | *46* | *-26.1* | *47* | *8.9* | *32* | *14.4* | *38* | *7.3* | *62* | *11.5* | *54* | *24.5* | *28* | *-11.6* | *95* |
| *Absolute Nominal Target Rate of Return* | *8.1* | *4* | *6.6* | *98* | *7.9* | *99* | *5.1* | *1* | *8.9* | *33* | *6.6* | *96* | *7.6* | *47* | *7.4* | *96* | *6.1* | *98* | *6.8* | *2* |
| **Global Equity** | **-6.5** | **--** | **16.0** | **--** | **33.7** | **--** | **-39.8** | **--** | **8.6** | **--** | **17.5** | **--** | **8.6** | **--** | **14.4** | **--** | **32.4** | **--** | **-19.8** | **--** |
| *Asset Class Target* | *-7.9* | *--* | *15.1* | *--* | *33.8* | *--* | *-40.4* | *--* | *8.5* | *--* | *18.4* | *--* | *8.7* | *--* | *14.1* | *--* | *33.2* | *--* | *-20.3* | *--* |
| **Domestic Equities** | **1.6** | **21** | **17.2** | **65** | **28.8** | **46** | **-37.4** | **48** | **5.3** | **52** | **14.7** | **61** | **6.3** | **76** | **12.3** | **44** | **30.2** | **72** | **-21.4** | **68** |
| *Asset Class Target* | *1.0* | *30* | *16.9* | *70* | *28.3* | *55* | *-37.3* | *45* | *5.1* | *53* | *15.7* | *40* | *6.1* | *88* | *11.9* | *68* | *31.1* | *68* | *-21.5* | *72* |
| **Foreign Equities** | **-12.9** | **45** | **15.2** | **7** | **42.7** | **9** | **-44.3** | **36** | **16.3** | **35** | **26.4** | **31** | **16.1** | **46** | **21.3** | **29** | **39.8** | **28** | **-12.7** | **30** |
| *Asset Class Target* | *-14.6* | *80* | *13.0* | *41* | *43.7* | *8* | *-46.1* | *78* | *16.4* | *30* | *26.7* | *28* | *16.6* | *39* | *20.9* | *32* | *40.8* | *17* | *-14.7* | *57* |
| **Global Equities** | **-5.7** | **--** | **10.4** | **--** | **32.8** | **--** | **-41.8** | **--** | **10.2** | **--** | **20.0** | **--** | **9.4** | **--** | **15.4** | **--** | **--** | **--** | **--** | **--** |
| *Benchmark* | *-6.7* | *--* | *13.1* | *--* | *34.6* | *--* | *-42.1* | *--* | *11.8* | *--* | *21.1* | *--* | *11.3* | *--* | *16.4* | *--* | *--* | *--* | *--* | *--* |
| **Fixed Income** | **7.6** | **45** | **9.2** | **34** | **14.4** | **46** | **-3.9** | **43** | **6.7** | **29** | **4.7** | **39** | **2.8** | **28** | **5.0** | **51** | **6.0** | **56** | **9.7** | **36** |
| *Asset Class Target* | *7.8* | *38* | *6.5* | *92* | *5.9* | *91* | *5.2* | *9* | *7.2* | *21* | *4.7* | *38* | *2.5* | *45* | *4.7* | *67* | *5.1* | *67* | *9.7* | *36* |
| **Private Equity** | **8.0** | **--** | **18.6** | **--** | **-12.1** | **--** | **-4.3** | **--** | **16.5** | **--** | **12.2** | **--** | **12.9** | **--** | **0.6** | **--** | **10.3** | **--** | **-1.4** | **--** |
| *Asset Class Target* | *4.0* | *--* | *19.9* | *--* | *32.8* | *--* | *-32.8* | *--* | *9.6* | *--* | *20.2* | *--* | *10.6* | *--* | *16.5* | *--* | *33.8* | *--* | *-15.4* | *--* |
| *Secondary Target** | *14.2* | *--* | *16.7* | *--* | *-9.9* | *--* | *-3.9* | *--* | *30.2* | *--* | *21.8* | *--* | *35.5* | *--* | *20.1* | *--* | *11.0* | *--* | *-8.2* | *--* |
| **Real Estate** | **14.5** | **18** | **5.1** | **70** | **-22.8** | **30** | **-1.5** | **28** | **13.6** | **43** | **22.5** | **6** | **17.2** | **85** | **17.4** | **22** | **12.2** | **28** | **6.3** | **17** |
| *Asset Class Target* | *15.3* | *12* | *8.8* | *61* | *-29.7* | *63* | *-1.1* | *23* | *12.1* | *68* | *6.5* | *95* | *8.8* | *99* | *7.8* | *99* | *11.6* | *31* | *7.0* | *15* |
| **Strategic Investments** | **5.5** | **--** | **8.9** | **--** | **22.0** | **--** | **-37.4** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** | **--** |
| *Short-Term Target* | *4.2* | *--* | *3.5* | *--* | *20.8* | *--* | *-33.6* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* |
| **Cash** | **0.3** | **--** | **0.4** | **--** | **1.7** | **--** | **-5.8** | **--** | **4.1** | **--** | **5.1** | **--** | **3.4** | **--** | **1.4** | **--** | **1.2** | **--** | **2.1** | **--** |
| *Asset Class Target* | *0.1* | *--* | *0.2* | *--* | *0.7* | *--* | *3.0* | *--* | *5.4* | *--* | *5.1* | *--* | *3.4* | *--* | *1.4* | *--* | *1.1* | *--* | *1.7* | *--* |

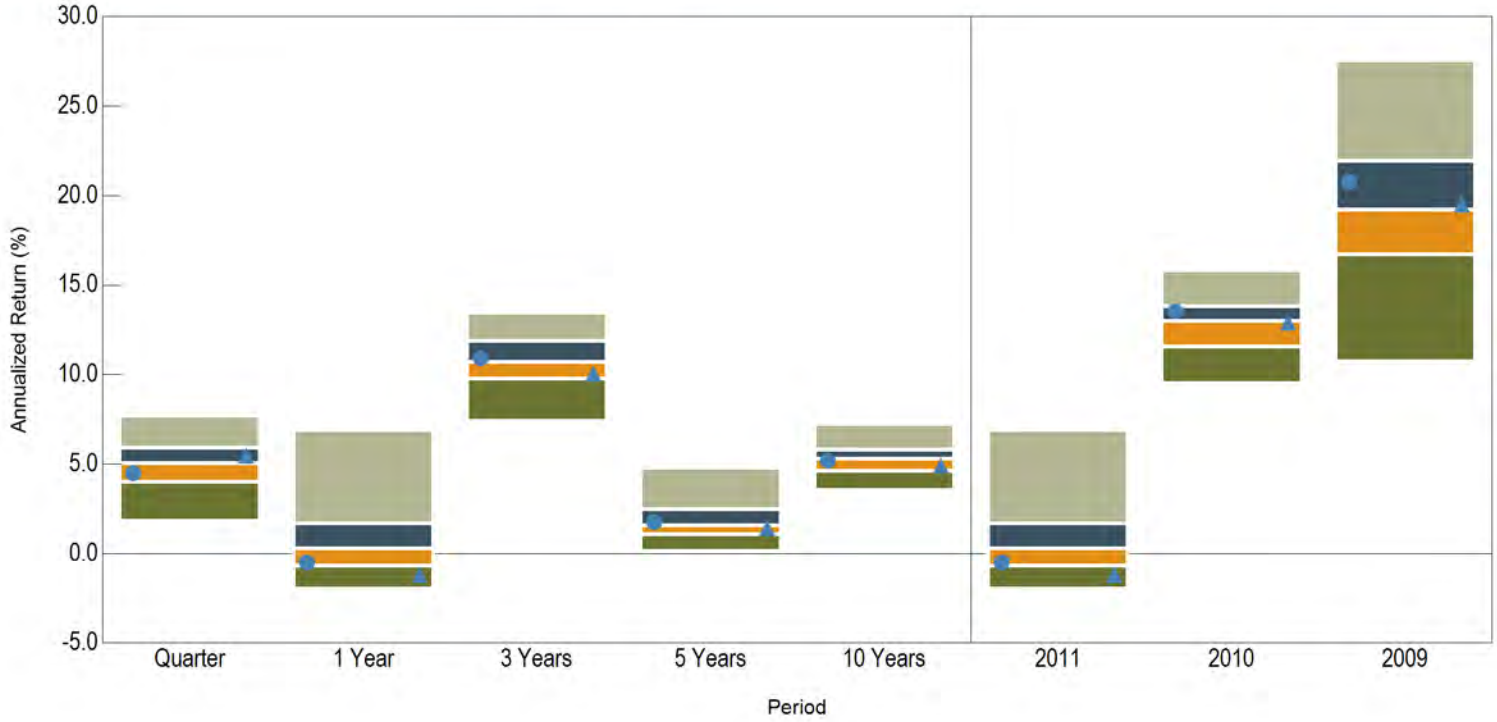
* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

# Universe Comparison

Benchmark: Performance Benchmark

Universe: Public Funds >$1B Net

## Ending December 31, 2011



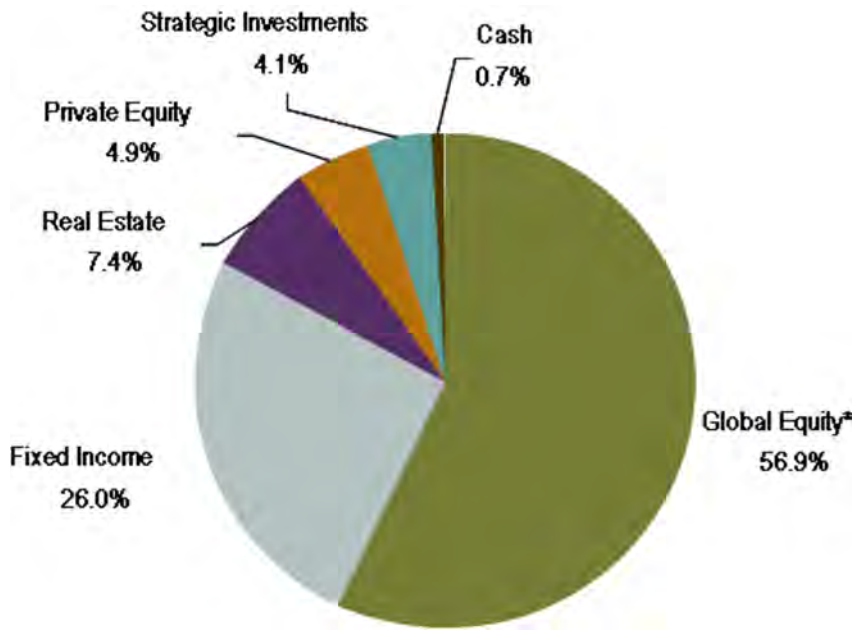

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5th Percentile | 7.7 | | 6.9 | | 13.5 | | 4.8 | | 7.2 | | 6.9 | | 15.8 | | 27.6 | |
| 25th Percentile | 5.9 | | 1.7 | | 11.9 | | 2.5 | | 5.8 | | 1.7 | | 13.8 | | 22.0 | |
| Median | 5.1 | | 0.3 | | 10.7 | | 1.6 | | 5.3 | | 0.3 | | 13.0 | | 19.2 | |
| 75th Percentile | 4.0 | | -0.7 | | 9.8 | | 1.1 | | 4.6 | | -0.7 | | 11.6 | | 16.7 | |
| 95th Percentile | 1.9 | | -2.0 | | 7.4 | | 0.2 | | 3.6 | | -2.0 | | 9.6 | | 10.8 | |
| # of Portfolios | 74 | | 72 | | 66 | | 64 | | 54 | | 72 | | 67 | | 67 | |
| ● Total Fund | 4.5 | (65) | -0.5 | (71) | 10.9 | (46) | 1.7 | (45) | 5.2 | (57) | -0.5 | (71) | 13.5 | (37) | 20.8 | (36) |
| ▲ Performance Benchmark | 5.5 | (38) | -1.2 | (84) | 10.1 | (65) | 1.4 | (57) | 4.9 | (68) | -1.2 | (84) | 12.9 | (52) | 19.5 | (46) |

# Universe Asset Allocation Comparison

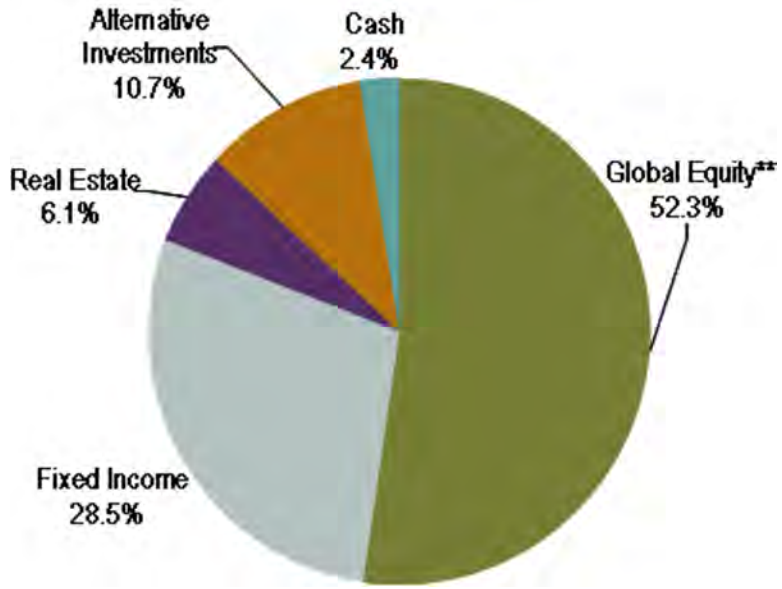
Benchmark: Performance Benchmark

Universe: Public Funds >$1B Net

**Total Fund**




**BNY Mellon Public Funds >$1B Net Universe**




*Global Equity Allocation: 25.5% Domestic Equities; 28.7% Foreign Equities; 2.8% Global Equities. Percentages are of the Total FRS Fund.

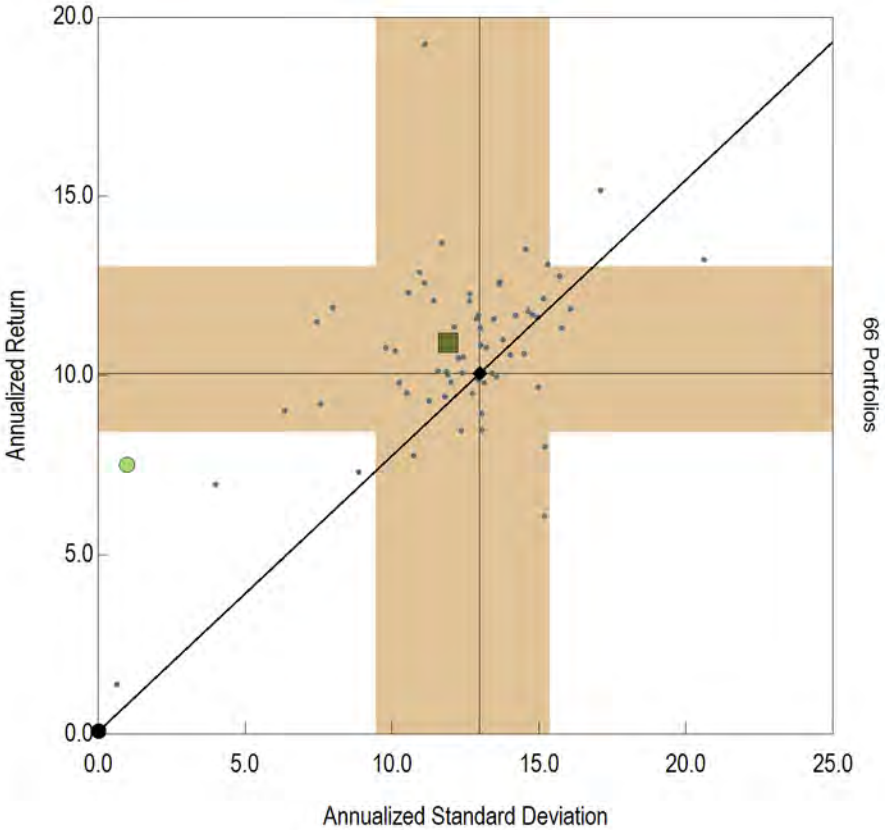
**Global Equity Allocation: 36.2% Domestic Equities; 16.1% Foreign Equities.

# Risk Profile

Benchmark: Performance Benchmark

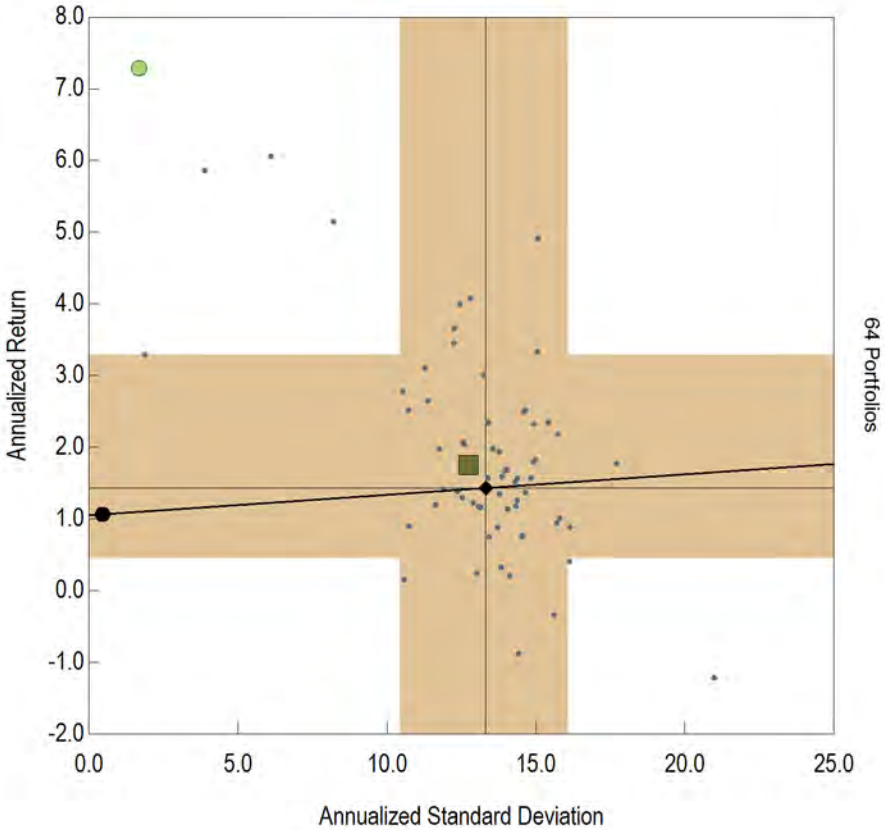
Universe: Public Funds >$1B Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011



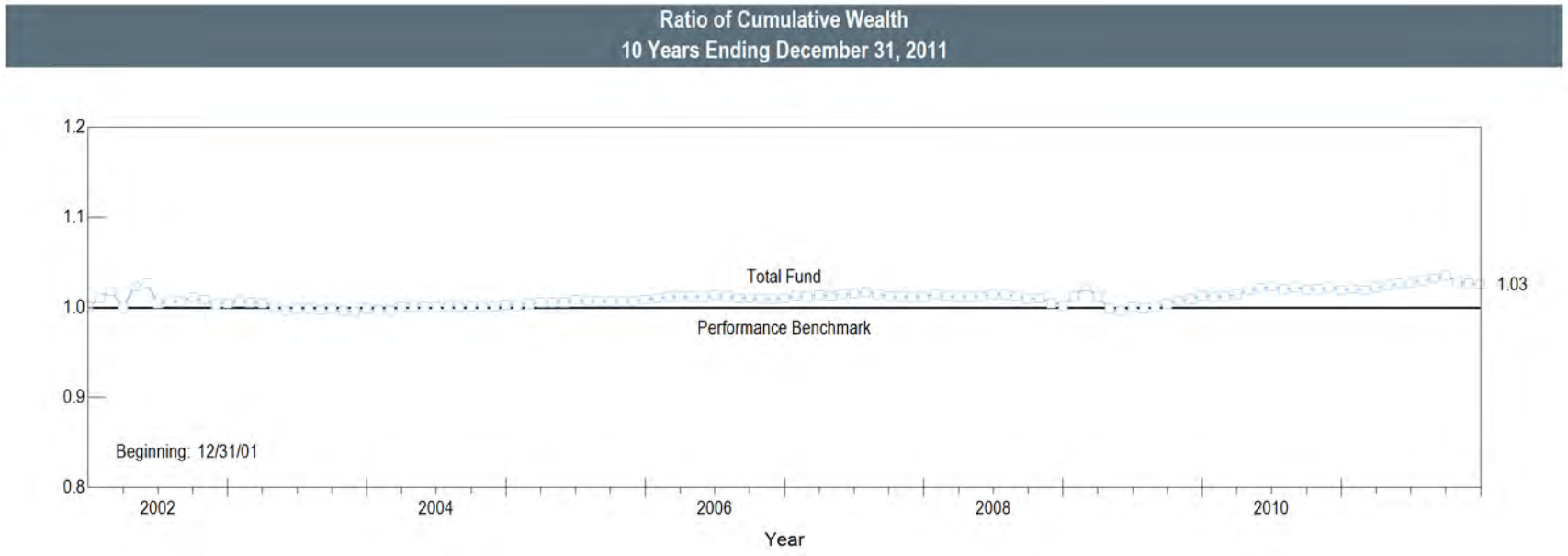

- Total Fund
- Performance Benchmark
- Absolute Nominal Target Rate of Return
- Risk Free
- 68% Confidence Interval
- Public Funds >$1B Net

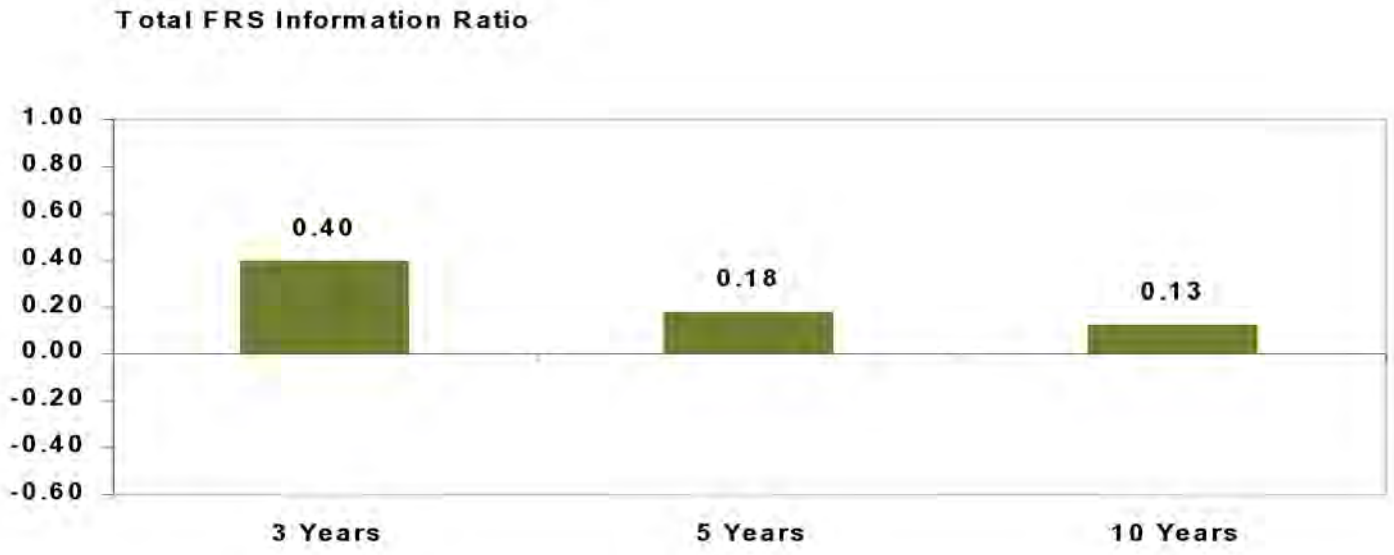
## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011



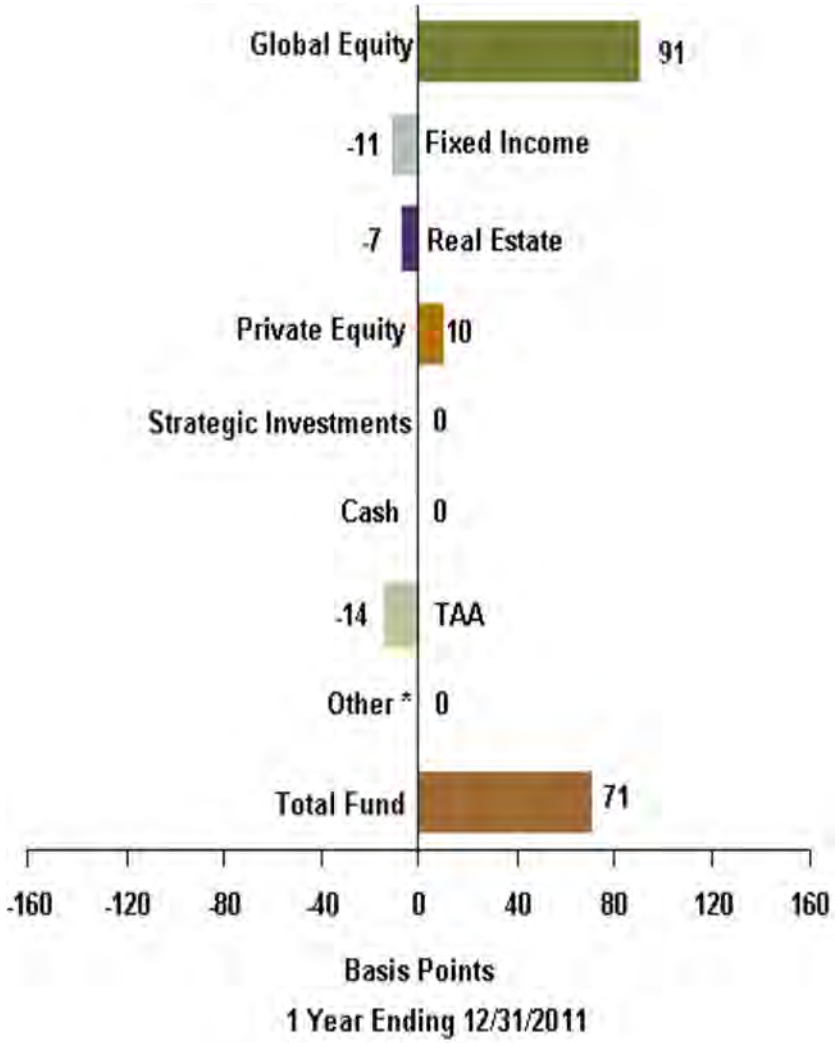

- Total Fund
- Performance Benchmark
- Absolute Nominal Target Rate of Return
- Risk Free
- 68% Confidence Interval
- Public Funds >$1B Net

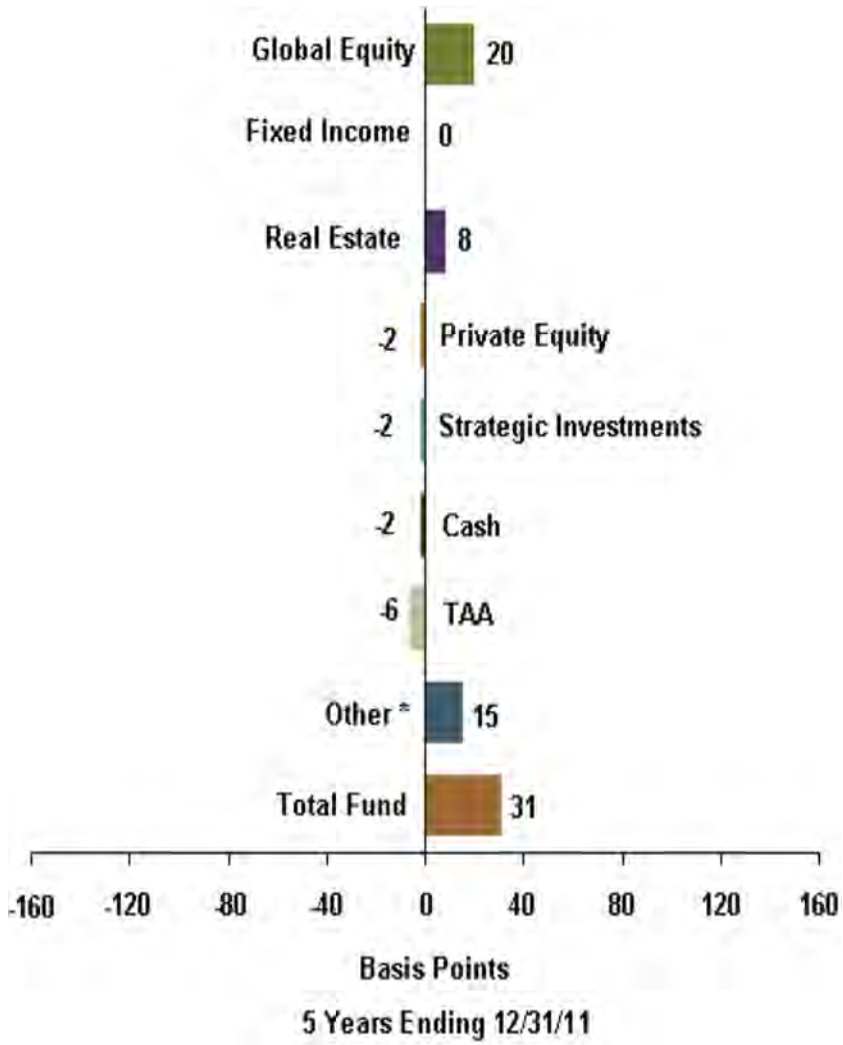
# Attribution



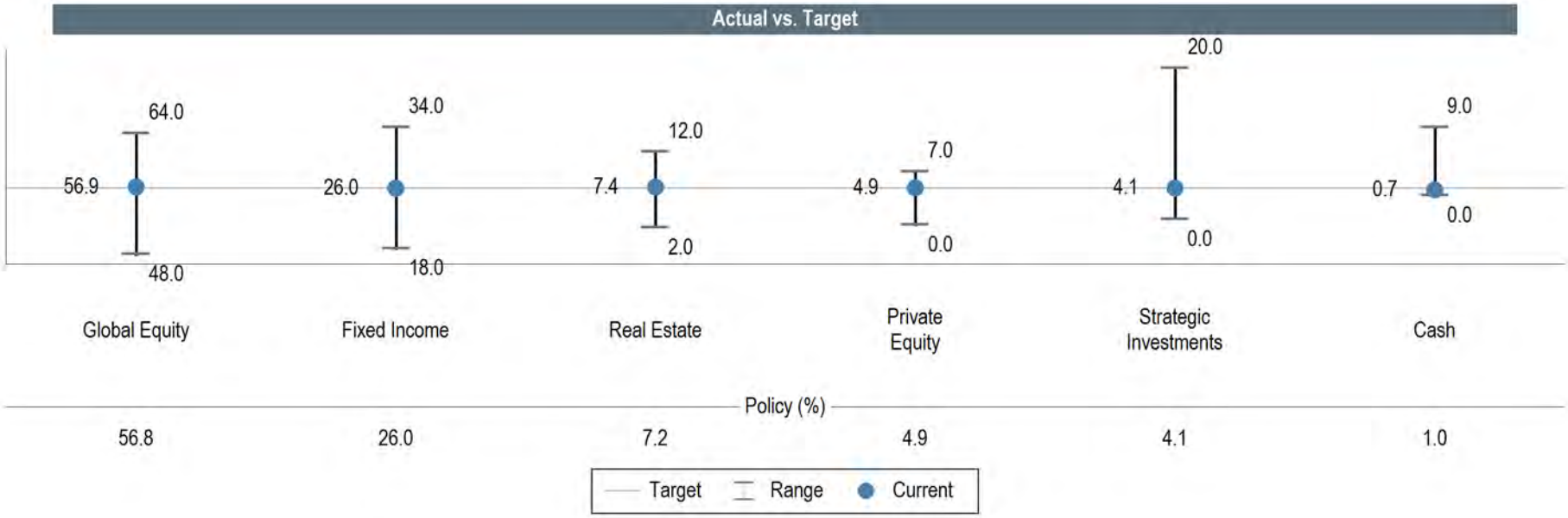
# Attribution

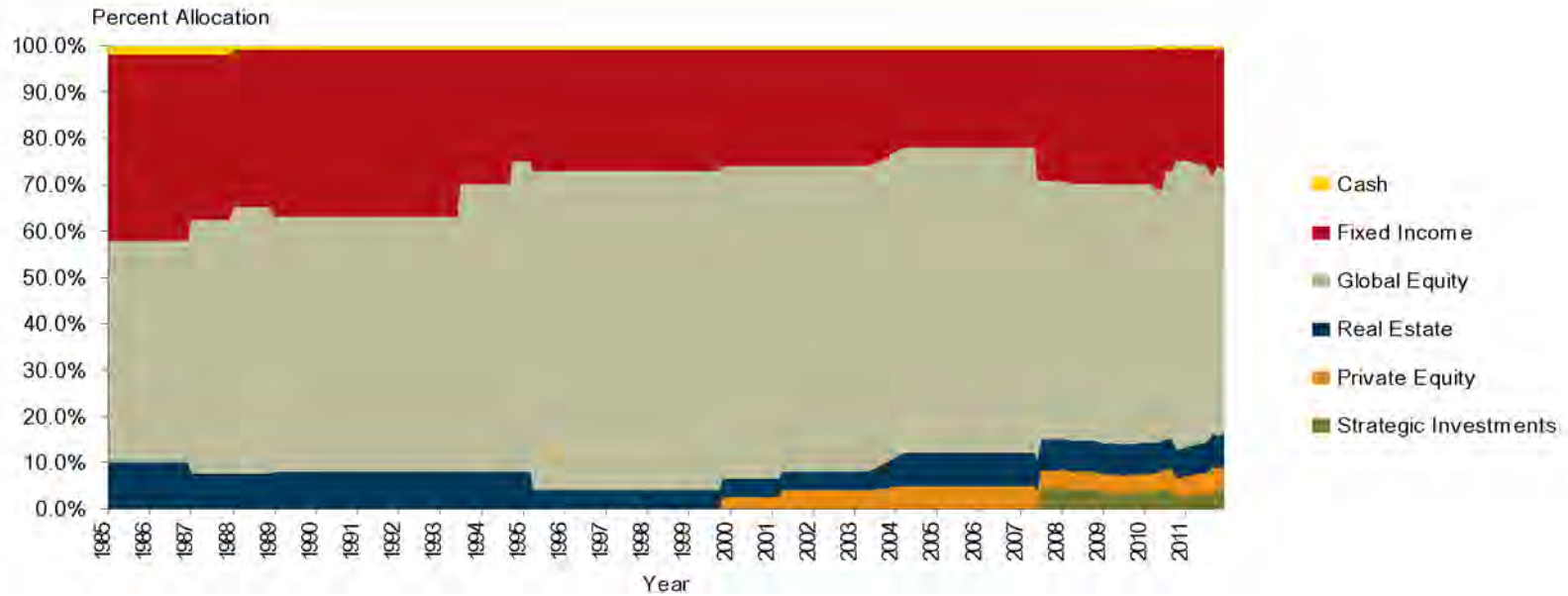



*Other includes legacy accounts, securities lending, and unexplained differences due to methodology.

# Asset Allocation



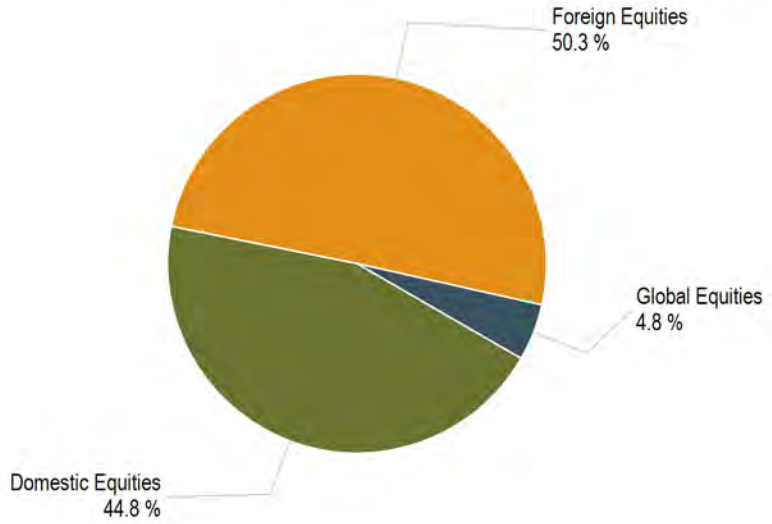



# Global Equity

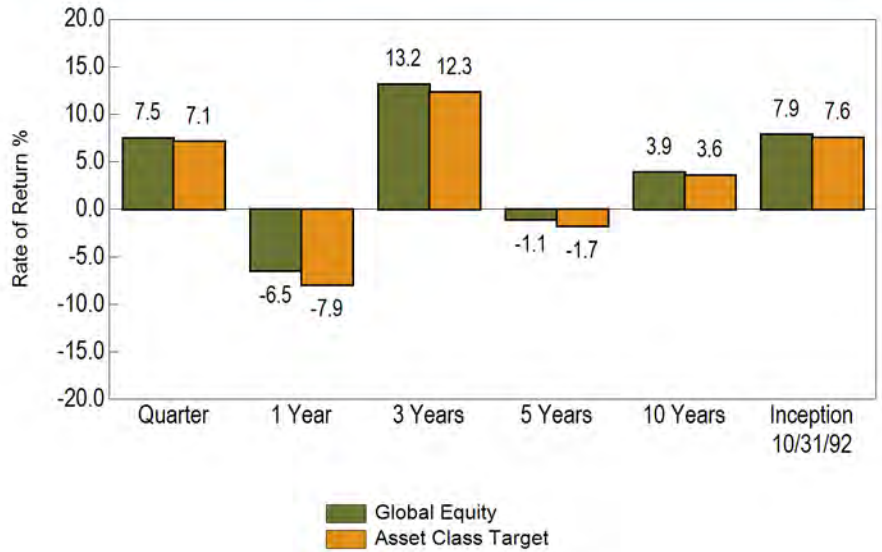
# Overview

Benchmark: Asset Class Target

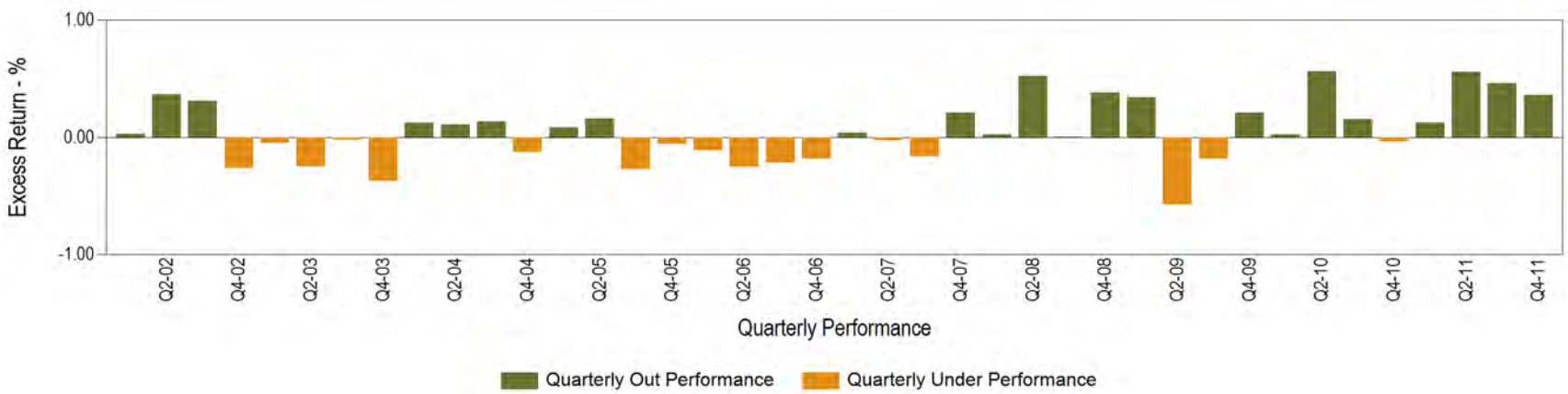
## Allocation




## Return Summary




## Quarterly Excess Performance



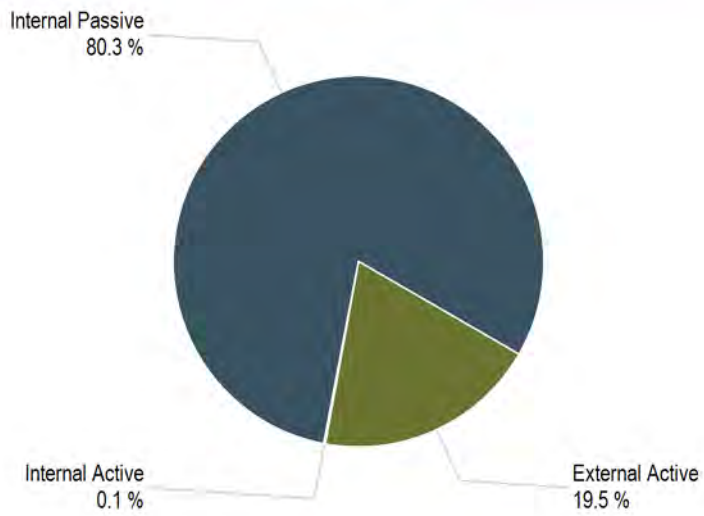

Global Equity became an asset class in July 2010. The historical return series prior to July 2010 was derived from the underlying Domestic Equities, Foreign Equities, and Global Equities components.

# Domestic Equities

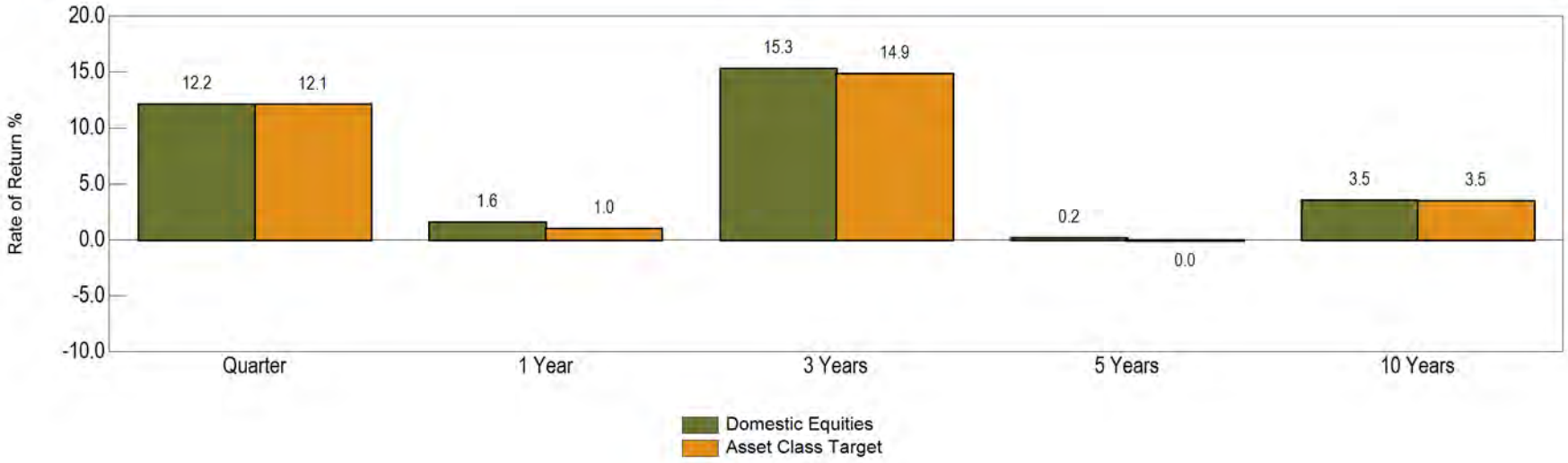
# Overview

Benchmark: Asset Class Target

## Current Allocation

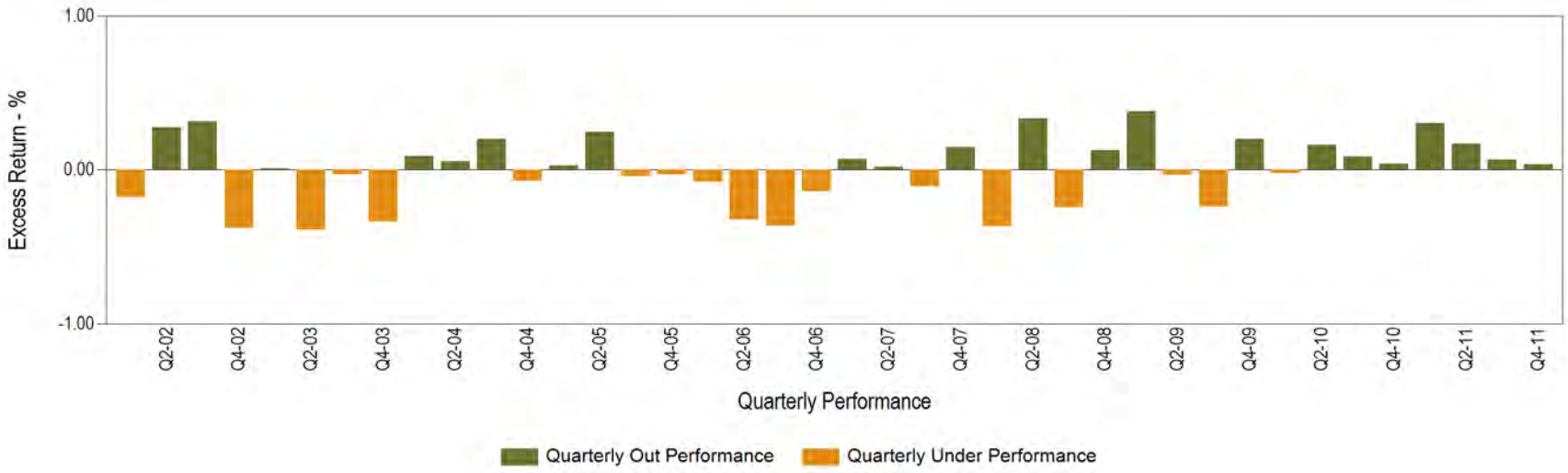



## Return Summary

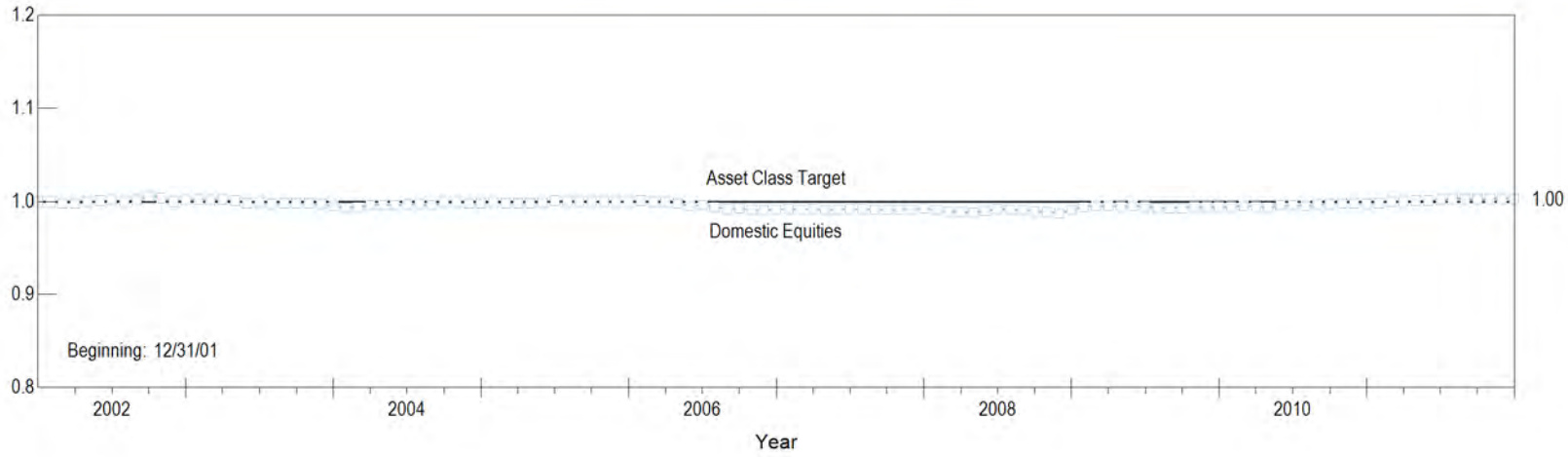


# Overview

## Quarterly Excess Performance




## Ratio of Cumulative Wealth
## 10 Years Ending December 31, 2011

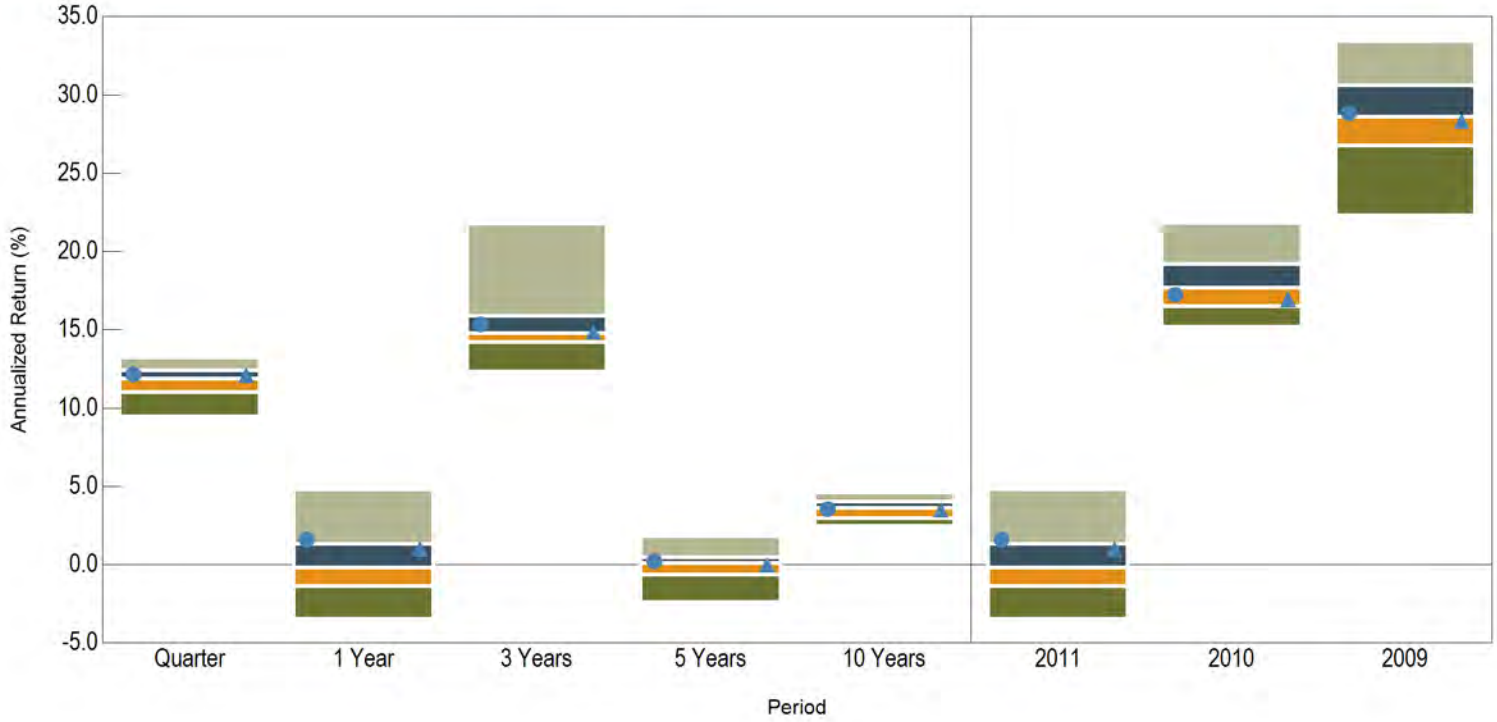


# Universe Comparison

Benchmark: Asset Class Target

Universe: Public Funds >$1B - US Eq Net

## Ending December 31, 2011



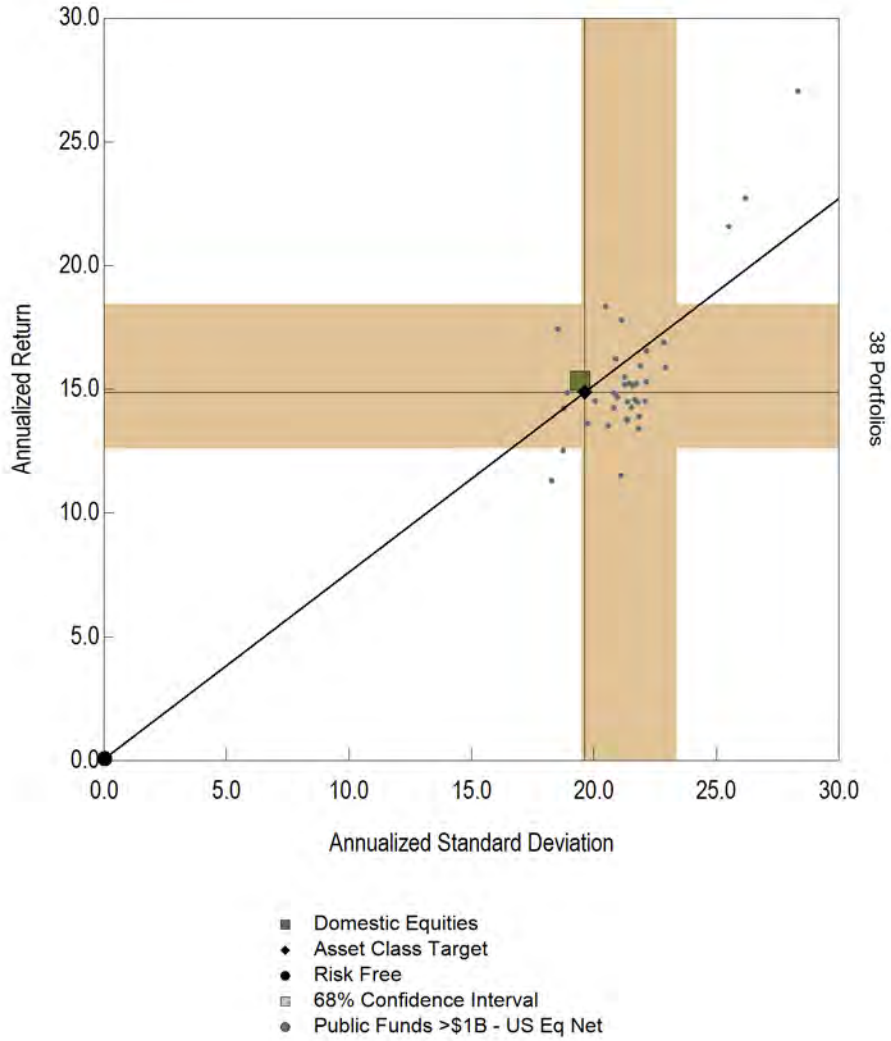

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **5th Percentile** | 13.2 | | 4.8 | | 21.8 | | 1.8 | | 4.6 | | 4.8 | | 21.8 | | 33.4 | |
| **25th Percentile** | 12.4 | | 1.4 | | 15.9 | | 0.5 | | 4.1 | | 1.4 | | 19.2 | | 30.6 | |
| **Median** | 11.9 | | -0.2 | | 14.8 | | 0.1 | | 3.6 | | -0.2 | | 17.7 | | 28.7 | |
| **75th Percentile** | 11.0 | | -1.3 | | 14.2 | | -0.6 | | 3.0 | | -1.3 | | 16.5 | | 26.8 | |
| **95th Percentile** | 9.5 | | -3.4 | | 12.4 | | -2.4 | | 2.5 | | -3.4 | | 15.2 | | 22.3 | |
| **# of Portfolios** | 54 | | 51 | | 38 | | 29 | | 17 | | 51 | | 46 | | 40 | |
| ● **Domestic Equities** | 12.2 | (38) | 1.6 | (21) | 15.3 | (32) | 0.2 | (42) | 3.5 | (54) | 1.6 | (21) | 17.2 | (65) | 28.8 | (46) |
| ▲ **Asset Class Target** | 12.1 | (40) | 1.0 | (30) | 14.9 | (46) | 0.0 | (52) | 3.5 | (55) | 1.0 | (30) | 16.9 | (70) | 28.3 | (55) |

# Risk Profile

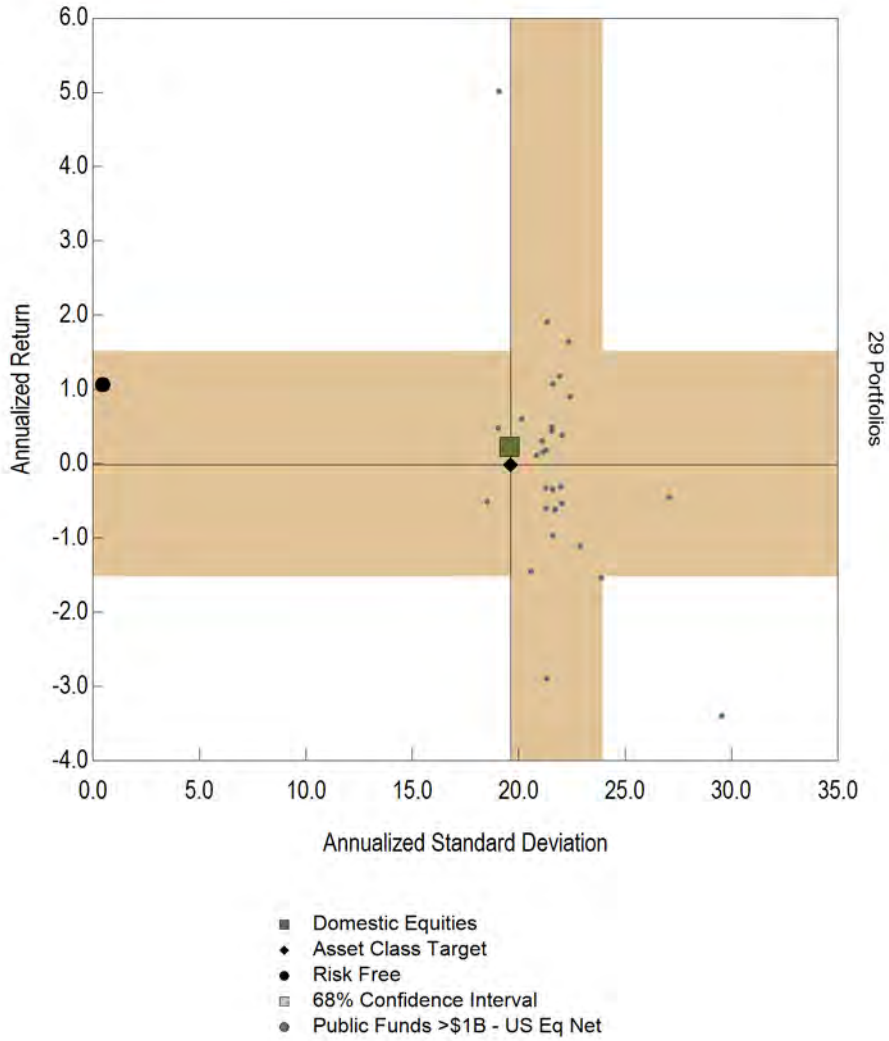
Benchmark: Asset Class Target

Universe: Public Funds >$1B - US Eq Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011



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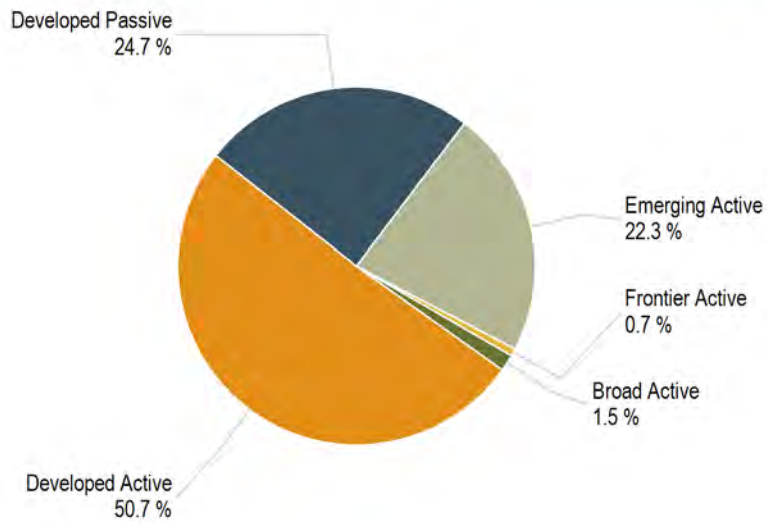
# Foreign Equities

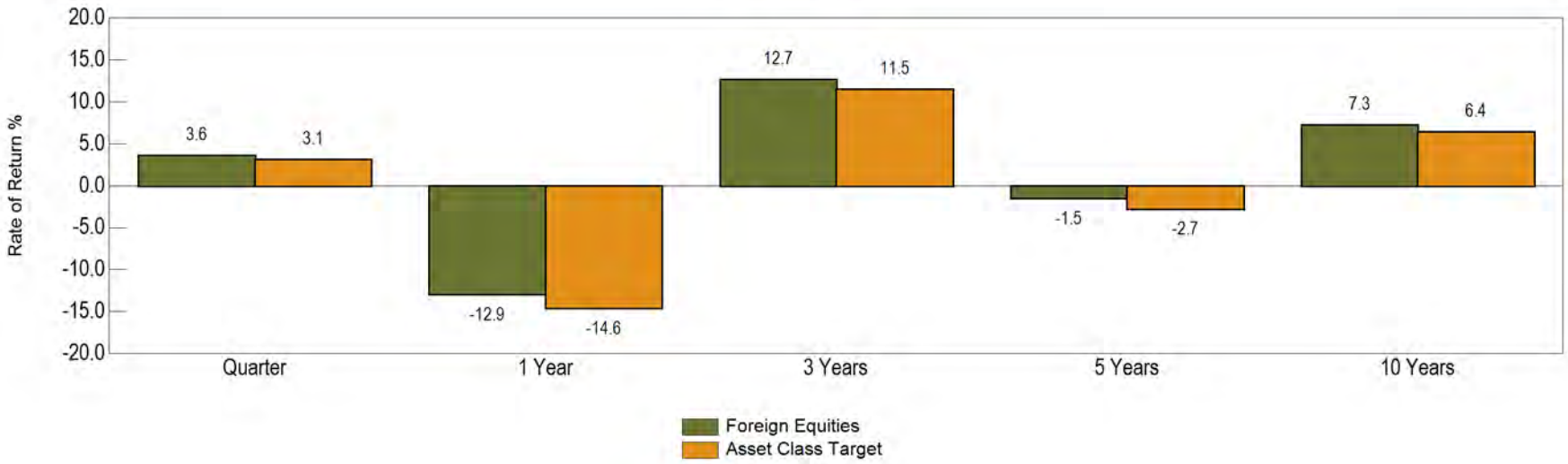
# Overview

Benchmark: Asset Class Target

## Current Allocation



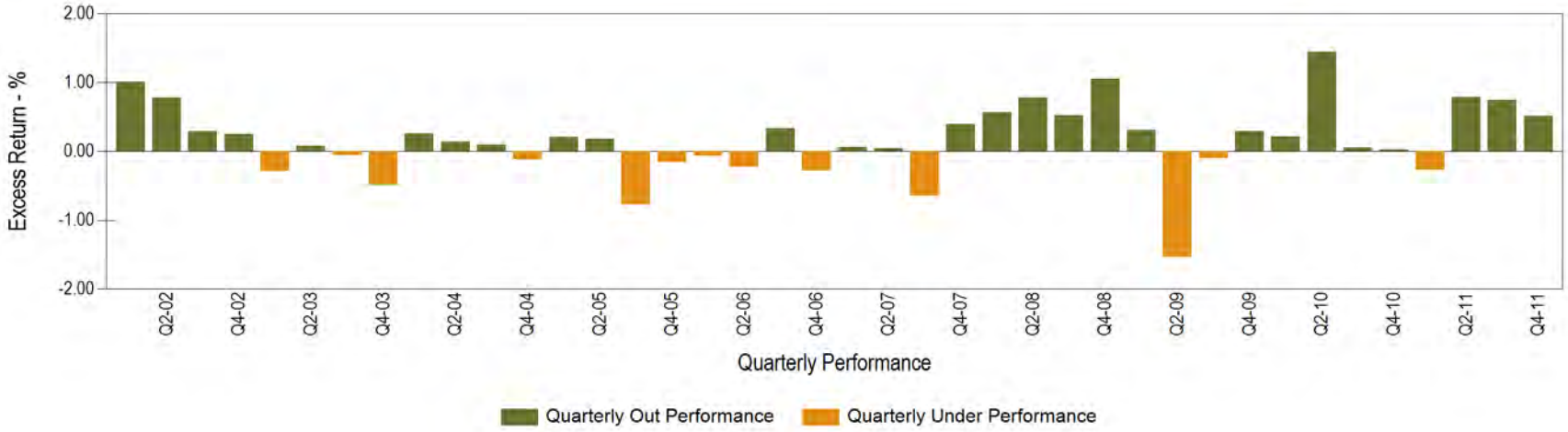

## Return Summary



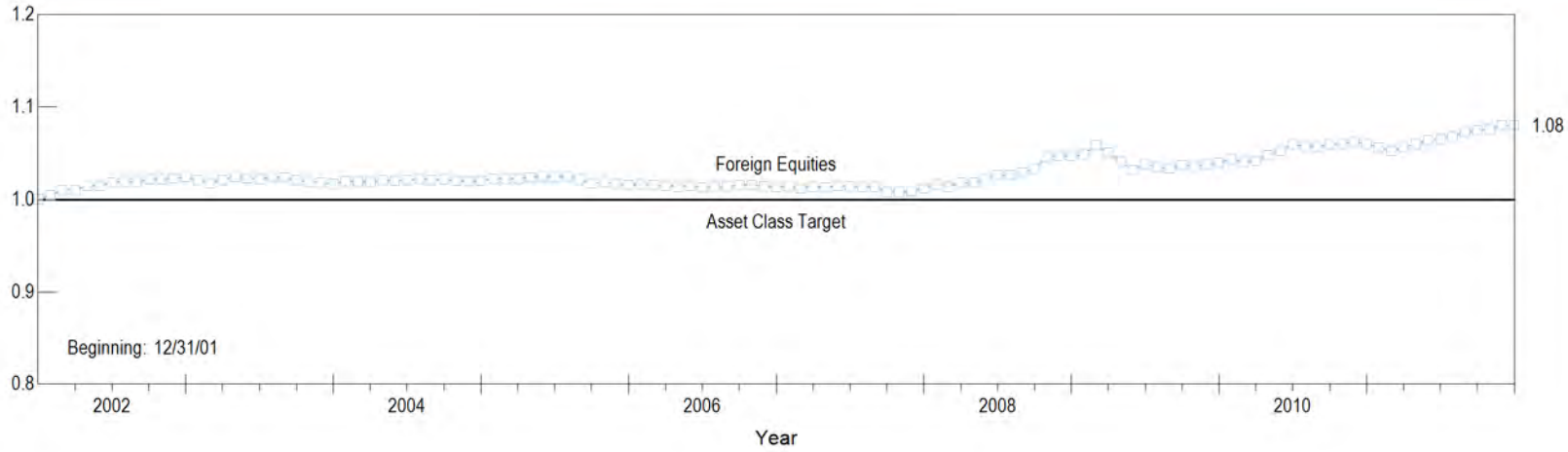
# Overview

Benchmark: Asset Class Target

## Quarterly Excess Performance




## Ratio of Cumulative Wealth
## 10 Years Ending December 31, 2011

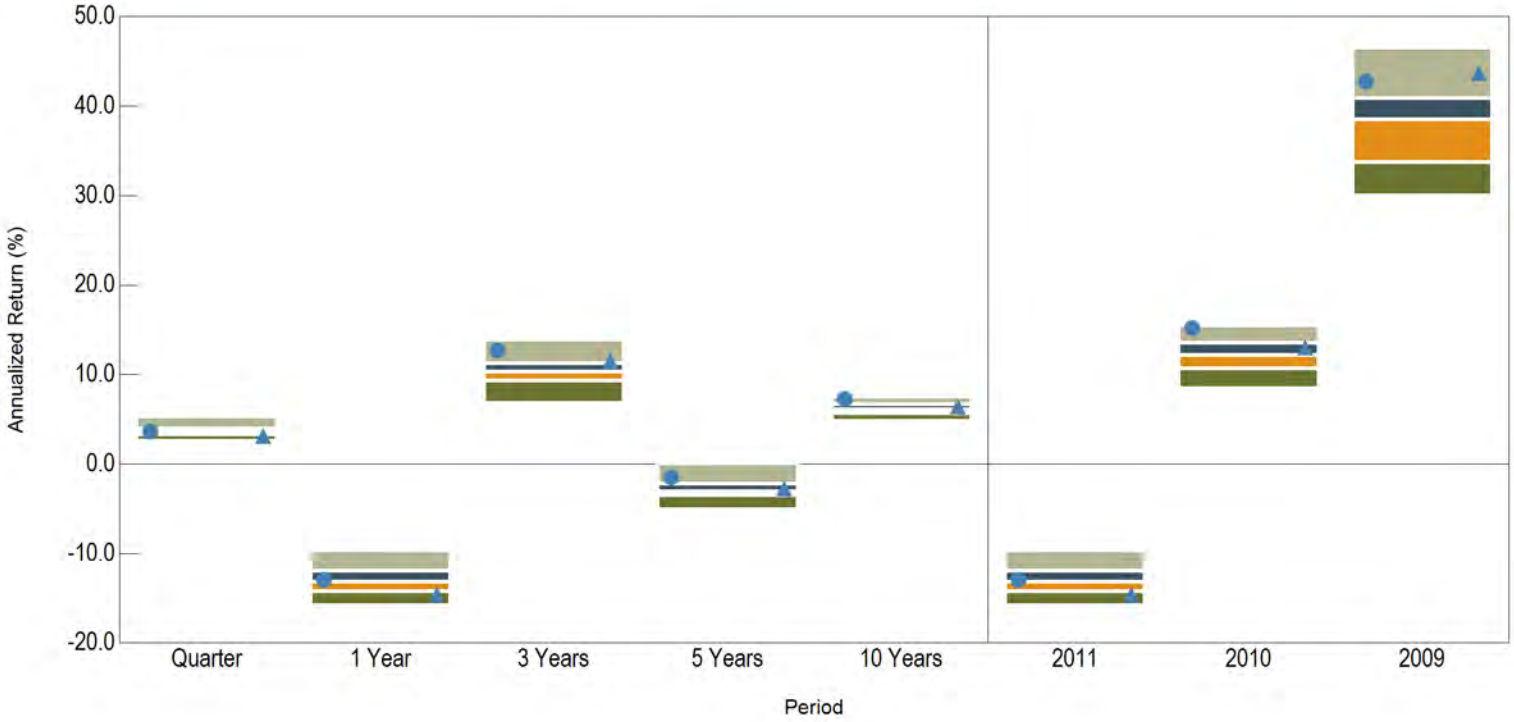


# Universe Comparison

Benchmark: Asset Class Target

Universe: Public Funds >$1B - Non-US Eq Net

## Ending December 31, 2011



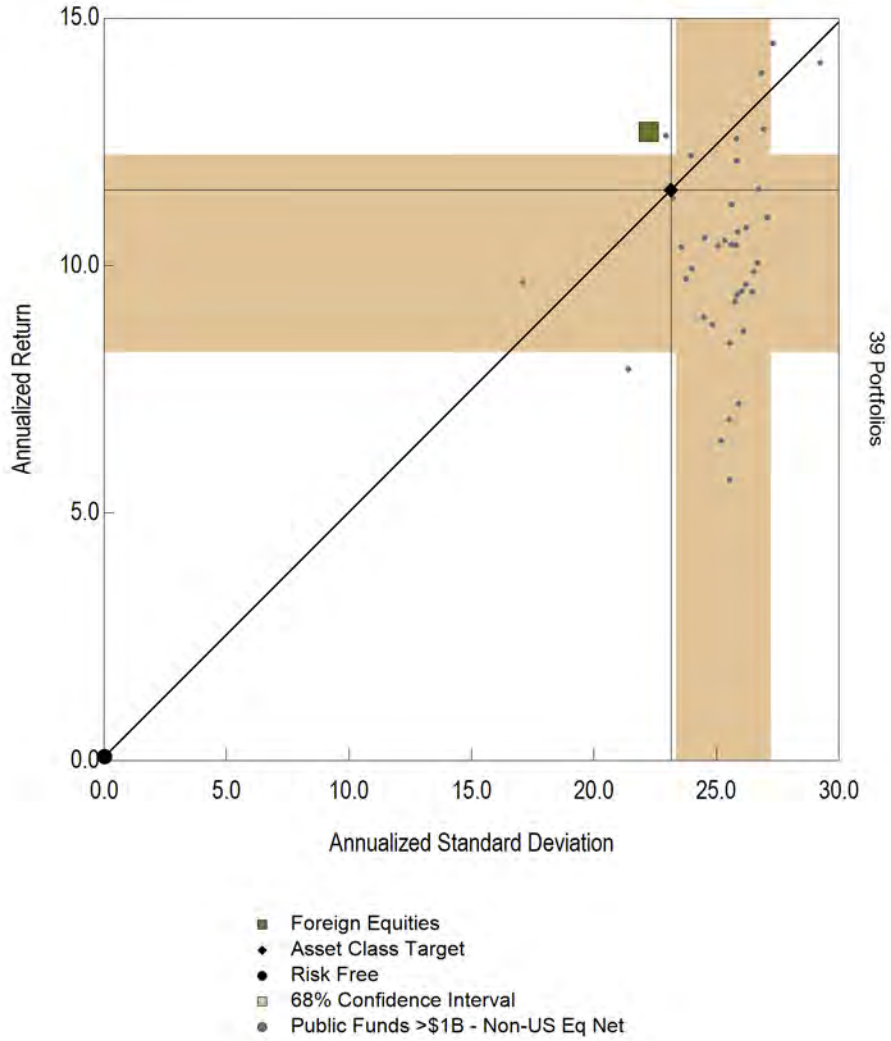

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5th Percentile | 5.3 | | -9.7 | | 13.9 | | 0.1 | | 7.5 | | -9.7 | | 15.5 | | 46.5 | |
| 25th Percentile | 4.0 | | -11.9 | | 11.3 | | -2.2 | | 6.7 | | -11.9 | | 13.6 | | 40.9 | |
| Median | 3.7 | | -13.1 | | 10.4 | | -3.0 | | 6.2 | | -13.1 | | 12.2 | | 38.6 | |
| 75th Percentile | 3.3 | | -14.2 | | 9.3 | | -3.5 | | 5.7 | | -14.2 | | 10.7 | | 33.7 | |
| 95th Percentile | 2.7 | | -15.8 | | 6.8 | | -5.0 | | 4.8 | | -15.8 | | 8.5 | | 30.0 | |
| # of Portfolios | 48 | | 45 | | 39 | | 31 | | 18 | | 45 | | 40 | | 38 | |
| ● Foreign Equities | 3.6 | (54) | -12.9 | (45) | 12.7 | (9) | -1.5 | (7) | 7.3 | (6) | -12.9 | (45) | 15.2 | (7) | 42.7 | (9) |
| ▲ Asset Class Target | 3.1 | (85) | -14.6 | (80) | 11.5 | (22) | -2.7 | (41) | 6.4 | (34) | -14.6 | (80) | 13.0 | (41) | 43.7 | (8) |

# Risk Profile

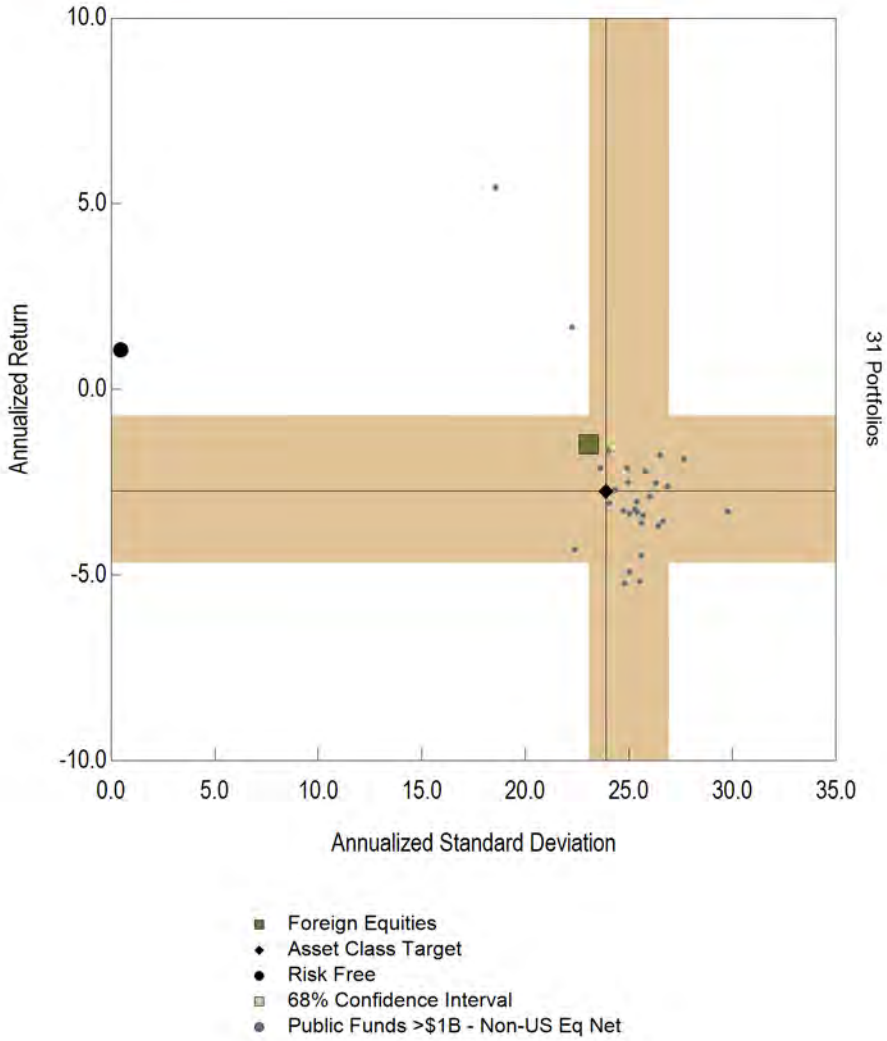
Benchmark: Asset Class Target

Universe: Public Funds >$1B - Non-US Eq Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011



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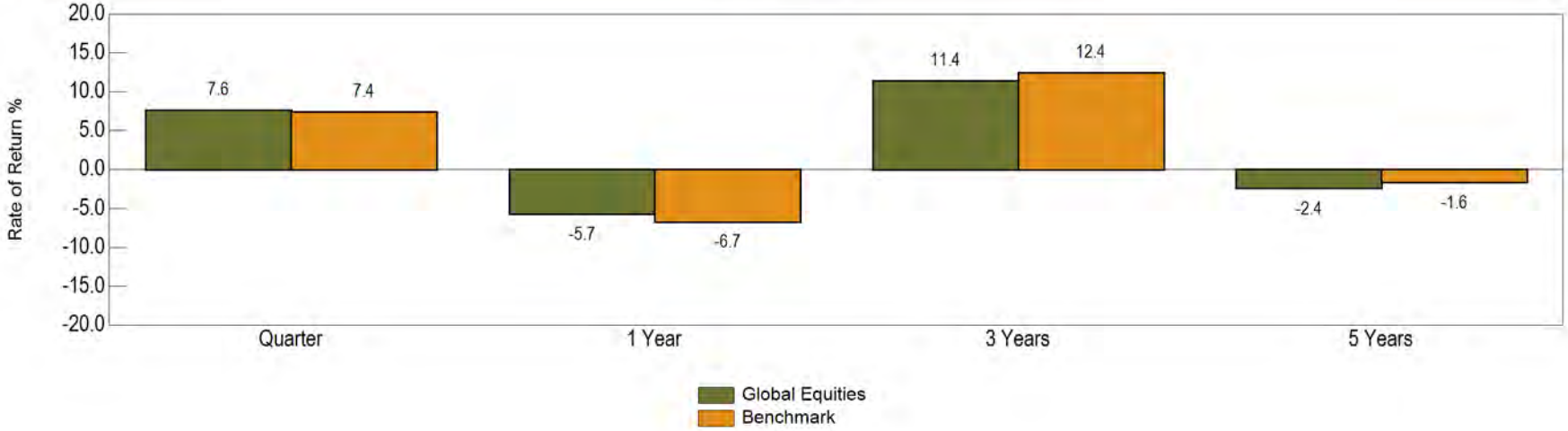
# Global Equities

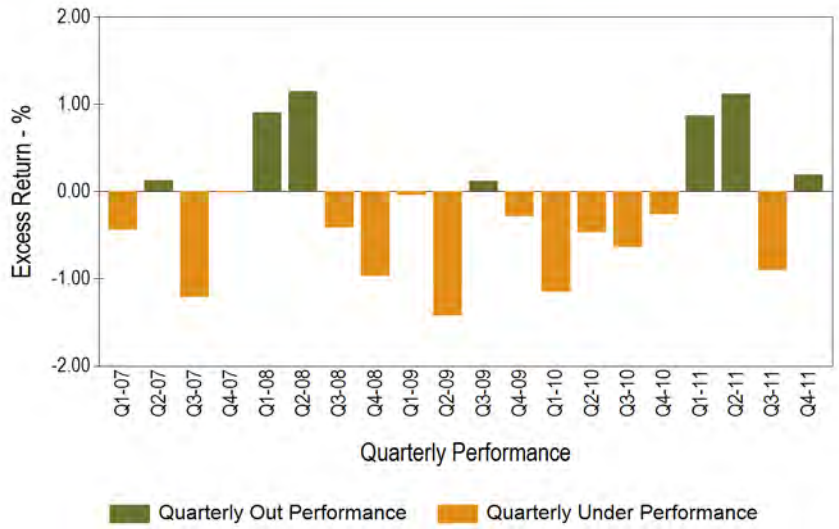
# Overview

Benchmark: Aggregate Benchmark

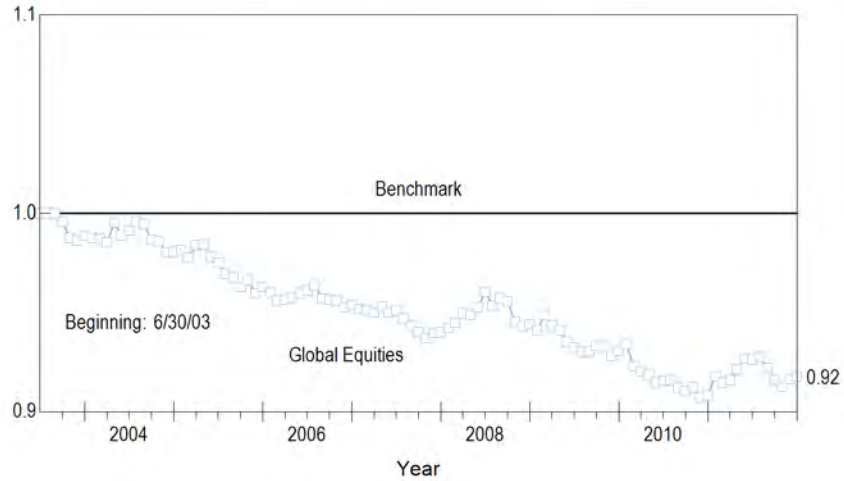
## Return Summary




## Quarterly Excess Performance

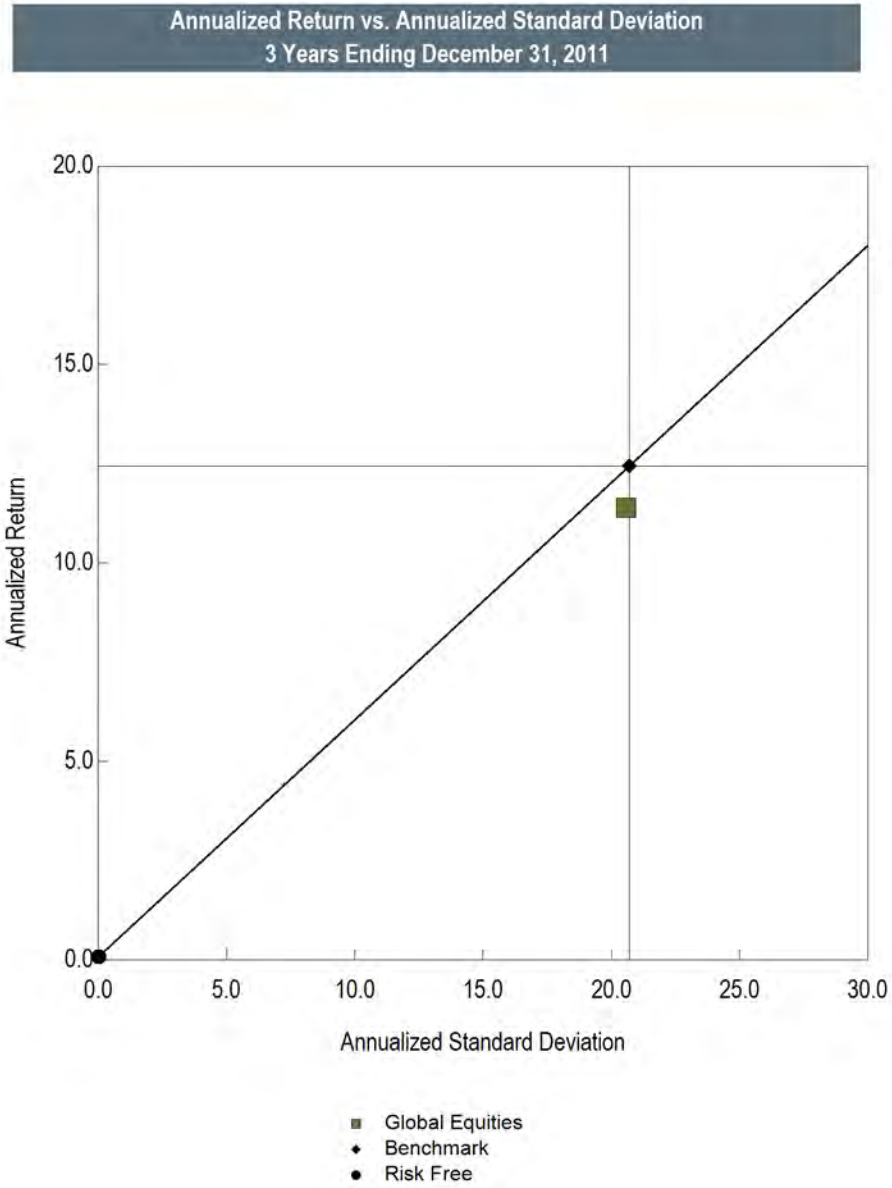


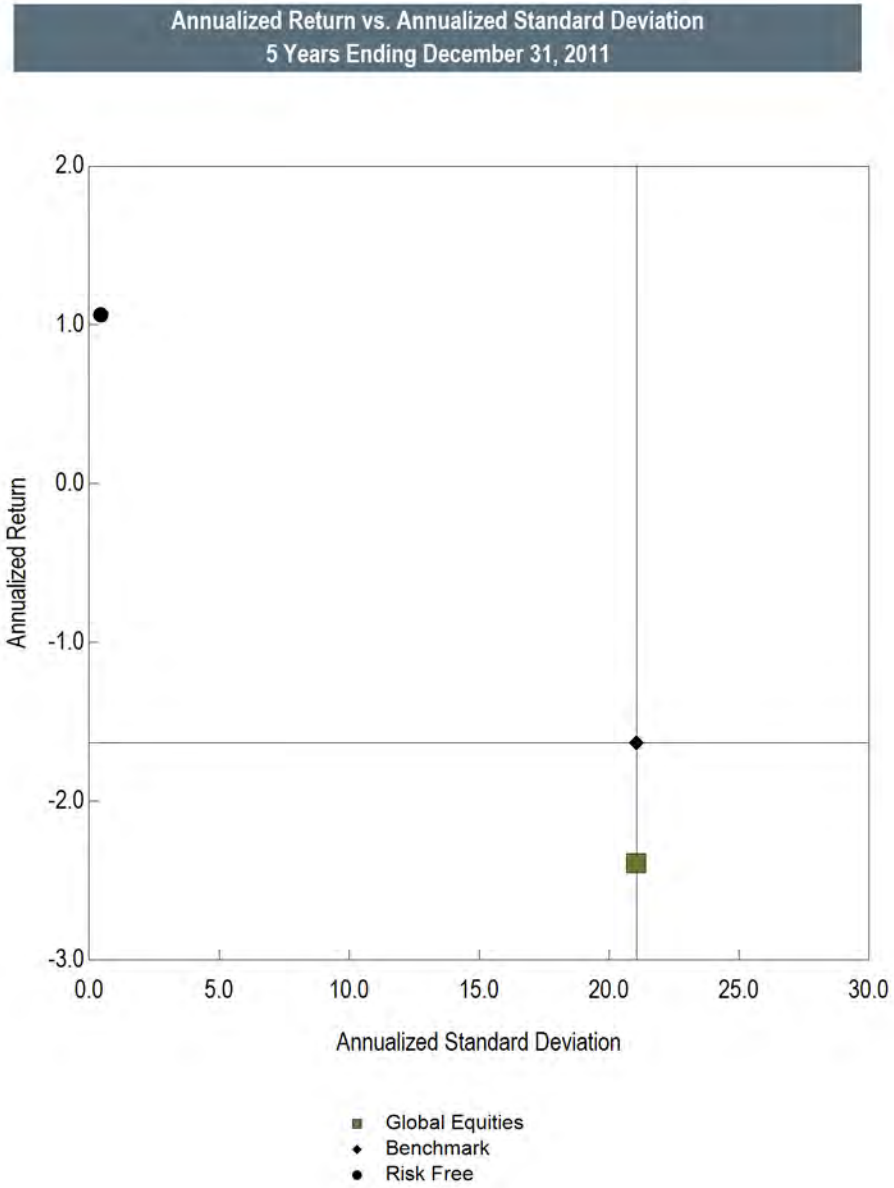

## Ratio of Cumulative Wealth
## 8 Years 6 Months Ending December 31, 2011



# Risk Profile

Benchmark: Aggregate Benchmark



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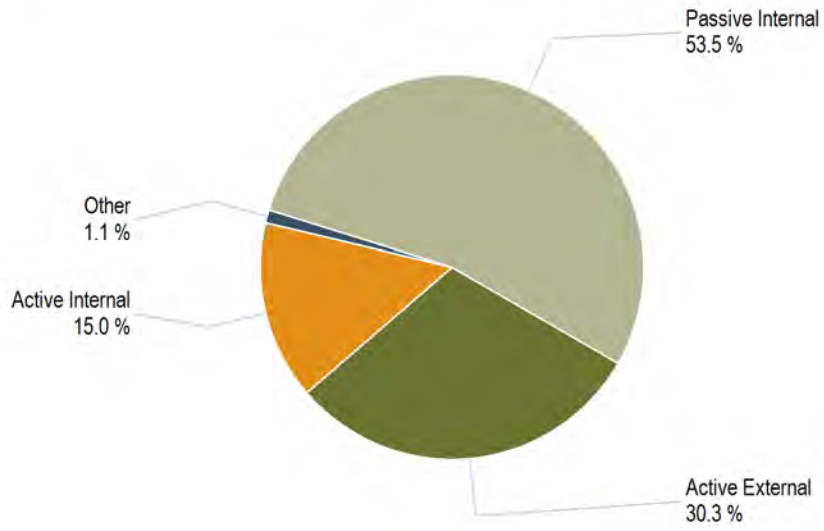
# Fixed Income

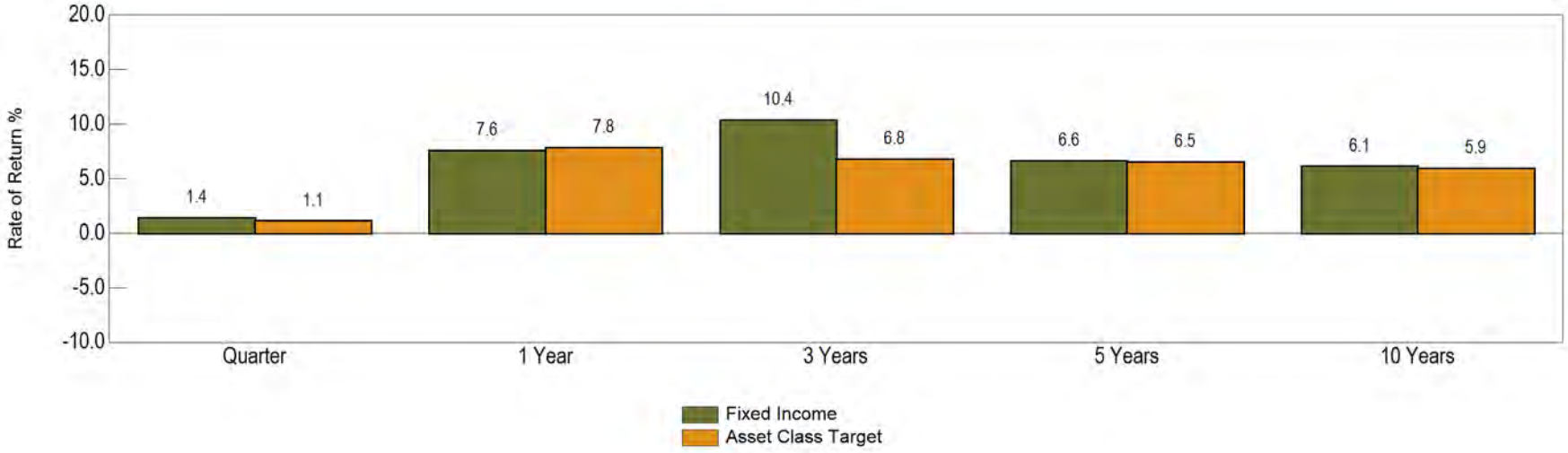
# Overview

Benchmark: Asset Class Target

## Current Allocation



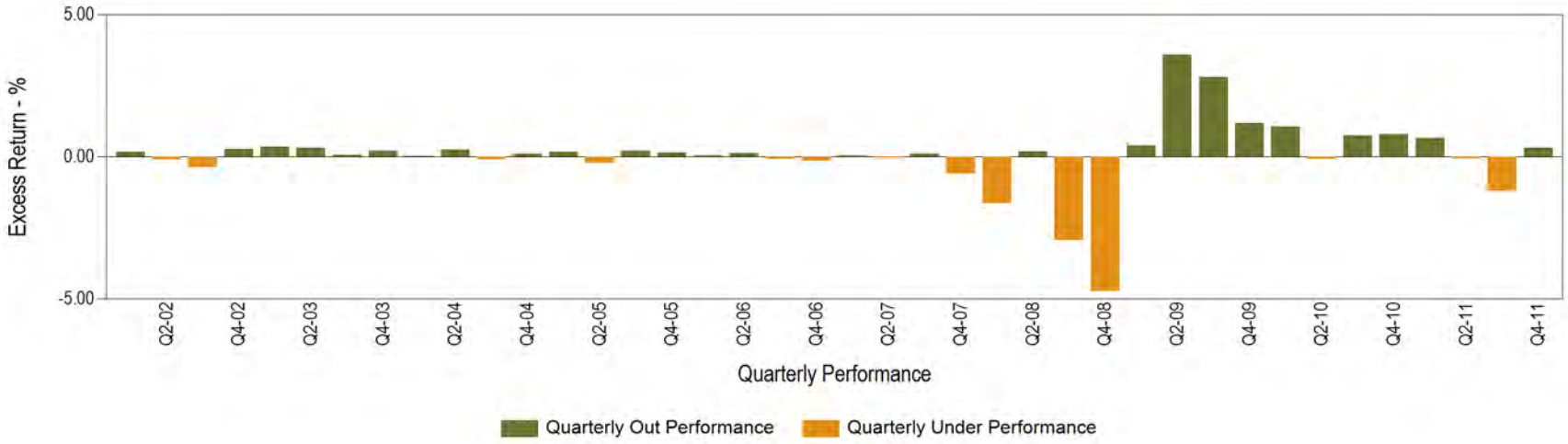

## Return Summary



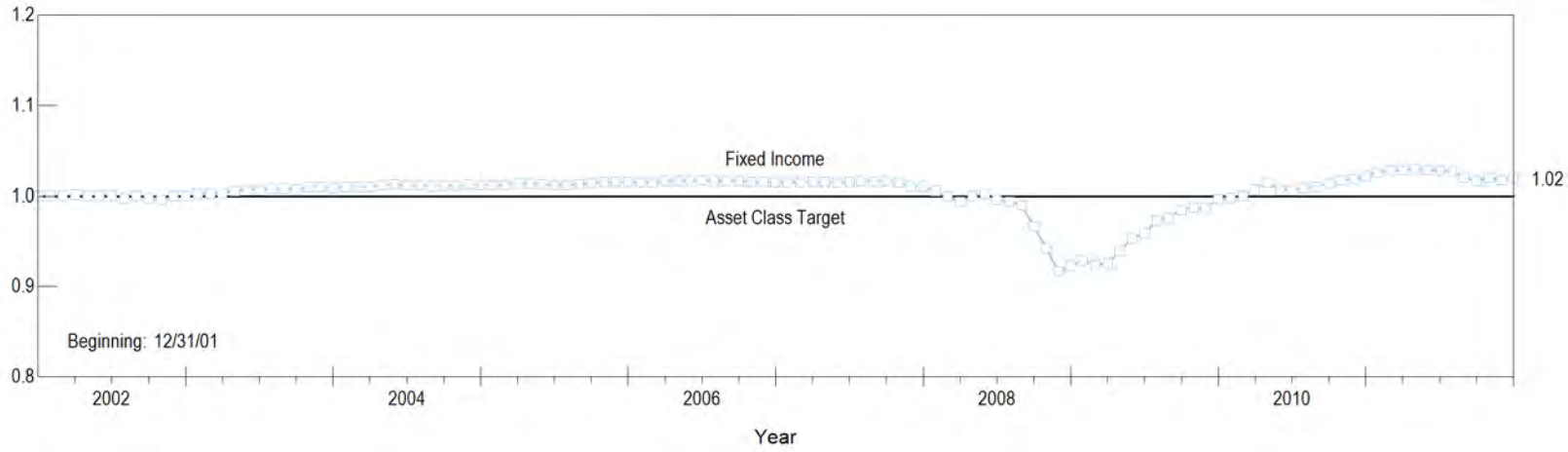
# Overview

Benchmark: Asset Class Target

## Quarterly Excess Performance




## Ratio of Cumulative Wealth
## 10 Years Ending December 31, 2011

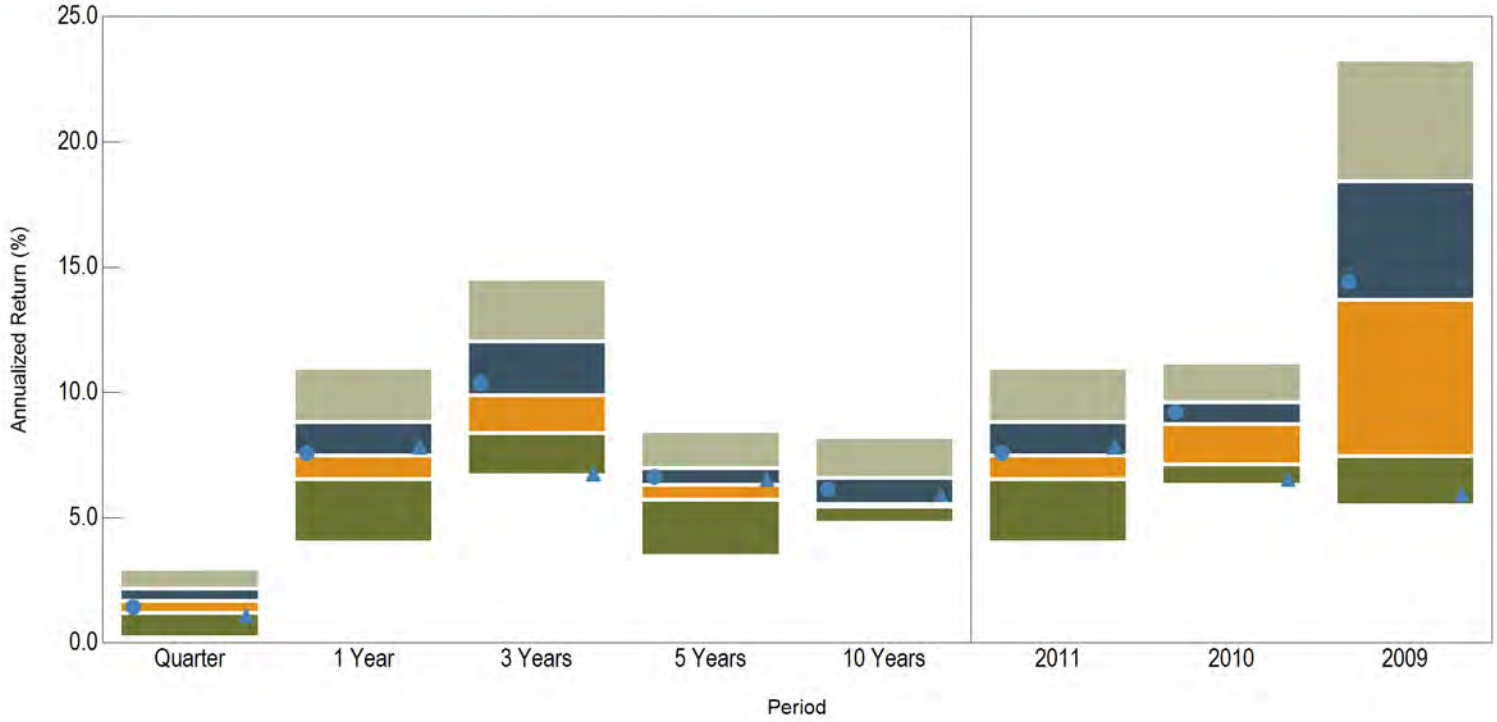


# Universe Comparison

Benchmark: Asset Class Target

Universe: Public Funds >$1B - US FI Net

## Ending December 31, 2011



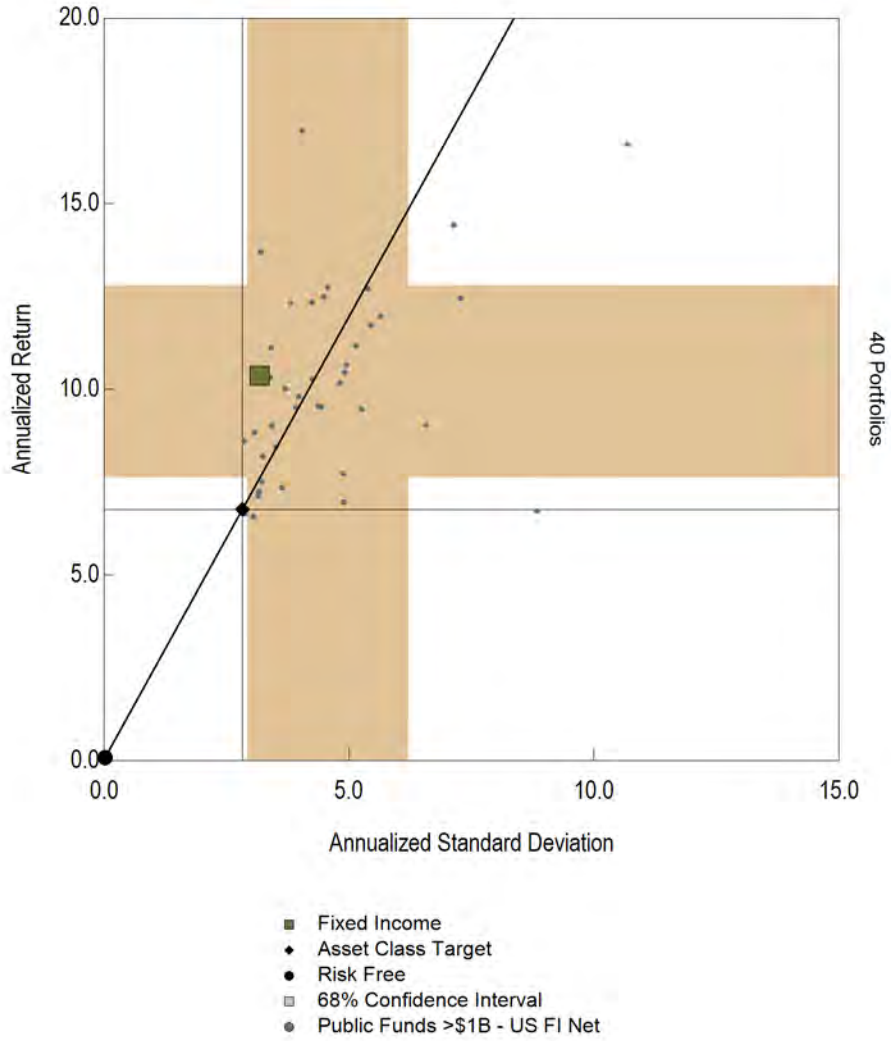

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5th Percentile | 2.9 | | 11.0 | | 14.5 | | 8.4 | | 8.2 | | 11.0 | | 11.2 | | 23.3 | |
| 25th Percentile | 2.2 | | 8.8 | | 12.1 | | 7.0 | | 6.6 | | 8.8 | | 9.6 | | 18.4 | |
| Median | 1.7 | | 7.5 | | 9.9 | | 6.3 | | 5.5 | | 7.5 | | 8.8 | | 13.7 | |
| 75th Percentile | 1.2 | | 6.5 | | 8.4 | | 5.7 | | 5.4 | | 6.5 | | 7.1 | | 7.5 | |
| 95th Percentile | 0.2 | | 4.0 | | 6.7 | | 3.5 | | 4.8 | | 4.0 | | 6.3 | | 5.5 | |
| # of Portfolios | 54 | | 51 | | 40 | | 31 | | 19 | | 51 | | 47 | | 45 | |
| ● Fixed Income | 1.4 | (64) | 7.6 | (45) | 10.4 | (41) | 6.6 | (41) | 6.1 | (38) | 7.6 | (45) | 9.2 | (34) | 14.4 | (46) |
| ▲ Asset Class Target | 1.1 | (81) | 7.8 | (38) | 6.8 | (95) | 6.5 | (48) | 5.9 | (46) | 7.8 | (38) | 6.5 | (92) | 5.9 | (91) |

# Risk Profile

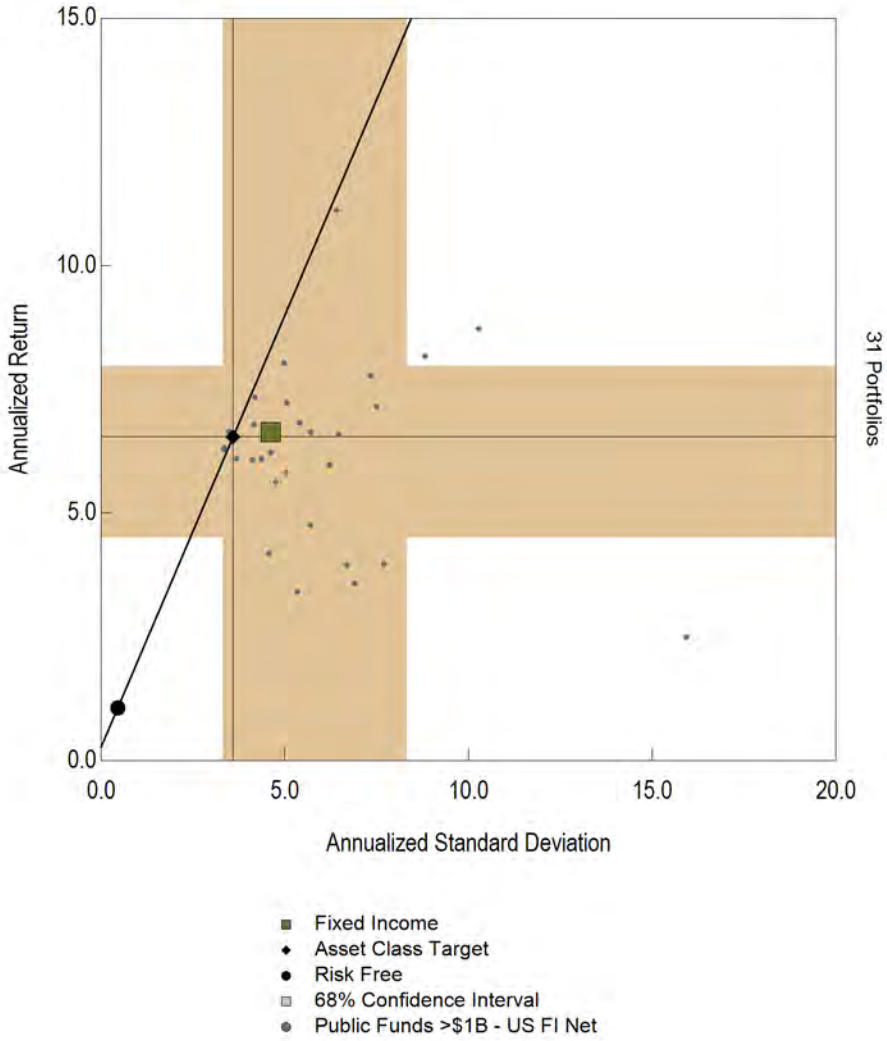
Benchmark: Asset Class Target

Universe: Public Funds >$1B - US FI Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011



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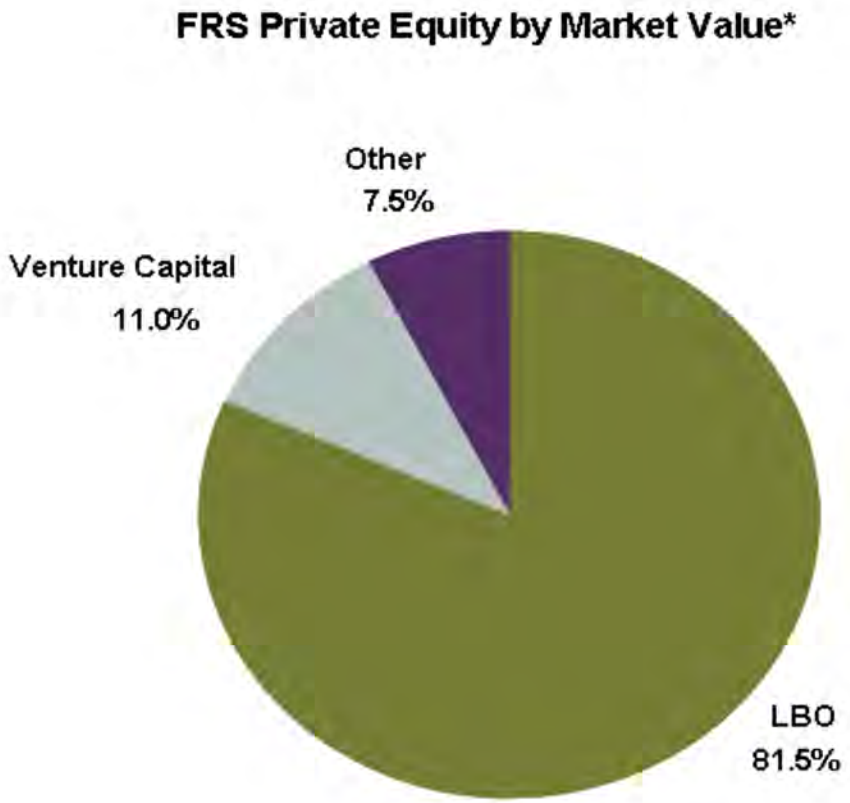
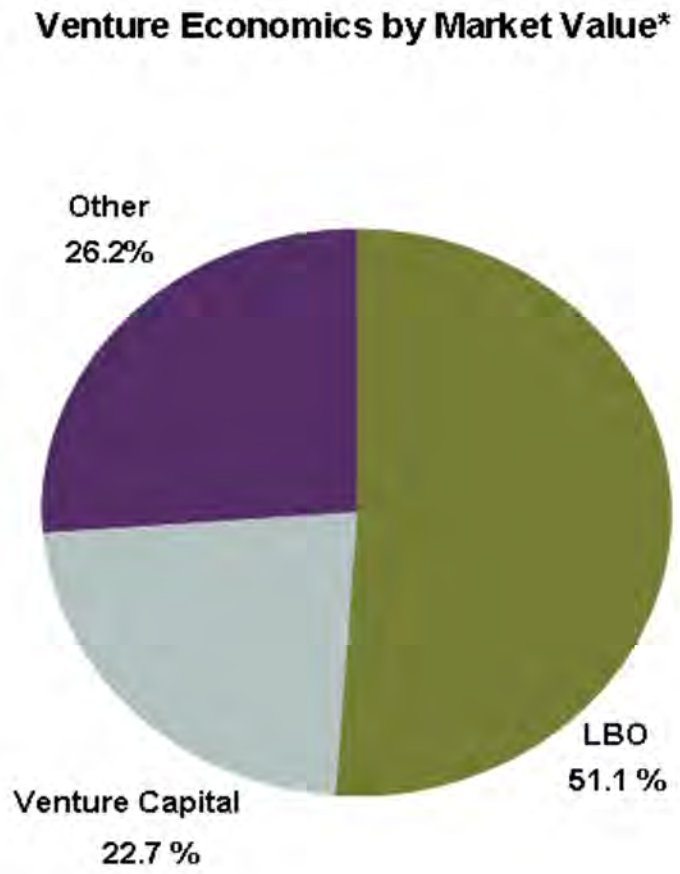
# Private Equity

## Overview



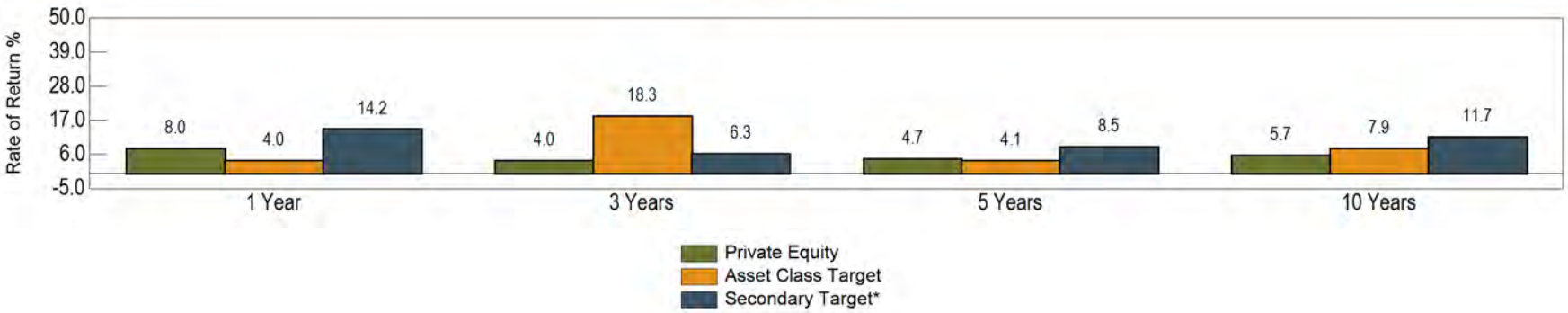




* Allocation data is as of September 30, 2011

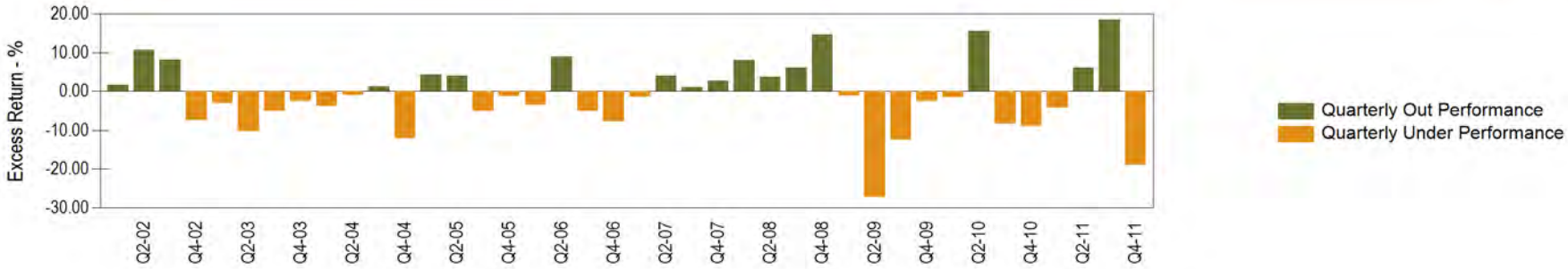
# Time-Weighted Investment Results

Benchmark: Asset Class Target

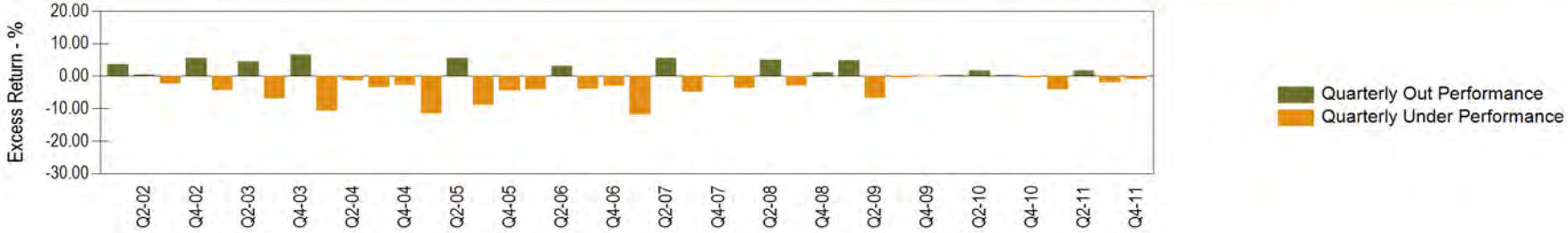
## Return Summary




## Quarterly Excess Performance vs. Asset Class Target




## Quarterly Excess Performance vs. Secondary Target

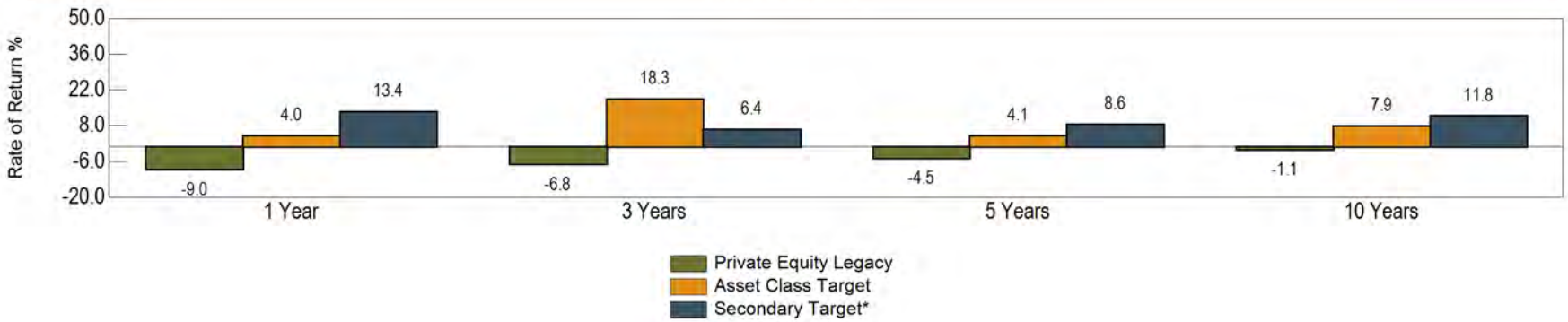



* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

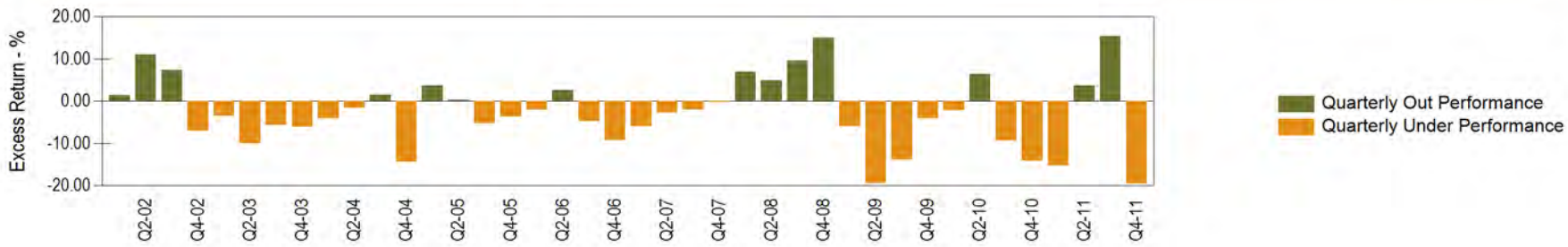
# Time-Weighted Investment Results

Benchmark: Asset Class Target

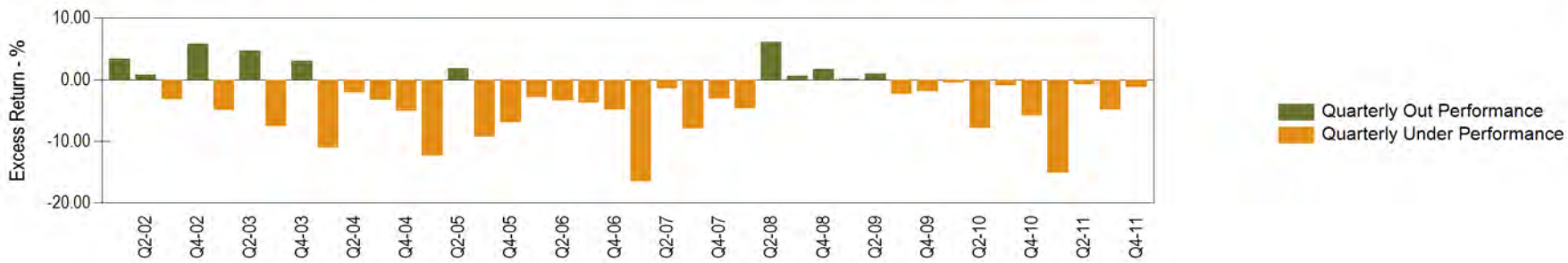
## Return Summary




## Quarterly Excess Performance vs. Asset Class Target




## Quarterly Excess Performance vs. Secondary Target

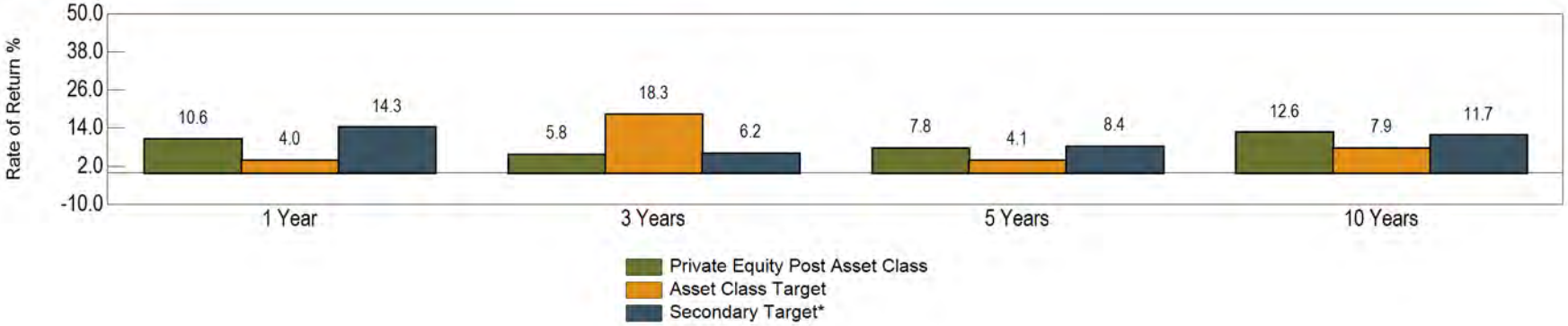



* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

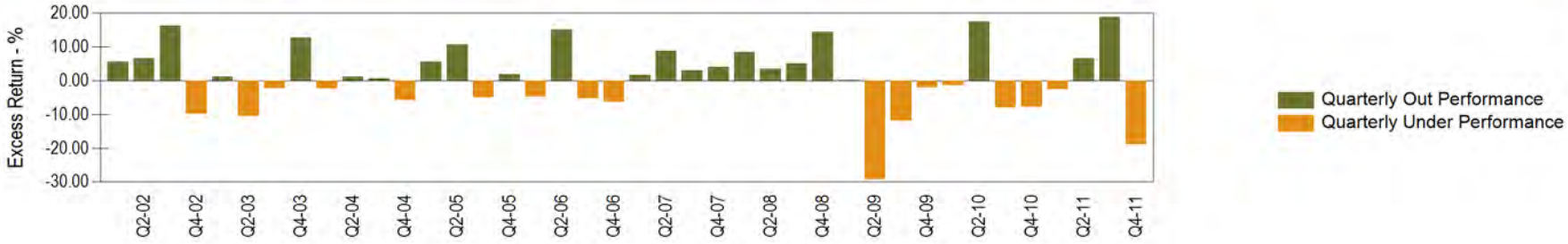
# Time-Weighted Investment Results

Benchmark: Asset Class Target

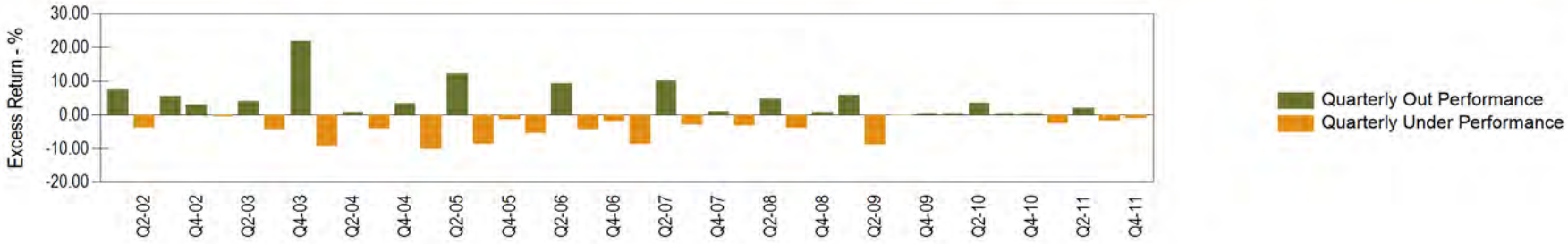
## Return Summary




## Quarterly Excess Performance vs. Asset Class Target

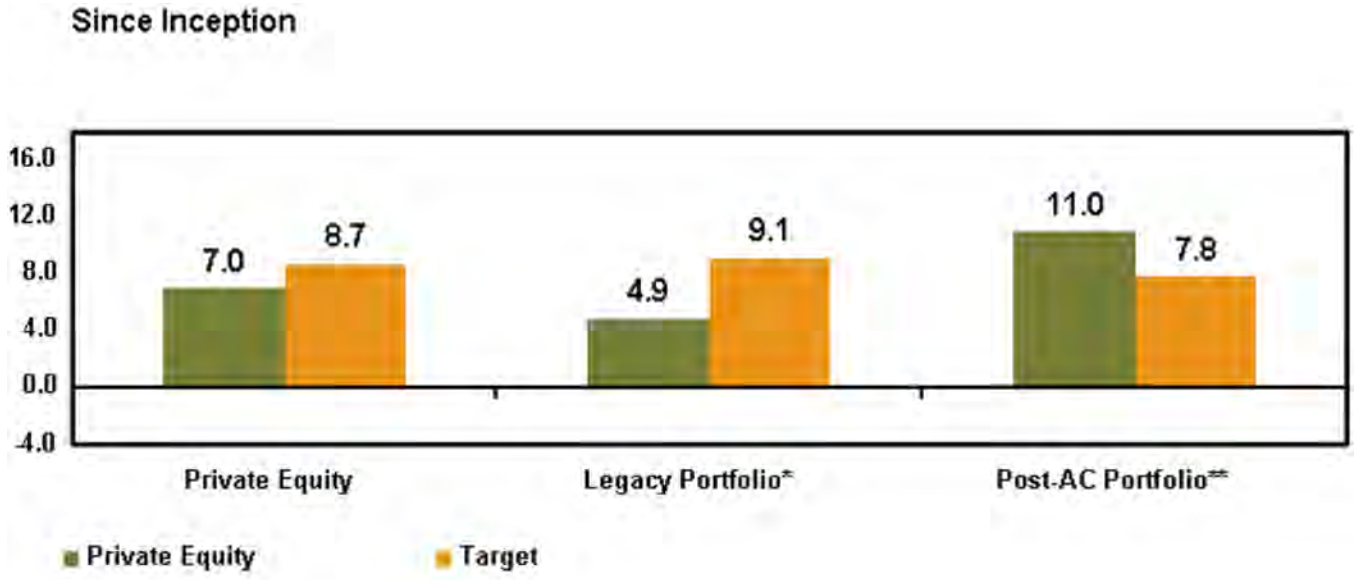


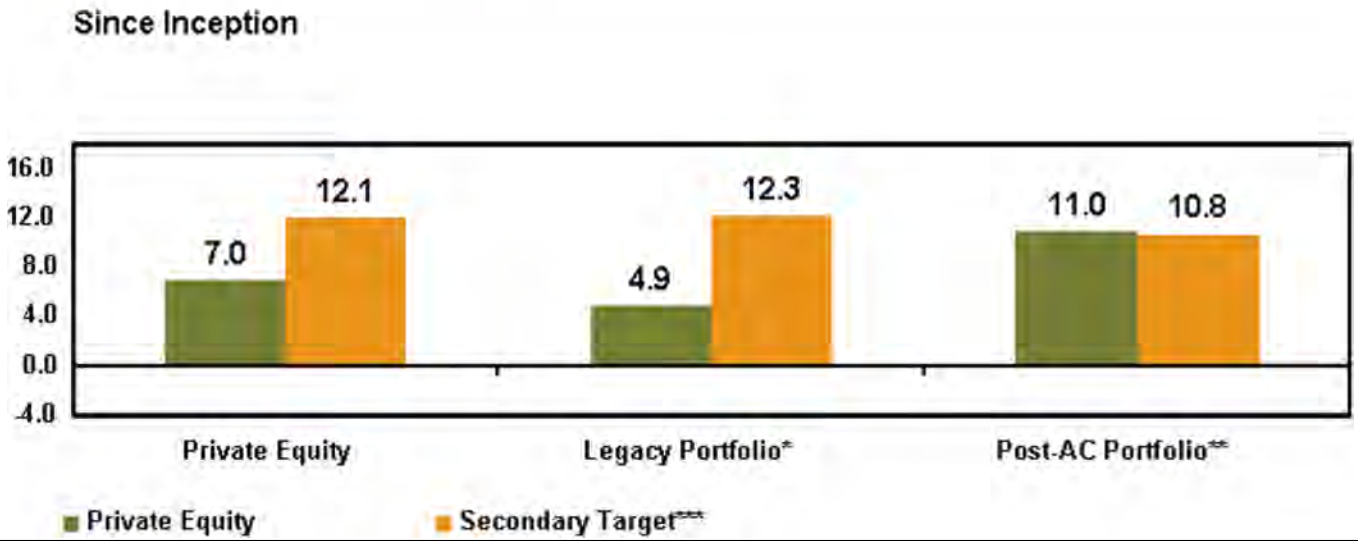

## Quarterly Excess Performance vs. Secondary Target




* The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

## Dollar-Weighted Investment Results




* The Inception Date for the Legacy Portfolio is January 1989.

** The Inception Date for the Post-AC Portfolio is September 2000.

*** The Secondary Target is a blend of the Cambridge Associates Private Equity Index and the Cambridge Associates Venture Capital Index.

## Private Equity Dollar-Weighted Performance
## Cumulative Performance Measures Since Inception Through December 31, 2011

| Name | Years Since Inception | Commitment | Net Paid In Cap. | Net Asset Value | IRR |
|---|---|---|---|---|---|
| Corporate Partners | CLOSED | N/A | $-133,709,385 | N/A | N/A |
| Liberty Partners I, L.P. | CLOSED | N/A | $-267,090,548 | N/A | N/A |
| Liberty Partners IV, L.P. | CLOSED | N/A | $66,000,789 | N/A | N/A |
| Thomas H. Lee Equity Fund IV, L.P. | CLOSED | N/A | $12,688,674 | N/A | N/A |
| Ripplewood Partners I, L.P. | CLOSED | N/A | $-75,695,566 | N/A | N/A |
| TSG Capital Fund II, L.P. | CLOSED | N/A | $46,347,448 | $72,830 | N/A |
| Liberty Partners II, L.P. | 17.52 | $659,789,821 | $-213,382,441 | $23,874,031 | 10.90% |
| Cypress Equity Group Trust Fund | 16.32 | $15,000,000 | $-10,034,610 | $879,231 | 16.33% |
| Centre Capital Investors II, L.P. | 15.97 | $200,000,000 | $52,090,331 | $1,911,424 | -4.22% |
| Liberty Partners III, L.P. | 15.51 | $506,208,481 | $6,349,591 | $10,000,000 | 0.18% |
| Carlyle Partners II, L.P. | 15.31 | $200,000,000 | $-264,179,271 | $17,003,282 | 19.94% |
| Hicks, Muse, Tate & Furst Fund III, L.P. | 14.82 | $200,000,000 | $24,793,309 | $20,862,850 | -0.34% |
| Lexington Co-Investment Partners, L.P. | 13.97 | $500,000,000 | $-140,257,984 | $6,882,146 | 5.57% |
| Apollo Investment Fund IV, L.P. | 13.53 | $250,000,000 | $-161,037,375 | $14,302,208 | 8.70% |
| Chartwell Capital Investors II, L.P. | 13.21 | $50,000,000 | $-12,451,250 | $10,107,801 | 5.59% |
| Hicks, Muse, Tate & Furst Fund IV, L.P. | 13.09 | $400,000,000 | $141,908,790 | $7,601,165 | -7.54% |
| Liberty Partners V, L.P. | 12.85 | $329,664,359 | $-20,443,580 | $25,865,812 | 2.58% |
| Green Equity Investors III, L.P. | 12.80 | $60,000,000 | $-65,616,553 | $5,588,838 | 21.49% |
| Private Equity Cash | 12.78 | N/A | $108,666,297 | $134,960,814 | 3.18% |
| Willis Stein & Partners II, L.P. | 12.74 | $40,000,000 | $16,789,706 | $105,735 | -9.61% |
| Carlyle Partners III, L.P. | 11.34 | $200,000,000 | $-229,574,615 | $19,403,559 | 22.85% |
| Willis Stein & Partners III, L.P. | 11.07 | $100,000,000 | $37,661,972 | $44,411,569 | 1.12% |
| Ripplewood Partners II, L.P. | 10.85 | $100,000,000 | $19,696,163 | $47,096,993 | 7.10% |
| Lexington Capital Partners IV, L.P. | 10.72 | $200,000,000 | $-125,163,055 | $24,420,605 | 19.60% |
| Apollo Investment Fund V, L.P. | 10.63 | $150,000,000 | $-168,857,112 | $55,793,796 | 37.58% |
| Thomas H. Lee Equity Fund V, L.P. | 10.50 | $50,000,000 | $-11,515,697 | $17,331,619 | 12.99% |
| Hicks, Muse, Tate & Furst Fund V, L.P. | 10.15 | $25,000,000 | $-18,554,410 | $1,196,726 | 19.44% |
| Liberty Partners VI, L.P. | 9.96 | $595,484,687 | $305,547,002 | $251,736,965 | -1.75% |
| Lexington Capital Partners V, L.P. | 9.39 | $100,000,000 | $-33,787,719 | $31,281,717 | 20.01% |
| Lexington Co-Investment Partners II, L.P. | 9.27 | $500,000,000 | $-220,031,052 | $238,904,069 | 24.26% |
| Wellspring Capital Partners III, L.P. | 8.64 | $50,000,000 | $-41,487,786 | $10,803,379 | 26.69% |
| Green Equity Investors IV, L.P. | 8.33 | $100,000,000 | $55,308,648 | $115,073,266 | 9.98% |
| Top Tier Venture Capital II | 8.26 | $120,000,000 | $79,272,884 | $87,028,742 | 1.34% |
| Gores Capital Partners I, L.P. | 7.94 | $50,000,000 | $-2,642,965 | $35,827,451 | 17.64% |

## Private Equity Dollar-Weighted Performance (continued)
## Cumulative Performance Measures Since Inception Through December 31, 2011

| Name | Years Since Inception | Commitment | Net Paid In Cap. | Net Asset Value | IRR |
|---|---|---|---|---|---|
| Platinum Equity Capital Partners I, L.P | 7.89 | $50,000,000 | $-44,623,250 | $12,905,664 | 58.63% |
| Pantheon Venture Partners II, L.P. | 7.89 | $100,000,000 | $65,047,500 | $74,508,181 | 3.54% |
| FS Equity Partners V, L.P. | 7.67 | $50,000,000 | $5,369,969 | $31,444,754 | 12.55% |
| TPG Partners IV, L.P. | 7.59 | $50,000,000 | $-1,929,381 | $30,954,926 | 14.40% |
| GS Partners Ventures, LLC | 7.51 | $200,000,000 | $148,632,541 | $176,276,231 | 4.46% |
| Kelso Investment Associates VII, L.P. | 7.50 | $50,000,000 | $15,756,728 | $40,874,695 | 11.71% |
| Fairview Ventures Fund II, L.P. | 7.50 | $50,000,000 | $39,410,268 | $34,740,775 | -2.74% |
| Hellman & Friedman Capital Partners V, L.P. | 7.06 | $75,000,000 | $-34,569,329 | $51,492,391 | 27.30% |
| Kohlberg Investors V, L.P. | 7.01 | $45,000,000 | $22,161,237 | $27,991,827 | 3.29% |
| New Mountain Partners II, L.P. | 6.97 | $50,000,000 | $10,617,826 | $27,885,510 | 8.28% |
| Top Tier Venture Capital III | 6.72 | $75,000,000 | $55,699,939 | $66,033,028 | 4.84% |
| Carlyle Partners IV, L.P. | 6.68 | $75,000,000 | $25,763,075 | $64,676,906 | 9.96% |
| Warburg Pincus Private Equity IX, L.P. | 6.33 | $75,000,000 | $40,174,973 | $70,434,984 | 7.93% |
| Lexington Co-Investment Partners 2005, L.P. | 6.29 | $500,000,000 | $367,390,018 | $353,861,513 | -0.79% |
| Pomona Capital VI, L.P. | 6.29 | $50,000,000 | $25,523,182 | $35,652,946 | 5.73% |
| Liberty Partners VII, L.P. | 6.18 | $290,808,542 | $54,246,978 | $42,950,733 | -2.23% |
| Lexington Capital Partners VI-B, L.P. | 6.07 | $100,000,000 | $57,954,155 | $70,574,013 | 4.39% |
| Apollo Investment Fund VI, L.P. | 6.07 | $200,000,000 | $152,915,844 | $182,197,084 | 3.91% |
| Wellspring Capital Partners IV, L.P. | 5.93 | $75,000,000 | $65,380,314 | $74,190,234 | 3.67% |
| Blackstone Capital Partners V, L.P. | 5.80 | $150,000,000 | $125,093,809 | $124,580,442 | -0.11% |
| TowerBrook Investors II, L.P. | 5.75 | $75,000,000 | $15,760,944 | $40,237,560 | 9.06% |
| Thoma Cressey Fund VIII, L.P. | 5.74 | $50,000,000 | $16,837,855 | $49,738,934 | 12.76% |
| TPG Partners V, L.P. | 5.52 | $100,000,000 | $76,066,901 | $57,674,862 | -6.12% |
| Fairview Ventures Fund III, L.P. | 5.51 | $75,000,000 | $44,465,188 | $49,200,802 | 5.09% |
| Permira IV, L.P. | 5.38 | € 50,000,000 | $51,375,118 | $48,090,214 | -1.82% |
| Lindsay Goldberg & Bessemer II, L.P. | 5.38 | $100,000,000 | $67,538,674 | $75,103,867 | 2.29% |
| Grove Street Partners Buyouts, LLC | 5.26 | $150,000,000 | $77,597,780 | $85,508,347 | 3.63% |
| Thomas H. Lee Equity Fund VI, L.P. | 5.13 | $75,000,000 | $50,931,703 | $55,042,863 | 2.07% |
| First Reserve Fund XI, L.P. | 5.13 | $100,000,000 | $60,221,896 | $59,880,475 | -0.13% |
| 3i Europartners Vb L.P | 5.13 | € 59,000,000 | $61,805,973 | $35,549,966 | -16.32% |
| RCP Advisors Fund IV, LLC | 5.01 | $50,000,000 | $27,745,198 | $33,480,189 | 5.20% |
| Hellman & Friedman Capital Partners VI, L.P. | 4.95 | $100,000,000 | $57,103,707 | $71,544,253 | 4.98% |
| Providence Equity Partners VI, L.P. | 4.80 | $50,000,000 | $39,727,448 | $44,839,415 | 4.06% |
| Carlyle Partners Europe III | 4.78 | € 49,000,000 | $49,547,691 | $43,124,155 | -6.08% |

## Private Equity Dollar-Weighted Performance (continued)
## Cumulative Performance Measures Since Inception Through December 31, 2011

| Name | Years Since Inception | Commitment | Net Paid In Cap. | Net Asset Value | IRR |
|---|---|---|---|---|---|
| Green Equity Investors V, L.P. | 4.67 | $100,000,000 | $57,728,600 | $80,068,397 | 13.75% |
| Gores Capital Partners II, L.P. | 4.44 | $50,000,000 | $14,648,853 | $28,477,342 | 12.13% |
| New Mountain Partners III, L.P. | 4.40 | $100,000,000 | $53,110,944 | $55,061,377 | 1.62% |
| Carlyle Partners V, L.P. | 4.26 | $200,000,000 | $104,003,615 | $128,859,248 | 7.54% |
| Kohlberg Investors VI, L.P. | 4.23 | $50,000,000 | $24,262,604 | $39,406,758 | 15.46% |
| Apollo Investment Fund VII, L.P. | 4.21 | $200,000,000 | $92,749,880 | $117,329,916 | 10.68% |
| Kelso Investment Associates VIII, L.P | 4.21 | $100,000,000 | $42,550,716 | $38,891,073 | -5.76% |
| Platinum Equity Capital Partners II, L.P. | 4.21 | $75,000,000 | $44,305,782 | $56,325,785 | 8.87% |
| RCP Advisors, LLC (Fund V) | 4.15 | $50,000,000 | $26,298,800 | $28,095,163 | 3.24% |
| Warburg Pincus X | 4.11 | $150,000,000 | $129,176,427 | $129,482,087 | 0.11% |
| Top Tier Venture Capital IV | 3.90 | $100,000,000 | $59,039,865 | $74,849,915 | 14.60% |
| TPG Partners VI, L.P. | 3.71 | $200,000,000 | $112,331,109 | $109,374,896 | -1.87% |
| Liberty Partners Group II | 3.64 | $12,625,000 | $639,847 | $-723 | 0.00% |
| PAI Europe V | 3.63 | € 27,500,000 | $26,606,204 | $20,588,014 | -11.41% |
| Pomona Capital VII, L.P. | 3.52 | $50,000,000 | $22,591,066 | $28,592,555 | 9.79% |
| GS Partners Ventures II, LLC | 3.52 | $200,000,000 | $64,589,194 | $73,258,543 | 11.11% |
| Advent International GPE VI | 3.49 | $58,000,000 | $36,672,196 | $39,327,084 | 4.18% |
| Lindsay Goldberg III | 3.46 | $100,000,000 | $32,480,364 | $28,646,949 | -9.08% |
| CVC European Equity Partners V | 3.46 | € 70,000,000 | $51,068,663 | $58,493,278 | 7.49% |
| Thoma Bravo Fund IX | 3.46 | $50,000,000 | $24,667,637 | $46,150,132 | 30.16% |
| TowerBrook Investors III, L.P. | 3.46 | $150,000,000 | $41,294,276 | $62,987,977 | 17.88% |
| KKR European Fund III | 3.35 | € 40,000,000 | $26,341,701 | $23,944,847 | -6.27% |
| Ares Corporate Opportunities Fund III | 3.27 | $100,000,000 | $29,875,002 | $57,658,172 | 22.32% |
| RCP Advisors, LLC (Fund VI) | 3.24 | $50,000,000 | $19,492,553 | $18,011,250 | -6.46% |
| Blackstone Capital Partners VI | 3.15 | $200,000,000 | $21,897,075 | $18,659,777 | -53.01% |
| Cressey & Company Fund IV | 3.15 | $50,000,000 | $15,262,941 | $11,117,613 | -17.64% |
| First Reserve Fund XII | 3.13 | $200,000,000 | $132,736,789 | $127,498,006 | -2.12% |
| Carlyle Asia Growth Partners IV | 3.04 | $75,000,000 | $30,768,233 | $31,523,754 | 1.68% |
| Charterhouse Capital Partners IX | 2.68 | € 70,000,000 | $37,788,785 | $37,381,731 | -0.96% |
| Top Tier Special Opportunities Fund | 2.60 | $12,450,000 | $10,208,239 | $12,956,627 | 15.94% |
| Riverside Capital Appreciation Fund V | 2.54 | $75,000,000 | $47,333,814 | $48,927,930 | 2.39% |
| FS Equity Partners VI | 2.43 | $75,000,000 | $40,888,526 | $38,666,689 | -5.12% |
| Energy Capital Partners II | 2.42 | $100,000,000 | $38,430,596 | $46,532,690 | 13.23% |
| KPS Special Situations Fund III | 2.27 | $50,000,000 | $14,920,591 | $14,816,213 | -0.73% |

***IRR returns less than one year are not reported

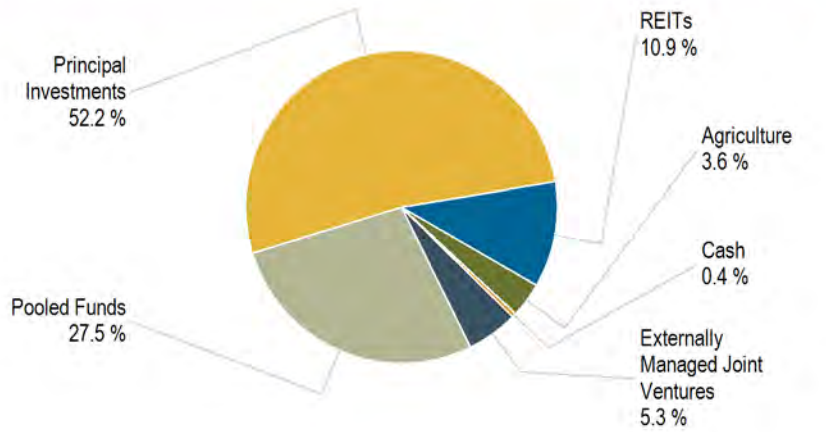
| Private Equity Dollar-Weighted Performance (continued)<br>Cumulative Performance Measures Since Inception Through December 31, 2011 | | | | | |
|---|---|---|---|---|---|
| Name | Years Since Inception | Commitment | Net Paid In Cap. | Net Asset Value | IRR |
| Gores Capital Partners III, L.P. | 2.25 | $125,000,000 | $37,096,339 | $30,258,851 | -29.07% |
| Charlesbank Equity Fund VII, L.P. | 2.19 | $75,000,000 | $22,023,549 | $24,244,931 | 8.85% |
| Lexington Capital Partners VII | 2.08 | $200,000,000 | $61,584,047 | $76,749,331 | 18.86% |
| 3i Growth Capital Fund | 1.77 | € 40,000,000 | $29,114,098 | $25,706,563 | -8.28% |
| Riverside Europe Fund IV, L.P. | 1.54 | € 40,000,000 | $35,769,959 | $30,853,658 | -18.66% |
| TA XI | 1.42 | $100,000,000 | $38,250,000 | $39,269,764 | 4.39% |
| Snow Phipps II, L.P. | 1.39 | $50,000,000 | $10,417,090 | $8,700,073 | -19.84% |
| Pantheon Global Secondary Fund IV, L.P. | 1.36 | $100,000,000 | $19,437,534 | $23,538,475 | 21.15% |
| JH Whitney VII | 1.22 | $75,000,000 | $16,803,635 | $16,486,611 | -2.96% |
| Trident V | 1.17 | $75,000,000 | $19,457,457 | $17,923,187 | -11.36% |
| RCP Fund VII | 1.08 | $50,000,000 | $6,499,995 | $5,079,868 | -46.25% |
| EnerVest Energy XII-A | 1.01 | $60,000,000 | $28,642,532 | $27,602,462 | -7.41% |
| EnCap Energy Capital Fund VIII | 0.87 | $75,000,000 | $9,223,284 | $9,159,893 | *** |
| Cortec Group V | 0.70 | $50,000,000 | $830,000 | $265,786 | *** |
| Montagu Private Equity Fund IV | 0.60 | € 40,000,000 | $4,602,271 | $3,215,351 | *** |
| Francisco Partners III | 0.50 | $75,000,000 | $12,750,000 | $11,258,327 | *** |
| Wellspring Capital Partners V | 0.50 | $150,000,000 | $11,813,846 | $10,026,344 | *** |
| GS Partners Buyouts II | 0.44 | $200,000,000 | $9,087,591 | $8,299,912 | *** |
| Fairview Special Opportunities Fund | 0.43 | $50,000,000 | $3,971,878 | $3,775,371 | *** |
| ABRY Partners VII | 0.39 | $75,000,000 | $16,119,446 | $14,394,637 | *** |
| Hellman & Friedman Capital Partners VII, L.P. | 0.39 | $200,000,000 | $41,716,970 | $39,036,955 | *** |
| Berkshire Fund VIII | 0.35 | $60,000,000 | $3,238,138 | $3,189,985 | *** |
| BC European Capital IX | 0.28 | € 70,000,000 | $9,107,434 | $7,863,049 | *** |
| Strategic Investors Fund V-A | 0.26 | $100,000,000 | $8,000,000 | $7,976,042 | *** |
| TPG Growth II | 0.03 | $100,000,000 | $3,985,802 | $2,784,508 | *** |
| **Private Equity Aggregate** | | | **$2,636,655,485** | **$5,783,192,360** | **6.97%** |

***IRR returns less than one year are not reported

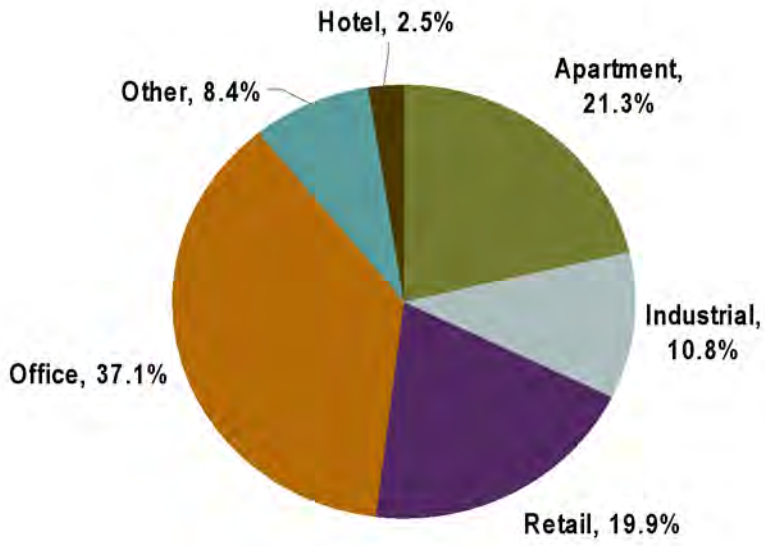
# Real Estate

# Overview

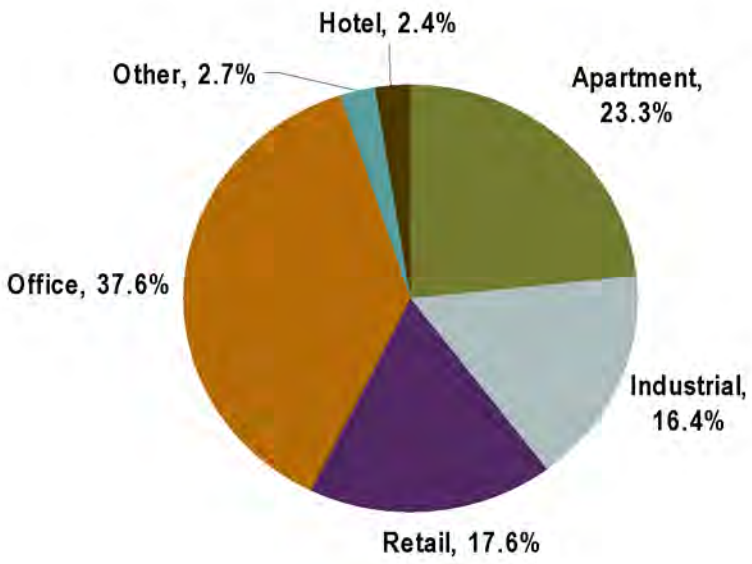
## Current Allocation




**FRS***




**NFI-ODCE Index***

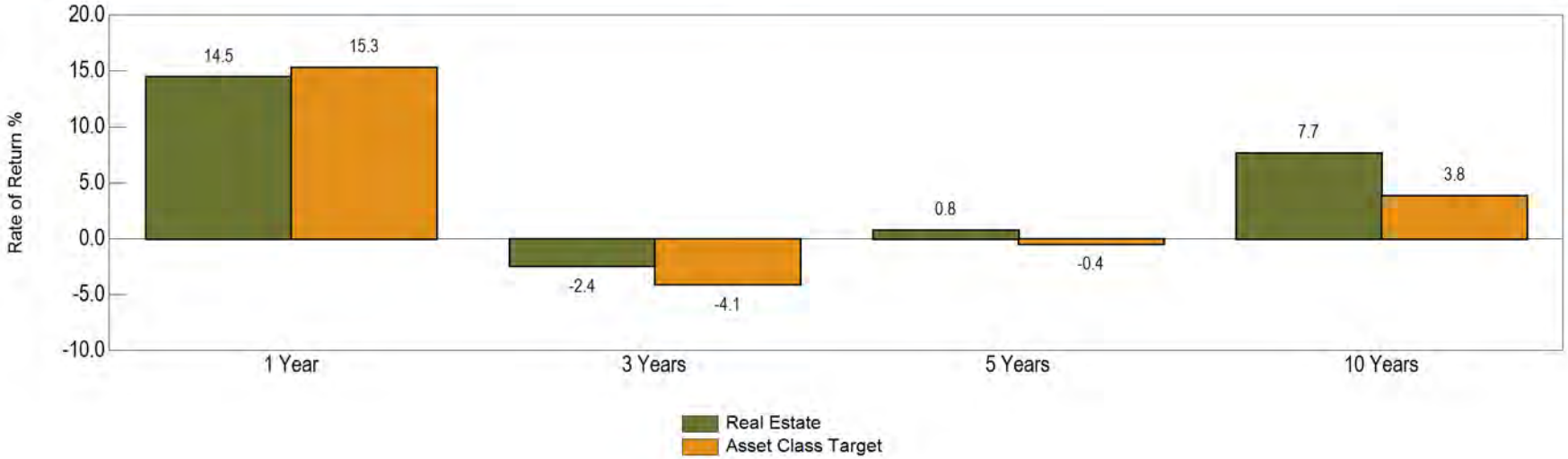



*Property Allocation data is as of September 30, 2011. The FRS chart includes only the FRS private real estate assets. Property type information for the REIT portfolios is not included.

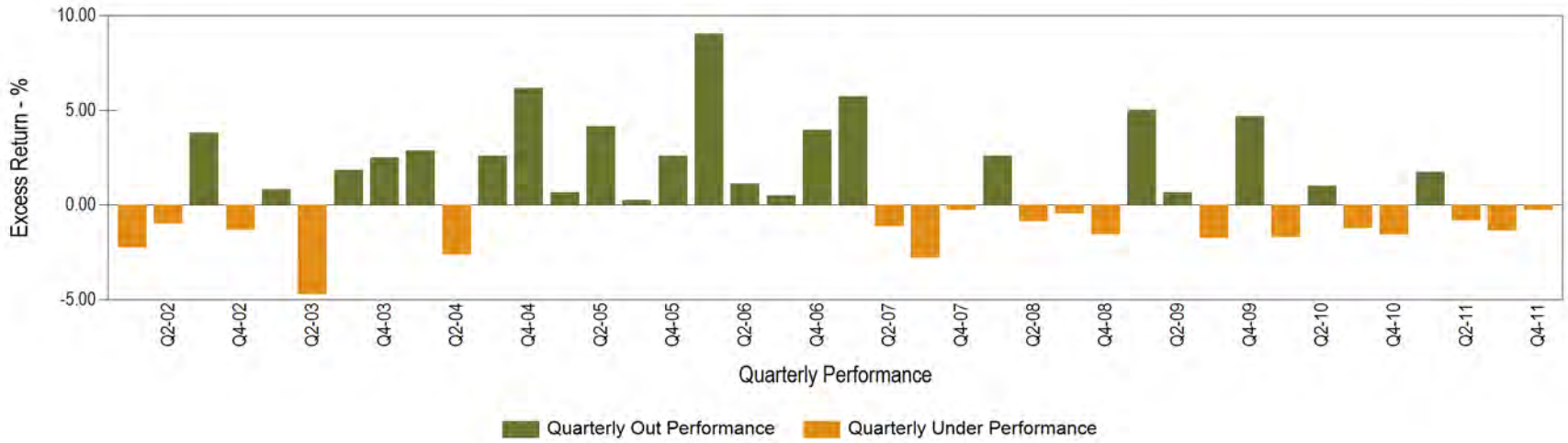
# Overview

Benchmark: Asset Class Target

## Return Summary



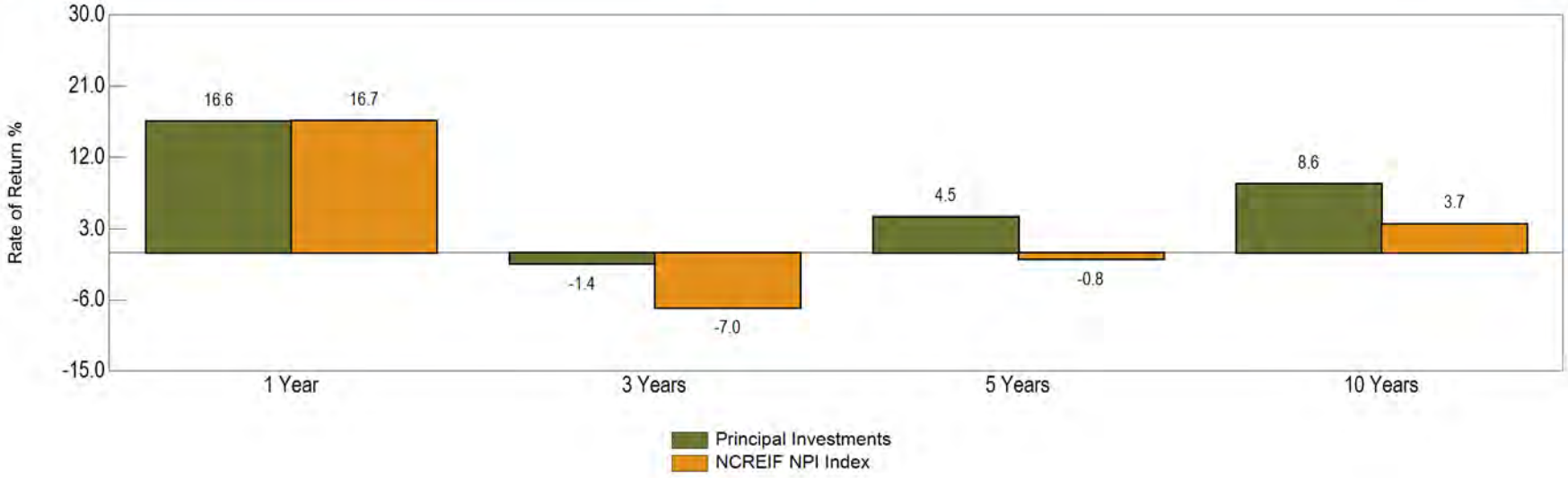

## Quarterly Excess Performance



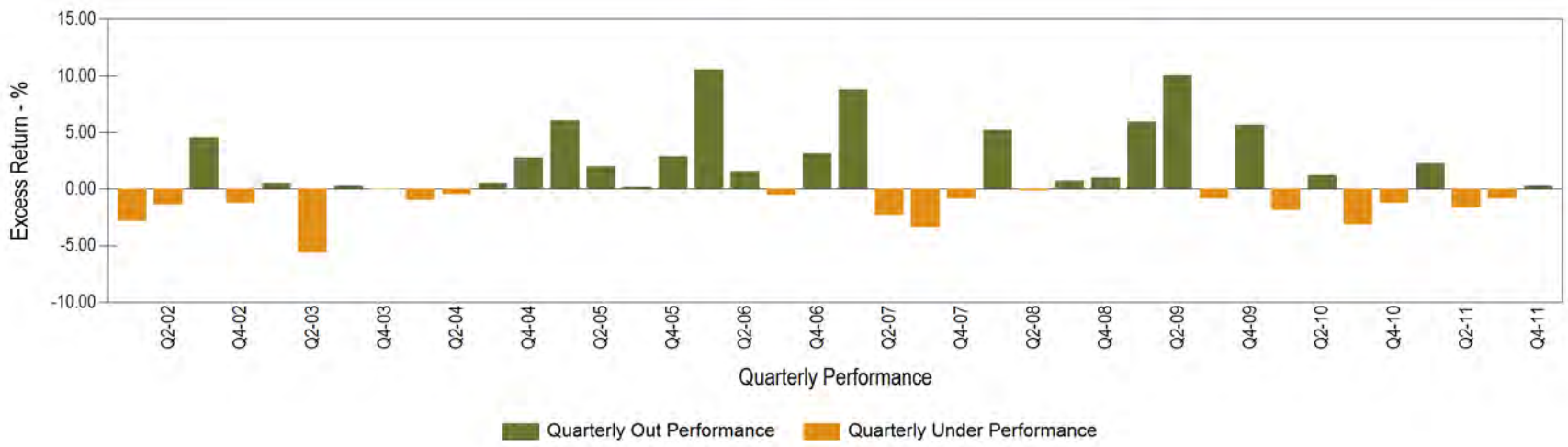
# Principal Investments

Benchmark: NCREIF NPI Index

## Return Summary



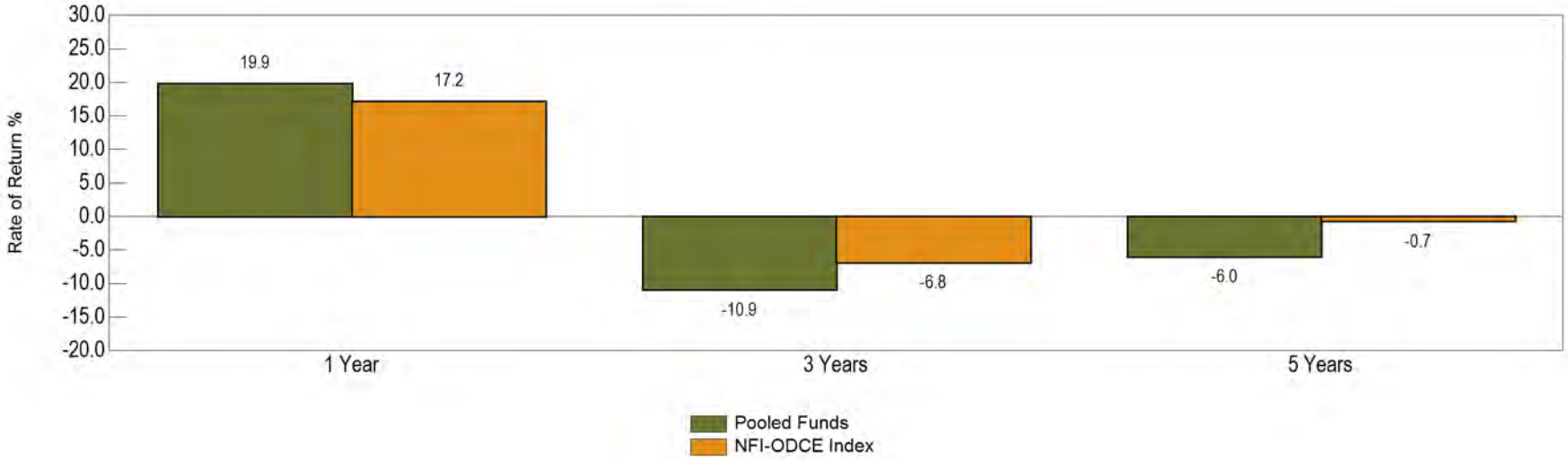

## Quarterly Excess Performance



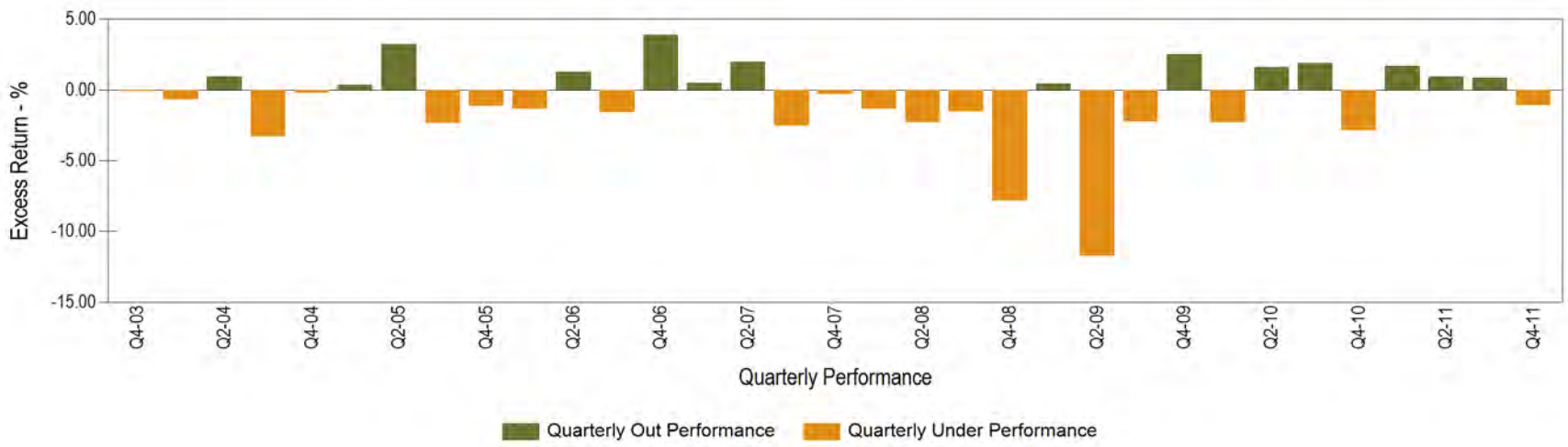
# Pooled Funds

Benchmark: NFI-ODCE Index

## Return Summary



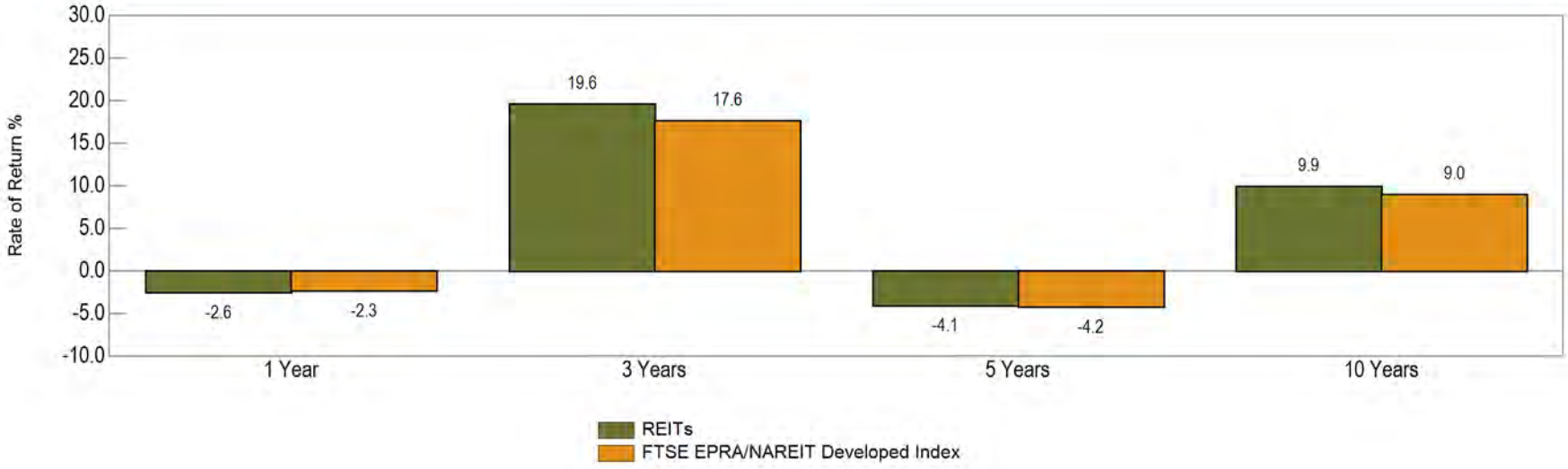

## Quarterly Excess Performance



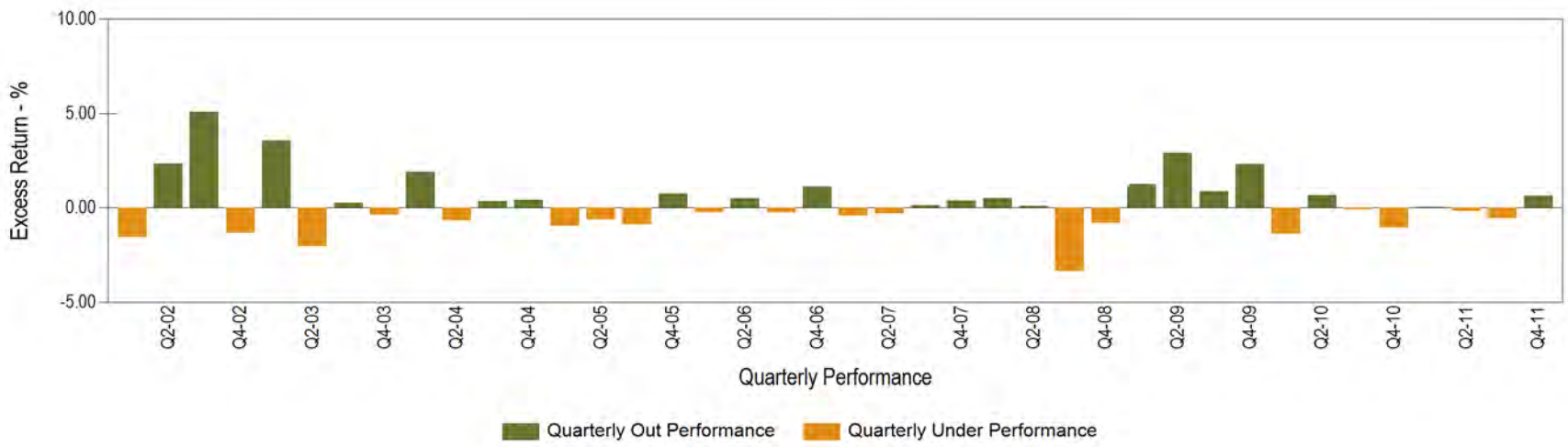
# REITs

Benchmark: FTSE EPRA/NAREIT Developed Index

## Return Summary




## Quarterly Excess Performance



# Real Estate Pooled Funds Time-Weighted Performance
## Performance Measures Through December 31, 2011

| Name | Inception Date | Commitment | Net Paid in Cap. | Net Asset Value | Since Inception Managed Return |
|---|---|---|---|---|---|
| **Pooled Funds** | | | | | |
| Beacon Capital SP Fund VI | Aug-07 | $100,000,000 | $82,019,972 | $42,433,649 | -20.7% |
| Black Rock Granite Fund | Aug-03 | $150,000,000 | $142,234,901 | $136,742,452 | 0.9% |
| Blackrock Retail Opportunity Fund | Nov-07 | $60,000,000 | $39,778,914 | $16,030,880 | -41.5% |
| Blackstone Real Estate Partners VI | Sep-07 | $200,000,000 | $180,614,821 | $222,854,993 | -1.2% |
| Diamond Property Fund | Aug-06 | $100,000,000 | $99,216,065 | $36,746,896 | -16.6% |
| Enhanced Property Fund | Jun-07 | $100,000,000 | $95,146,377 | $60,387,939 | -8.3% |
| Hines US Office Value Added Fund II | Sep-07 | $135,437,699 | $123,221,844 | $42,013,085 | -31.6% |
| JP Morgan Pooled Fund | Sep-03 | $250,000,000 | $209,821,658 | $275,979,920 | 6.5% |
| JP Morgan Special Situation Fund | Dec-07 | $150,000,000 | $149,010,997 | $100,526,329 | -9.0% |
| Prime Property Fund | Jun-06 | $250,000,000 | $228,709,213 | $236,068,478 | 1.3% |
| Principal Financial Group Pooled Fund | Oct-03 | $175,000,000 | $148,379,314 | $195,527,334 | 4.5% |
| Prudential PRISA | Apr-05 | $250,000,000 | $228,057,999 | $223,949,651 | 2.0% |
| Prudential PRISA Fund II | Sep-07 | $145,000,000 | $138,560,282 | $114,483,652 | -8.4% |
| Prudential PRISA III | Jan-08 | $150,000,000 | $146,003,544 | $139,747,802 | -13.0% |
| Rockpoint Real Estate Fund III, L.P.* | Jan-08 | $100,000,000 | $53,175,442 | $73,600,734 | -71.0% |
| RREEF America REIT Pooled Fund | Jul-03 | $250,000,000 | $209,715,543 | $265,561,266 | 4.4% |
| UBS Pooled Fund | Jul-03 | $200,000,000 | $124,457,843 | $212,625,722 | 6.1% |
| **Total Pooled Funds** | | **$2,765,437,699** | **$2,398,124,729** | **$2,395,280,783** | **1.68%** |

* The since inception IRR is 20.2%.

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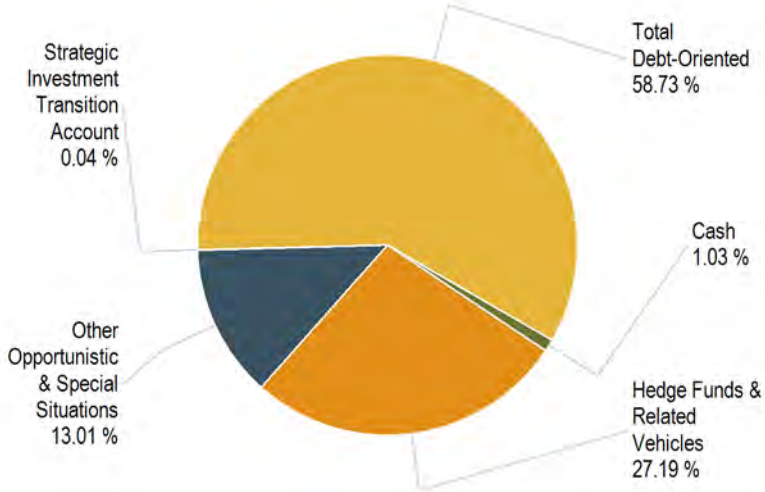
# Strategic Investments

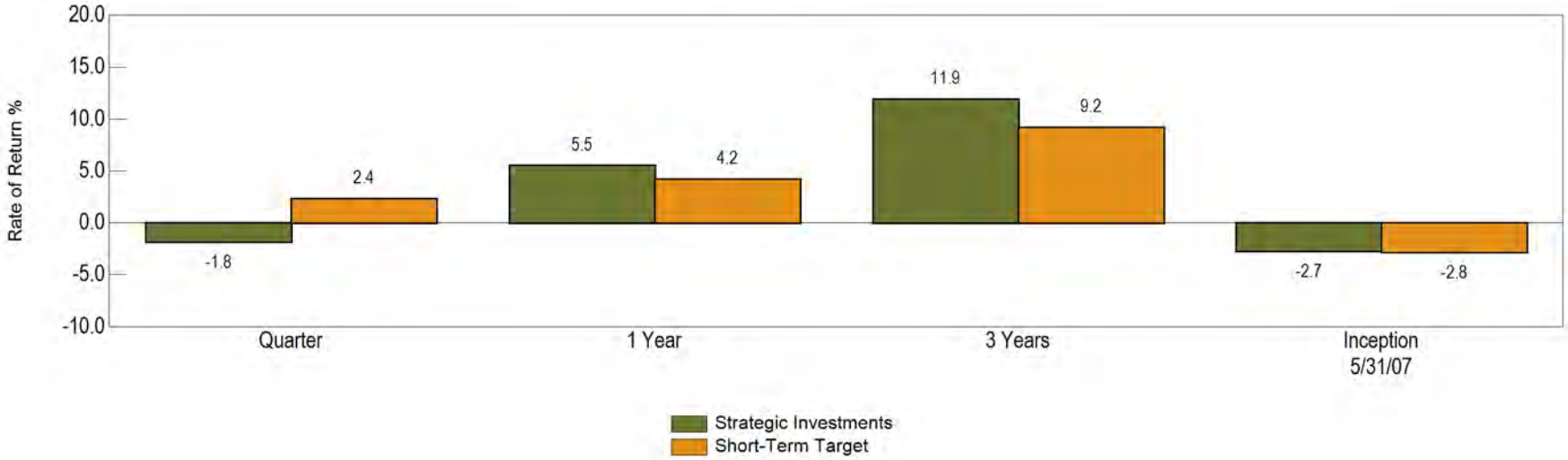
# Overview

Benchmark: Short-Term Target

## Current Allocation



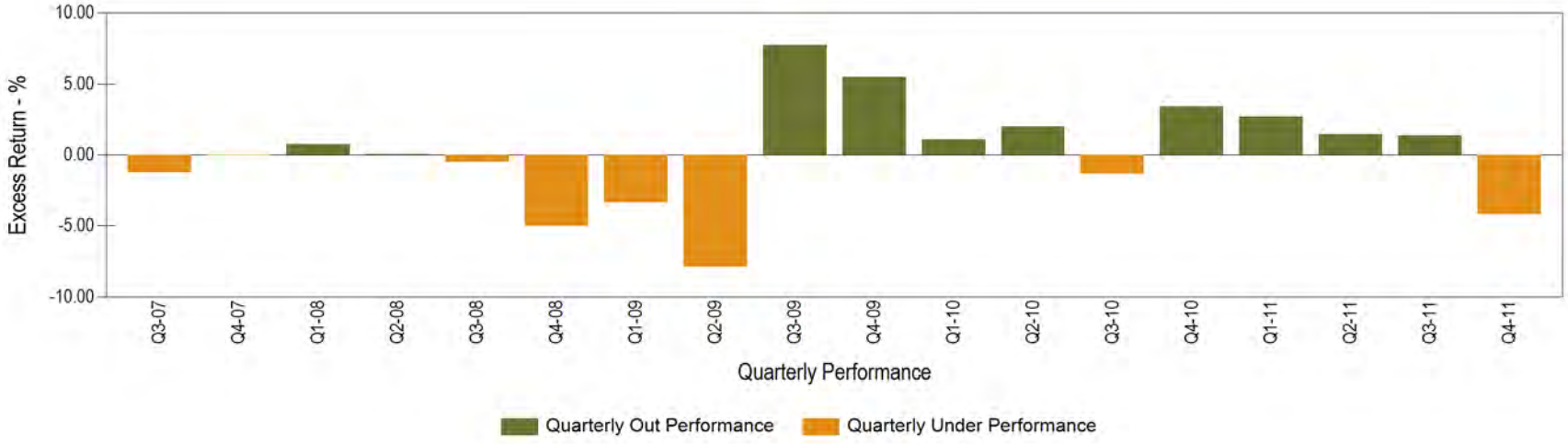

## Return Summary



# Overview

Benchmark: Short-Term Target

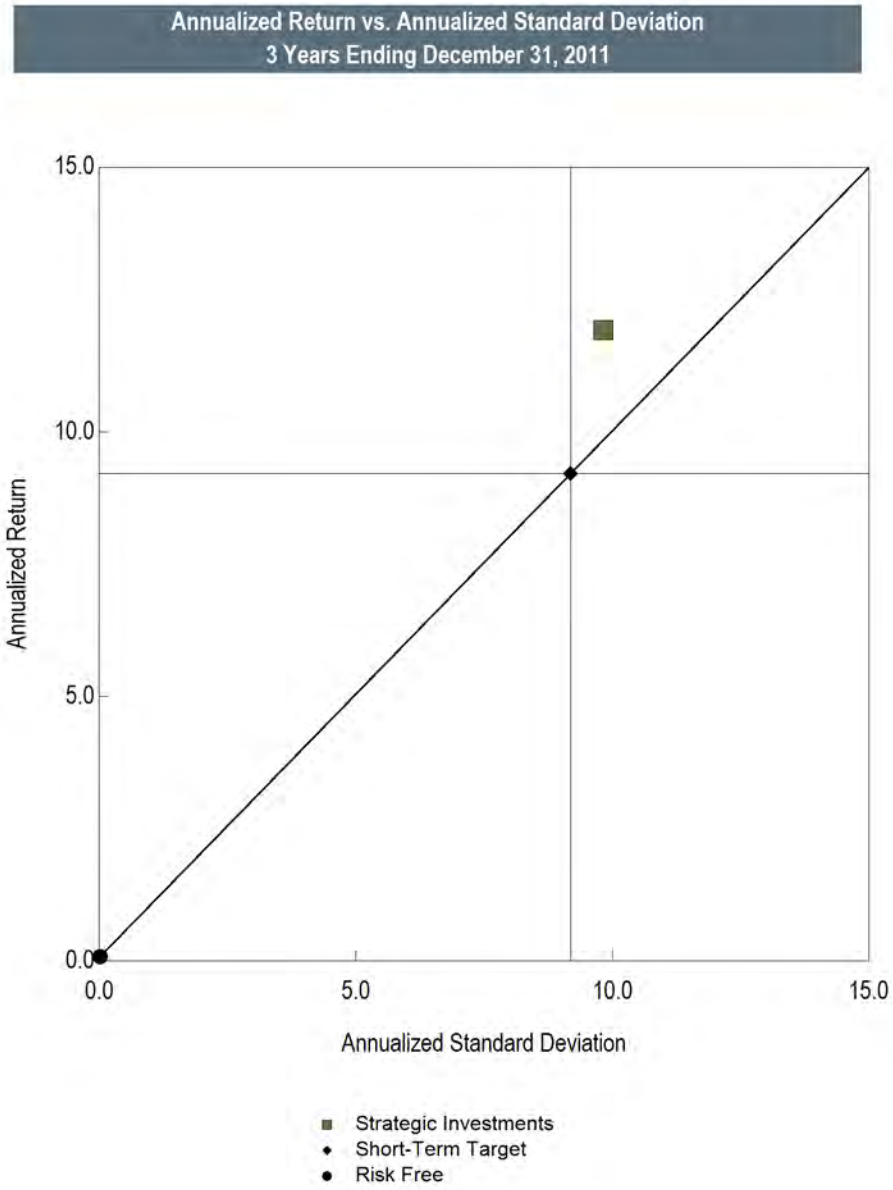
## Quarterly Excess Performance




## Ratio of Cumulative Wealth
## 4 Years 7 Months Ending December 31, 2011

# Risk Profile

Benchmark: Short-Term Target



## Strategic Investments Dollar-Weighted Performance
## Cumulative Performance Measures Since Inception Through December 31, 2011

| Name | Years Since Inception | Commitment | Net Paid In Cap. | Net Asset Value | Managed Return |
|---|---|---|---|---|---|
| Green Credit Investors | CLOSED | N/A | $14,344.42 | $0.00 | N/A |
| PCG Special Situations Partners, L.P. | 8.38 | 150,000,000 | $43,827,283 | $89,270,783 | 5.6% |
| Goldman Sachs Distressed Opportunities, L.P. | 7.48 | 150,000,000 | $79,328,971 | $89,600,986 | 1.5% |
| Special Situation Partners II | 4.68 | 100,000,000 | $66,419,730 | $80,539,928 | 4.4% |
| OCM Opportunities Fund VIIb | 4.21 | 50,000,000 | $14,192,805 | $36,048,608 | 15.6% |
| TAC 2007 (TPG Credit Fund) | 4.05 | 321,326,676 | $89,308,031 | $84,352,031 | -0.8% |
| Apollo Credit Liquidity Fund | 4.04 | 238,233,051 | $84,548,128 | $115,205,645 | 5.3% |
| Blackstone Credit Liquidity Partners, L.P. | 4.03 | 250,000,000 | $35,257,143 | $110,657,982 | 13.5% |
| Morgan Stanley Mezzanine Partners pooled fund | 4.01 | 177,500,000 | $33,197,489 | $8,111,911 | -25.3% |
| Wayzata Opportunities Fund II | 4.00 | 50,000,000 | $27,906,957 | $48,952,999 | 13.5% |
| Providence TMT Special Situation Fund | 3.69 | 150,000,000 | $100,158,396 | $154,738,908 | 12.5% |
| GSO Capital Opportunities Fund | 3.40 | 200,000,000 | $110,543,617 | $167,704,385 | 15.2% |
| Carlyle Mezzanine Partners II, L.P. | 3.40 | 150,000,000 | $55,592,021 | $62,287,227 | 3.3% |
| ABRY Advanced Securities Fund | 3.29 | 150,000,000 | $86,274,652 | $110,549,539 | 9.2% |
| TCW Crescent Mezzanine Partners V | 3.15 | 150,000,000 | $80,960,497 | $92,107,908 | 7.0% |
| Tricon IX | 3.13 | 105,000,000 | $67,451,097 | $78,628,240 | 6.8% |
| Blackrock Carbon Capital III | 3.00 | 100,000,000 | $87,088,662 | $96,692,941 | 6.5% |
| Square Mile Partners III | 2.99 | 100,000,000 | $69,774,236 | $75,516,872 | 4.1% |
| VSS Structured Capital II | 2.58 | 75,000,000 | $27,959,701 | $31,464,948 | 7.4% |
| Principal RE Debt (SBAF Mortgage Fund) | 2.10 | 300,000,000 | $191,422,496 | $210,371,948 | 10.6% |
| Falcon Strategic Partners III | 2.55 | 75,000,000 | $48,840,436 | $61,352,426 | 14.4% |
| Levine Leichtman Capital Partners IV | 2.13 | 100,000,000 | $39,197,081 | $54,691,396 | 22.2% |
| Varde Fund X, L.P. | 1.67 | 100,000,000 | $80,000,000 | $81,258,593 | 1.6% |
| Oaktree Opportunities Fund VIII, L.P. | 1.66 | 100,000,000 | $99,710,683 | $100,029,381 | 0.3% |
| Audax Credit Opportunities | 1.47 | 200,000,000 | $176,043,864 | $185,444,362 | 6.8% |
| Bayview Opportunity Master Fund II b | 1.45 | 100,000,000 | $92,893,231 | $96,376,857 | 5.3% |
| ABRY Senior Equity III, L.P. | 1.40 | 60,000,000 | $40,306,896 | $41,141,960 | 3.5% |
| Blackstone/GSO Capital Solutions Fund | 1.38 | 100,000,000 | $59,668,903 | $63,972,099 | 9.3% |
| Providence TMT Debt Opportunity Fund II, L.P. | 1.31 | 100,000,000 | $48,049,270 | $48,015,821 | -0.1% |
| CVI Credit Value Fund A | 1.05 | 100,000,000 | $94,439,378 | $93,387,641 | -2.0% |
| ABRY Advanced Securities Fund II | 0.66 | 150,000,000 | $45,157,066 | $36,344,511 | **** |
| Oaktree Opportunities Fund VIIIb, L.P. | 0.36 | 50,000,000 | $10,000,000 | $9,681,597 | **** |
| GSO Capital Opportunities Fund II | 0.16 | 150,000,000 | $21,053,233 | $21,053,274 | **** |
| Colony Distressed Credit Fund II | 0.11 | 75,000,000 | $15,354,511 | $15,354,511 | **** |
| **Strategic Investments Debt-Oriented** | | | **$2,221,940,809** | **$2,650,908,217** | **5.9%** |
| | | | | | |
| CVI Global Value Fund A-Class P | 3.16 | 250,000,000 | $175,613,376 | $323,426,033 | 20.5% |
| GI Partners III | 2.94 | 100,000,000 | $66,379,118 | $76,235,222 | 9.8% |
| Florida Growth Fund | 2.49 | 250,000,000 | $113,229,476 | $131,079,695 | 13.4% |
| KV Partners | 1.45 | 250,000,000 | $197,952,816 | $142,691,299 | -26.8% |
| Airline Credit Opportunities II | 1.04 | 75,000,000 | $27,773,298 | $30,169,578 | 11.7% |
| Starboard Value and Opportunity Fund | 0.66 | 125,000,000 | $125,000,000 | $125,202,561 | **** |
| Florida Growth Fund Tranche II | 0.24 | 250,000,000 | $370,131 | $36,798 | **** |

****IRR returns less than one year are not reported

| Strategic Investments - Hedge Fund and Related Vehicles<br>Time-Weighted Returns Since Inception Through December 31, 2011 | | | | |
|---|---|---|---|---|
| Name | Inception Date | Commitment | Net Asset Value | Since Inception Managed Return |
| Anchorage Capital Fund | 10/03/2011 | 100,000,000 | $99,527,756 | -0.5% |
| Cevian Capital II | 04/01/2010 | 150,000,000 | $116,673,000 | 9.2% |
| Gruss Global Investors Fund | 07/01/2011 | 150,000,000 | $147,513,166 | -1.7% |
| Highline Capital Partners | 04/01/2011 | 100,000,000 | $144,678,987 | -3.5% |
| King Street Capital Fund | 06/01/2011 | 150,000,000 | $144,478,447 | -5.4% |
| KV Partners | 07/20/2010 | 100,000,000 | $142,691,299 | -17.7% |
| Mason Capital Fund | 04/01/2011 | 100,000,000 | $151,729,666 | 3.8% |
| P2 Capital Fund | 09/29/2010 | 125,000,000 | $111,070,793 | 8.8% |
| Starboard Value and Opportunity Fund | 05/05/2011 | 100,000,000 | $125,202,561 | -0.7% |
| Taconic Opportunity Fund | 05/31/2011 | 100,000,000 | $143,311,921 | -6.7% |

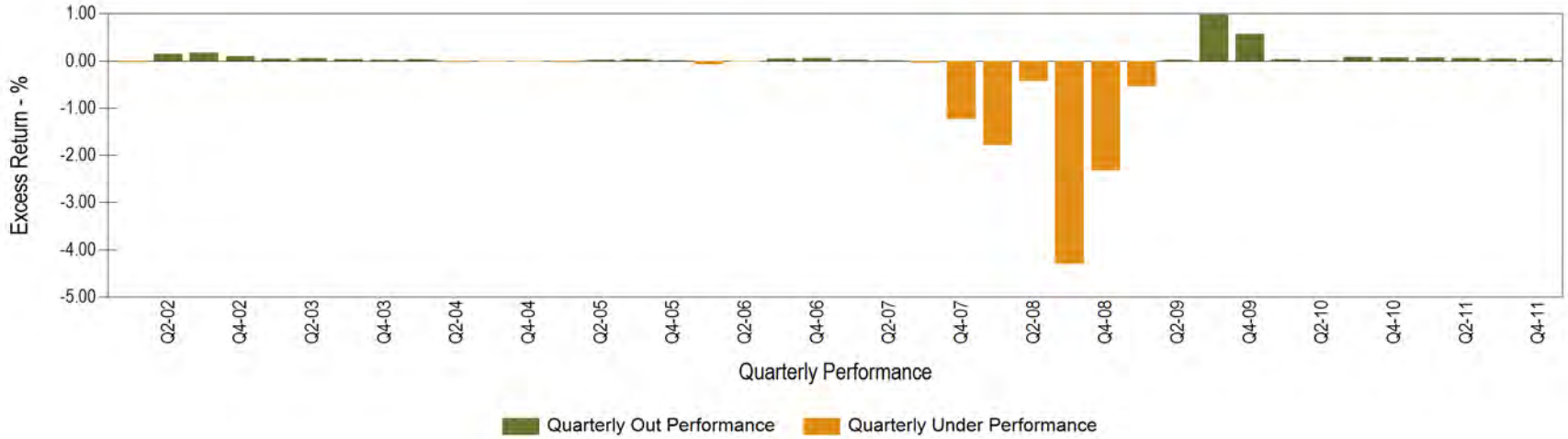
# Cash

# Overview

Benchmark: Asset Class Target

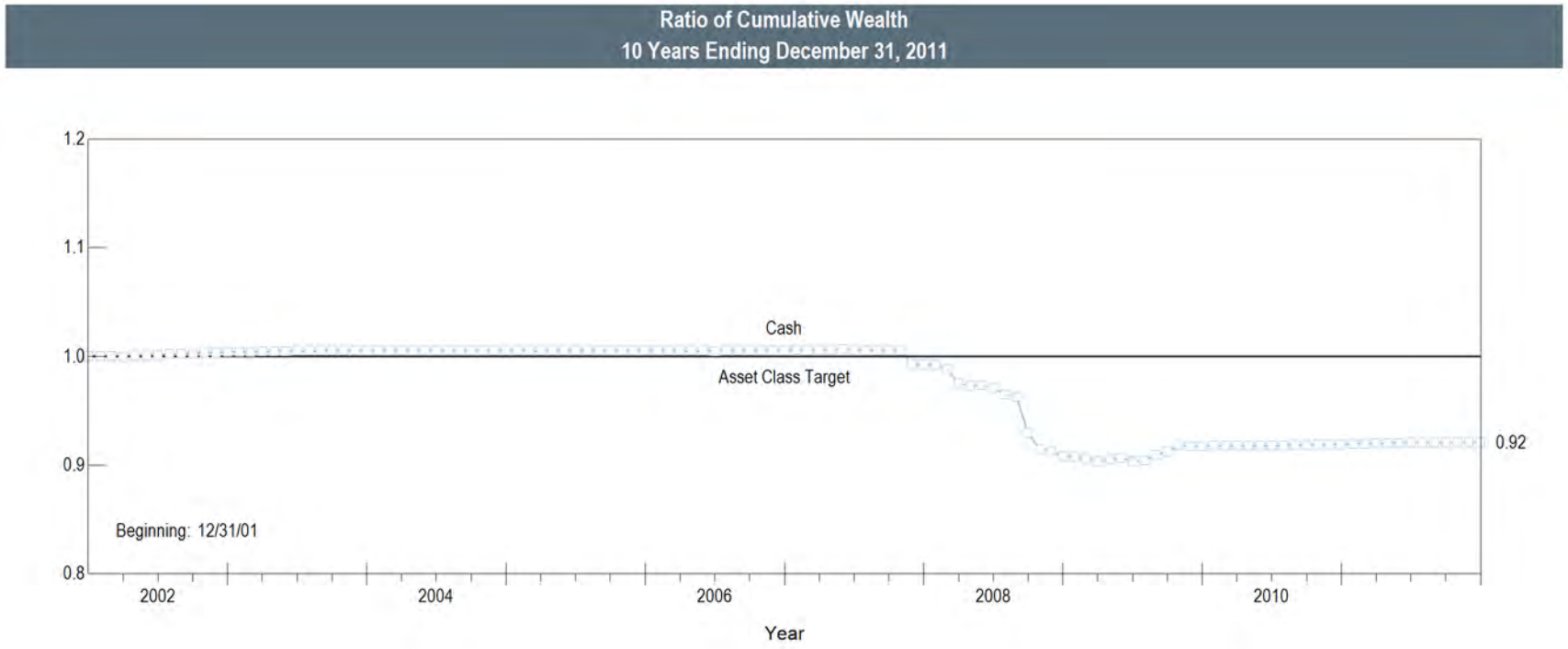
## Return Summary

## Quarterly Excess Performance



# Overview

Benchmark: Asset Class Target



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# Appendix

# Securities Lending

**FRS Pension Plan**

| | | | LOANS | | |
|---|---|---|---|---|---|
| Lending Agent | Lendable Base | Market Value on Loan | % on Loan | Intrinsic Market Value on Loan # | % Intrinsic on Loan |
| Bank of New York Mellon | $59,297,945,806 | $1,914,051,513 | 3.23% | $1,899,134,219 | 99.22% |
| Deutsche Bank | $21,698,455,990 | $1,883,833,037 | 8.68% | $1,883,256,845 | 99.97% |
| ClearLend (formerly Wachovia) | --- | --- | --- | --- | --- |
| Total FRS Pension Plan | $80,996,401,796 | $3,797,884,550 | 4.69% | $3,782,391,064 | 99.59% |

| | | | REINVESTMENT |
|---|---|---|---|
| Lending Agent | Book Value | Market Value | Unrealized Gain/(Loss) |
| Bank of New York Mellon | $2,001,716,151 | $1,888,325,481 | ($113,390,670) |
| Deutsche Bank | $1,930,363,556 | $1,927,979,989 | ($2,383,567) |
| ClearLend (formerly Wachovia) | --- | --- | --- |
| Total FRS Pension Plan | $3,932,079,707 | $3,816,305,470 | ($115,774,237) |

# Intrinsic value loans are those made at or below the federal funds rate.

# Appendix

| Returns Of The Major Capital Markets | | | | | | |
|---|---|---|---|---|---|---|
| | Fourth | Annualized Periods Ending 12/31/11 | | | | |
| | Quarter | 1-Year | 3-Year | 5-Year | 10-Year | 15-Year |
| **Domestic Stock Indices:** | | | | | | |
| Dow Jones US Total Stock Index | 12.1 | 1.1 | 15.2 | 0.2 | 3.9 | 5.8 |
| S&P 500 Index | 11.8 | 2.1 | 14.1 | -0.3 | 2.9 | 5.5 |
| Russell 3000 Index | 12.1 | 1.0 | 14.9 | 0.0 | 3.5 | 5.7 |
| Russell 1000 Value Index | 13.1 | 0.4 | 11.5 | -2.6 | 3.9 | 6.3 |
| Russell 1000 Growth Index | 10.6 | 2.6 | 18.0 | 2.5 | 2.6 | 4.5 |
| Russell MidCap Value Index | 13.4 | -1.4 | 18.2 | 0.0 | 7.7 | 8.9 |
| Russell MidCap Growth Index | 11.2 | -1.7 | 22.1 | 2.4 | 5.3 | 6.5 |
| Russell 2000 Value Index | 16.0 | -5.5 | 12.4 | -1.9 | 6.4 | 8.0 |
| Russell 2000 Growth Index | 15.0 | -2.9 | 19.0 | 2.1 | 4.5 | 3.9 |
| **Domestic Bond Indices:** | | | | | | |
| Barclays Capital Aggregate Index | 1.1 | 7.8 | 6.8 | 6.5 | 5.8 | 6.3 |
| Barclays Capital Govt/Credit Index | 1.2 | 8.7 | 6.6 | 6.5 | 5.9 | 6.4 |
| Barclays Capital Long Govt/Credit Index | 2.6 | 22.5 | 11.2 | 9.7 | 8.5 | 8.4 |
| Barclays Capital 1-3 Year Govt/Credit Index | 0.2 | 1.6 | 2.7 | 4.0 | 3.6 | 4.6 |
| Barclays Capital U.S. MBS Index | 0.9 | 6.2 | 5.8 | 6.5 | 5.7 | 6.3 |
| Barclays Capital High Yield Index | 6.5 | 5.0 | 24.1 | 7.5 | 8.9 | 6.9 |
| Barclays Capital Universal Index | 1.4 | 7.4 | 7.7 | 6.4 | 6.0 | 6.4 |
| **Real Estate Indices:** | | | | | | |
| NCREIF Property Index | 3.0 | 14.3 | 2.4 | 3.1 | 8.1 | 9.4 |
| NCREIF ODCE Index | 2.7 | 15.0 | -2.7 | -1.1 | 5.2 | 7.3 |
| Dow Jones Real Estate Securities Index | 15.3 | 8.9 | 21.7 | -2.2 | 10.1 | 9.0 |
| FTSE NAREIT US Real Estate Index | 15.3 | 8.3 | 21.0 | -1.4 | 10.2 | 8.9 |
| **Foreign/Global Stock Indices:** | | | | | | |
| MSCI All Country World Index | 7.2 | -7.3 | 12.0 | -1.9 | 4.2 | 4.5 |
| MSCI All Country World IMI | 7.2 | -7.9 | 12.8 | -1.6 | 4.9 | 4.6 |
| MSCI All Country World ex-U.S. Index | 3.7 | -13.7 | 10.7 | -2.9 | 6.3 | 4.4 |
| MSCI All Country World ex-U.S. IMI | 3.3 | -14.3 | 11.5 | -2.7 | 6.9 | 4.3 |
| MSCI All Country World ex-U.S. Small Cap Index | 0.4 | -18.5 | 18.5 | -1.7 | 10.6 | 5.3 |
| MSCI EAFE Index | 3.3 | -12.1 | 7.6 | -4.7 | 4.7 | 3.4 |
| MSCI EAFE IMI | 2.9 | -12.6 | 8.4 | -4.6 | 5.3 | 3.6 |
| MSCI EAFE Index (in local currency) | 4.1 | -12.2 | 4.7 | -6.6 | 0.7 | 2.3 |
| MSCI Emerging Markets IMI | 3.8 | -19.5 | 20.7 | 2.6 | 13.8 | 5.1 |
| **Foreign Bond Indices:** | | | | | | |
| Citigroup World Gov't Bond Index | -0.5 | 5.2 | 4.9 | 7.2 | 8.4 | 5.5 |
| Citigroup Hedged World Gov't Bond Index | 0.6 | 4.1 | 3.0 | 4.3 | 4.4 | 5.7 |
| **Cash Equivalents:** | | | | | | |
| Treasury Bills (30-Day) | 0.0 | 0.0 | 0.1 | 1.1 | 1.5 | 2.5 |
| EnnisKnupp STIF Index | 0.0 | 0.2 | 0.4 | 1.8 | 2.2 | 3.3 |
| **Inflation Index:** | | | | | | |
| Consumer Price Index | -0.5 | 3.0 | 2.4 | 2.3 | 2.5 | 2.4 |

# Historical Policy Allocation

| | Global Equity (%) | Domestic Equity (%) | Foreign Equity (%) | Global Equity Legacy (%) | Strategic Investments (%) | Fixed Income (%) | Real Estate (%) | Private Equity (%) | High Yield (%) | Cash (%) |
|---|---|---|---|---|---|---|---|---|---|---|
| 12/31/2011 | 56.8 | -- | -- | -- | 4.1 | 26.0 | 7.2 | 4.9 | -- | 1.0 |
| 09/30/2011 | 57.6 | -- | -- | -- | 3.7 | 26.0 | 6.9 | 4.7 | -- | 1.0 |
| 06/30/2011 | 59.1 | -- | -- | -- | 3.2 | 26.0 | 6.4 | 4.3 | -- | 1.0 |
| 03/31/2011 | 60.0 | -- | -- | -- | 2.6 | 26.0 | 6.3 | 4.0 | -- | 1.0 |
| 12/31/2010 | 59.6 | -- | -- | -- | 2.9 | 26.0 | 6.3 | 4.3 | -- | 1.0 |
| 09/30/2010 | 58.1 | -- | -- | -- | 4.2 | 26.0 | 6.5 | 4.2 | -- | 1.0 |
| 06/30/2010 | -- | 36.5 | 19.2 | -- | 3.9 | 26.9 | 6.7 | 3.8 | 1.9 | 1.0 |
| 03/31/2010 | -- | 36.6 | 19.3 | -- | 3.7 | 27.0 | 6.7 | 3.9 | 1.9 | 1.0 |
| 12/31/2009 | -- | 36.6 | 19.3 | -- | 3.6 | 27.0 | 6.7 | 3.9 | 1.9 | 1.0 |
| 09/30/2009 | -- | 36.7 | 19.3 | -- | 3.5 | 27.0 | 6.8 | 3.9 | 1.9 | 1.0 |
| 06/30/2009 | -- | 36.7 | 19.3 | -- | 3.4 | 27.1 | 6.8 | 3.9 | 1.9 | 1.0 |
| 03/31/2009 | -- | 36.6 | 19.3 | -- | 3.6 | 27.0 | 6.8 | 3.9 | 1.9 | 1.0 |
| 12/31/2008 | -- | 36.5 | 19.2 | -- | 4.0 | 26.9 | 6.7 | 3.8 | 1.9 | 1.0 |
| 09/30/2008 | -- | 36.4 | 19.1 | -- | 4.3 | 26.8 | 6.7 | 3.8 | 1.9 | 1.0 |
| 06/30/2008 | -- | 36.4 | 19.2 | -- | 4.2 | 26.8 | 6.7 | 3.8 | 1.9 | 1.0 |
| 03/31/2008 | -- | 36.4 | 19.1 | -- | 4.5 | 26.7 | 6.7 | 3.8 | 1.8 | 1.0 |
| 12/31/2007 | -- | 37.2 | 18.7 | -- | 4.5 | 26.7 | 6.7 | 3.8 | 1.4 | 1.0 |
| 09/30/2007 | -- | 38.1 | 17.8 | -- | 4.4 | 26.8 | 6.7 | 3.8 | 1.4 | 1.0 |
| 06/30/2007 | -- | 41.6 | 14.4 | -- | 4.4 | 26.8 | 6.7 | 3.8 | 1.4 | 1.0 |
| 03/01/04 - 03/31/04 | -- | 49.0 | 14.0 | 3.0 | -- | 21.0 | 7.0 | 5.0 | -- | 1.0 |
| 02/02/04 - 02/29/04 | -- | 49.0 | 14.0 | 3.0 | -- | 21.4 | 6.7 | 4.9 | -- | 1.0 |
| 01/01/04 - 02/01/04 | -- | 50.0 | 14.0 | 2.0 | -- | 21.8 | 6.4 | 4.8 | -- | 1.0 |
| 12/01/03 - 12/31/03 | -- | 50.0 | 14.0 | 2.0 | -- | 22.2 | 6.1 | 4.7 | -- | 1.0 |
| 11/03/03 - 11/30/03 | -- | 50.5 | 13.5 | 2.0 | -- | 22.6 | 5.8 | 4.6 | -- | 1.0 |
| 10/29/03 - 11/02/03 | -- | 50.5 | 13.5 | 2.0 | -- | 23.0 | 5.5 | 4.5 | -- | 1.0 |
| 10/01/03 - 10/28/03 | -- | 51.0 | 13.0 | 2.0 | -- | 23.0 | 5.5 | 4.5 | -- | 1.0 |
| 09/01/03 - 09/30/03 | -- | 52.5 | 12.5 | 1.0 | -- | 23.4 | 5.2 | 4.4 | -- | 1.0 |
| 08/01/03 - 08/31/03 | -- | 52.5 | 12.5 | 1.0 | -- | 23.8 | 4.9 | 4.3 | -- | 1.0 |
| 07/01/03 - 07/31/03 | -- | 52.5 | 12.5 | 1.0 | -- | 24.2 | 4.6 | 4.2 | -- | 1.0 |
| 06/02/03 - 06/30/03 | -- | 52.5 | 12.5 | 1.0 | -- | 24.6 | 4.3 | 4.1 | -- | 1.0 |
| 04/01/01 - 06/01/03 | -- | 54.0 | 12.0 | 0.0 | -- | 25.0 | 4.0 | 4.0 | -- | 1.0 |
| 10/31/99 - 03/31/01 | -- | 55.5 | 12.0 | 0.0 | -- | 25.0 | 4.0 | 2.5 | -- | 1.0 |
| 03/31/95 - 10/31/99 | -- | 61.0 | 8.0 | 0.0 | -- | 26.0 | 4.0 | 0.0 | -- | 1.0 |
| 09/30/94 - 03/31/95 | -- | 59.0 | 8.0 | 0.0 | -- | 24.0 | 8.0 | 0.0 | -- | 1.0 |
| 06/30/93 - 09/30/94 | -- | 59.0 | 3.0 | 0.0 | -- | 29.0 | 8.0 | 0.0 | -- | 1.0 |
| 11/30/88 - 06/30/93 | -- | 55.0 | 0.0 | 0.0 | -- | 36.0 | 8.0 | 0.0 | -- | 1.0 |
| 12/31/87 - 11/30/88 | -- | 50.0 | 5.0 | 0.0 | -- | 36.5 | 7.5 | 0.0 | -- | 1.0 |
| 12/31/86 - 12/31/87 | -- | 50.0 | 5.0 | 0.0 | -- | 35.5 | 7.5 | 0.0 | -- | 2.0 |
| 12/31/84 - 12/31/86 | -- | 48.0 | 0.0 | 0.0 | -- | 40.0 | 10.0 | 0.0 | -- | 2.0 |

# Appendix

**Total FRS Assets**

Performance Benchmark - A combination of the Global Equity Target, the Barclays Capital Aggregate Bond Index, the Private Equity Target Index, the Real Estate Investments Target Index, the Strategic Investments Target Benchmark, and the iMoneyNet First Tier Institutional Money Market Funds Net Index. The short-term target policy allocations to the Strategic Investments, Real Estate and Private Equity asset classes are floating and based on the actual average monthly balance of the Global Equity asset class. Prior to July 2010, the Performance Benchmark was a combination of the Russell 3000 Index, the Foreign Equity Target Index, the Strategic Investments Target Benchmark, the Barclays Capital Aggregate Bond Index, the Real Estate Investments Target Index, the Private Equity Target Index, the Barclays Capital U.S. High Yield Ba/B 2% Issuer Capped Index, and the iMoneyNet First Tier Institutional Money Market Funds Gross Index. During this time, the short-term target policy allocations to Strategic Investments, Real Estate and Private Equity asset classes were floating and based on the actual average monthly balance of the Strategic Investments, Real Estate and Private Equity asset classes. The target weights shown for Real Estate and Private Equity were the allocations that the asset classes were centered around. The actual target weight floated around this target month to month based on changes in asset values.

**Total Global Equity**

Performance Benchmark - A custom version of the MSCI All Country World Investable Market Index, adjusted to exclude companies divested under the provisions of the Protecting Florida's Investments Act (PFIA).

**Total Domestic Equities**

Performance Benchmark - The Russell 3000 Index. Prior to July 1, 2002, the benchmark was the Wilshire 2500 Stock Index. Prior to January 1, 2001, the benchmark was the Wilshire 2500 Stock Index ex-Tobacco. Prior to May 1, 1997, the benchmark was the Wilshire 2500 Stock Index. Prior to September 1, 1994, the benchmark was the S&P 500 Stock Index.

**Total Foreign Equities**

Performance Benchmark - A custom version of the MSCI ACWI ex-U.S. Investable Market Index adjusted to exclude companies divested under the PFIA. Prior to April 1, 2008, it was the MSCI All Country World Index ex-U.S. Investable Market Index. Prior to September 24, 2007, the target was the MSCI All Country World Ex-U.S. Free Index. Prior to November 1, 1999, the benchmark was 85% of the MSCI Europe, Australasia and Far East (EAFE) Foreign Stock Index and 15% of the IFCI Emerging Markets Index with a half weight in Malaysia. Prior to March 31, 1995, the benchmark was the EAFE Index.

**Total Global Equities**

Performance Benchmark - Aggregated based on each underlying manager's individual benchmark. The calculation accounts for the actual weight and the benchmark return. The benchmarks used for the underlying managers include both the MSCI FSB All Country World ex-Sudan ex-Iran Net Index and MSCI FSB All Country World ex-Sudan ex-Iran Net Investable Market Index (IMI).

**Total Fixed Income**

Performance Benchmark - The Barclays Capital U.S. Aggregate Bond Index. Prior to June 1, 2007, it was the Fixed Income Management Aggregate (FIMA). Prior to July 1, 1999, the benchmark was the Florida High Yield Extended Duration Index. Prior to July 31, 1997, the benchmark was the Florida Extended Duration Index. Prior to July 1, 1989, the Salomon Brothers Broad Investment-Grade Bond Index was the benchmark. For calendar year 1985, the performance benchmark was 70% Shearson Lehman Extended Duration and 30% Salomon Brothers Mortgage Index.

**Total Private Equity**

Performance Benchmark - The domestic equities target index return (Russell 3000 Index) plus a fixed premium return of 300 basis points per annum. Prior to July 1, 2010, it was the domestic equities target index return plus a fixed premium return of 450 basis points per annum. Prior to November 1, 1999, Private Equities was part of the Domestic Equities asset class and its benchmark was the domestic equities target index return plus 750 basis points.

**Total Real Estate**

Performance Benchmark - A combination of 90% of the NCREIF ODCE Index, net of fees, and 10% of the FTSE EPRA/NAREIT Developed Index, net of fees. Prior to July 1, 2010, it was a combination of 90% of the NCREIF ODCE Index, gross of fees, and 10% of the Dow Jones U.S. Select RESI. Prior to June 1, 2007, it was the Consumer Price Index plus 450 basis points annually. Prior to July 1, 2003, the benchmark was the Dow Jones U.S. Select Real Estate Securities Index Un-Levered. Prior to November 1, 1999, the benchmark was the Russell-NCREIF Property Index.

**Total Strategic Investments**

Performance Benchmark - Long-term, 5% plus the contemporaneous rate of inflation or CPI. Short-term, a weighted aggregation of individual portfolio level benchmarks.

**Total Cash**

Performance Benchmark - The iMoneyNet First Tier Institutional Money Market Funds Net Index. Prior to July 1, 2010, it was the iMoneyNet First Tier Institutional Money Market Funds Gross Index. Prior to June 1, 2007, it was the return of the Merrill Lynch 90-Day (Auction Average) Treasury Bill Yield Index.

## Description of Benchmarks

**Barclays Capital Aggregate Bond Index** - A market value-weighted index consisting of government bonds, SEC-registered corporate bonds and mortgage-related and asset-backed securities with at least one year to maturity and an outstanding par value of $200 million or greater. The index is a broad measure of the performance of the investment-grade U.S. fixed income market.

**Consumer Price Index (CPI)** - The CPI, an index consisting of a fixed basket of goods bought by the typical consumer and used to measure consumer inflation.

**FTSE EPRA/NAREIT Developed Index** - Designed to represent general trends in eligible real estate equities worldwide. Relevant real estate activities are defined as the ownership, disposure and development of income-producing real estate. This index covers the four primary core asset classes (Industrial, Retail, Office, and Apartment).

**iMoneyNet First Tier Institutional Money Market Funds Net Index** - An average of non-governmental institutional funds that do not hold any second tier securities. It includes money market mutual funds, net of fees, that invest in commercial paper, bank obligations and short-term investments in the highest ratings category and is open to corporations and fiduciaries only.

**MSCI All Country World Investable Market Index** - A free float-adjusted market capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets. This investable market index contains constituents from the large, mid, and small cap size segments and targets a coverage range around 99% of free-float adjusted market capitalization.

**NCREIF ODCE Property Index** - The NFI-ODCE is a capitalization-weighted, gross of fee, time-weighted return index. The index is a summation of open-end funds, which NCREIF defines as infinite-life vehicles consisting of multiple investors who have the ability to enter or exit the fund on a periodic basis, subject to contribution and/or redemption requests.

**Russell 3000 Index** - A capitalization-weighted stock index consisting of the 3,000 largest publicly traded U.S. stocks by capitalization. This represents most publicly traded, liquid U.S. stocks.

## Description of Universes

**Total Fund** - A universe comprised of 74 total fund portfolio returns, net of fees, of public defined benefit plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $736.1 billion as of quarter-end and the average market value was $17.9 billion.

**Domestic Equity** - A universe comprised of 54 total domestic equity portfolio returns, net of fees, of public defined benefit plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $223.9 billion as of quarter-end and the average market value was $5.7 billion.

**Foreign Equity** - A universe comprised of 48 total international equity portfolio returns, net of fees, of public defined benefit plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $120.6 billion as of quarter-end and the average market value was $3.5 billion.

**Fixed Income** - A universe comprised of 54 total fixed income portfolio returns, net of fees, of public defined benefit plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $204.2 billion as of quarter-end and the average market value was $5.1 billion.

**Real Estate** - A universe comprised of 13 total real-estate portfolio returns, net of fees, of public defined benefit plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $20.9 billion as of quarter-end and the average market value was $2.3 billion.

**Private Equity** - An appropriate universe for private equity is unavailable.

**Strategic Investments** - An appropriate universe for strategic investments is unavailable.

# Appendix

## Explanation of Exhibits

**Quarterly and Cumulative Excess Performance** - The vertical axis, excess return, is a measure of fund performance less the return of the primary benchmark. The horizontal axis represents the time series. The quarterly bars represent the underlying funds' relative performance for the quarter.

**Risk-Return Graph** - The horizontal axis, annualized standard deviation, is a statistical measure of risk, or the volatility of returns. The vertical axis is the annualized rate of return. As investors generally prefer less risk to more risk and always prefer greater returns, the upper left corner of the graph is the most attractive place to be. The line on this exhibit represents the risk and return tradeoffs associated with market portfolios, or index funds.

**Ratio of Cumulative Wealth Graph** - An illustration of a portfolio's cumulative, un-annualized performance relative to that of its benchmark. An upward-sloping line indicates superior fund performance versus its benchmark. Conversely, a downward-sloping line indicates underperformance by the fund. A flat line is indicative of benchmark-like performance.

**Performance Comparison - Universe Comparison** - An illustration of the distribution of returns for a particular asset class. The component's return is indicated by the circle and its performance benchmark by the triangle. The top and bottom borders represent the 5th and 95th percentiles, respectively. The solid line indicates the median while the dotted lines represent the 25th and 75th percentiles.

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Hewitt ennisknupp

An Aon Company

# State Board of Administration of Florida

# FRS Investment Plan

Fourth Quarter 2011

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# FRS Investment Plan

# Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|
| **FRS Investment Plan** | **6,642,321,806** | **100.0** | **5.2** | **--** | **0.7** | **--** | **9.7** | **--** | **1.8** | **--** |
| *Total Plan Aggregate Benchmark* | | | *5.2* | *--* | *0.9* | *--* | *9.1* | *--* | *1.1* | *--* |
| **Balanced Funds** | **2,833,352,104** | **42.7** | **4.2** | **--** | **1.4** | **--** | **8.8** | **--** | **1.4** | **--** |
| FRS Select Conservative Balanced Fund | 626,660,939 | 9.4 | 1.7 | -- | 3.9 | -- | 6.1 | -- | 3.7 | -- |
| *Conservative Balanced Fund Target Benchmark* | | | *1.8* | *--* | *4.0* | *--* | *5.8* | *--* | *3.3* | *--* |
| FRS Select Moderate Balanced Fund | 1,691,870,961 | 25.5 | 4.5 | -- | 1.2 | -- | 9.2 | -- | 1.3 | -- |
| *Moderate Balanced Fund Target Benchmark* | | | *4.6* | *--* | *1.3* | *--* | *8.8* | *--* | *0.8* | *--* |
| FRS Select Aggressive Balanced Fund | 514,820,204 | 7.8 | 6.2 | -- | -0.9 | -- | 10.0 | -- | -0.4 | -- |
| *Aggressive Balanced Fund Target Benchmark* | | | *6.3* | *--* | *-0.8* | *--* | *10.1* | *--* | *-0.6* | *--* |
| **Cash** | **921,202,884** | **13.9** | **0.1** | **1** | **0.2** | **1** | **0.3** | **14** | **1.7** | **20** |
| FRS Select Yield Plus Money Market Active Fund | 921,202,884 | 13.9 | 0.1 | 1 | 0.2 | 1 | 0.3 | 14 | 1.7 | 20 |
| *iMoneyNet 1st Tier Institutional Net Index* | | | *0.0* | *26* | *0.1* | *25* | *0.3* | *7* | *1.9* | *3* |
| **TIPS** | **288,104,372** | **4.3** | **2.5** | **--** | **13.6** | **--** | **10.4** | **--** | **8.0** | **--** |
| FRS Select TIPS Fund | 288,104,372 | 4.3 | 2.5 | 48 | 13.6 | 9 | 10.4 | 25 | 8.0 | 23 |
| *Barclays Capital US TIPS* | | | *2.7* | *8* | *13.6* | *9* | *10.4* | *26* | *8.0* | *26* |
| **Fixed Income** | **633,333,438** | **9.5** | **1.5** | **44** | **6.7** | **53** | **8.7** | **62** | **6.8** | **34** |
| FRS Select U.S. Bond Enhanced Index Fund | 148,002,354 | 2.2 | 1.0 | 88 | 7.9 | 75 | 7.0 | 96 | 6.8 | 64 |
| *Barclays Capital Aggregate Bond Index* | | | *1.1* | *88* | *7.8* | *76* | *6.8* | *97* | *6.5* | *66* |
| Pyramis Intermediate Duration Pool Fund | 74,251,707 | 1.1 | 1.0 | 79 | 5.9 | 70 | 8.3 | 67 | 5.7 | 70 |
| *Barclays Capital Int Aggregate* | | | *0.9* | *85* | *6.0* | *69* | *6.2* | *93* | *6.1* | *60* |
| FRS Select High Yield Fund | 133,251,345 | 2.0 | 5.8 | 51 | 6.0 | 10 | -- | -- | -- | -- |
| *Barclays Capital U.S. High Yield Ba-2% Issuer Cap* | | | *5.7* | *55* | *6.9* | *3* | *--* | *--* | *--* | *--* |
| PIMCO Total Return Fund | 277,828,032 | 4.2 | 2.2 | 11 | 4.0 | 91 | 8.7 | 61 | 7.9 | 9 |
| *Barclays Capital Aggregate Bond Index* | | | *1.1* | *68* | *7.8* | *17* | *6.8* | *87* | *6.5* | *44* |

# Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|
| **Domestic Equity** | **1,522,296,291** | **22.9** | **12.5** | **41** | **0.3** | **36** | **16.5** | **29** | **1.1** | **29** |
| FRS Select U.S. Stock Market Index Fund | 229,260,232 | 3.5 | 12.2 | 24 | 1.0 | 44 | 15.0 | 17 | 0.1 | 28 |
| *Russell 3000 Index* | | | *12.1* | *27* | *1.0* | *44* | *14.9* | *19* | *0.0* | *30* |
| FRS Select U.S. Large Value Stock Fund | 185,075,725 | 2.8 | 12.8 | 39 | 1.6 | 27 | 12.2 | 50 | -- | -- |
| *Russell 1000 Value Index* | | | *13.1* | *32* | *0.4* | *37* | *11.5* | *60* | -- | -- |
| QMA Mid Cap Quantitative Core Fund | 256,450,202 | 3.9 | 14.8 | 13 | 0.1 | 22 | 20.8 | 22 | 3.8 | 21 |
| *S&P 400 MidCap* | | | *13.0* | *36* | *-1.7* | *35* | *19.6* | *35* | *3.3* | *25* |
| FRS Select U.S. Large Growth Stock Active Fund | 77,940,867 | 1.2 | 8.0 | 79 | 1.2 | 25 | 17.6 | 26 | 2.7 | 24 |
| *Russell 1000 Growth Index* | | | *10.6* | *27* | *2.6* | *13* | *18.0* | *20* | *2.5* | *27* |
| Pioneer Fund | 129,522,387 | 1.9 | 11.4 | 61 | -4.2 | 82 | 11.6 | 80 | -0.8 | 63 |
| *S&P 500 Index* | | | *11.8* | *38* | *2.1* | *22* | *14.1* | *32* | *-0.3* | *36* |
| Fidelity Growth Company Fund | 278,322,925 | 4.2 | 7.8 | 81 | 0.9 | 26 | 19.9 | 11 | 4.2 | 9 |
| *Russell 3000 Growth Index* | | | *10.9* | *22* | *2.2* | *18* | *18.1* | *20* | *2.5* | *28* |
| American Beacon Small Cap Value Fund | 121,542,363 | 1.8 | 18.4 | 14 | -4.0 | 52 | 17.9 | 34 | 0.9 | 47 |
| *Russell 2000 Value Index* | | | *16.0* | *54* | *-5.5* | *63* | *12.4* | *91* | *-1.9* | *92* |
| T. Rowe Price Small Cap Stock Fund | 221,369,760 | 3.3 | 16.8 | 17 | -0.1 | 29 | 22.4 | 21 | 3.7 | 19 |
| *Russell 2000 Index* | | | *15.5* | *27* | *-4.2* | *65* | *15.6* | *85* | *0.2* | *80* |
| Fidelity Low Priced Stock Fund | 22,811,831 | 0.3 | 9.4 | 95 | 0.2 | 11 | 19.1 | 36 | 2.3 | 30 |
| *Russell 2500 Value Index* | | | *15.4* | *12* | *-3.4* | *56* | *15.5* | *77* | *-0.6* | *74* |
| **International/Global Equity** | **444,032,717** | **6.7** | **4.3** | **52** | **-11.3** | **25** | **9.6** | **44** | **-2.2** | **24** |
| FRS Select Foreign Stock Index Fund | 122,600,549 | 1.8 | 3.6 | 68 | -11.8 | 31 | 8.4 | 57 | -3.8 | 45 |
| *MSCI World ex USA* | | | *3.5* | *70* | *-12.2* | *35* | *8.5* | *57* | *-4.1* | *51* |
| American Funds New Perspective Fund | 169,420,449 | 2.6 | 6.4 | 71 | -7.4 | 48 | 13.0 | 42 | 0.9 | 17 |
| *MSCI World Index* | | | *7.6* | *43* | *-5.5* | *36* | *11.1* | *63* | *-2.4* | *54* |
| American Funds Euro-Pacific Growth Fund | 152,011,720 | 2.3 | 4.6 | 48 | -13.3 | 42 | 9.9 | 26 | -1.1 | 11 |
| *MSCI All Country World ex-U.S. Index* | | | *3.8* | *73* | *-13.3* | *43* | *8.6* | *47* | *-4.0* | *45* |

# Calendar Year Performance

| Name | 2011 (%) | Rank | 2010 (%) | Rank | 2009 (%) | Rank | 2008 (%) | Rank | 2007 (%) | Rank | 2006 (%) | Rank | 2005 (%) | Rank | 2004 (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **FRS Investment Plan** | **0.7** | **--** | **10.6** | **--** | **18.4** | **--** | **-23.2** | **--** | **7.8** | **--** | **12.4** | **--** | **7.4** | **--** | **10.6** | **--** |
| *Total Plan Aggregate Benchmark* | *0.9* | *--* | *10.2* | *--* | *16.8* | *--* | *-23.4* | *--* | *6.1* | *--* | *13.9* | *--* | *6.1* | *--* | *11.0* | *--* |
| **Balanced Funds** | **1.4** | **--** | **9.2** | **--** | **16.4** | **--** | **-22.8** | **--** | **7.7** | **--** | **13.9** | **--** | **6.9** | **--** | **11.0** | **--** |
| FRS Select Conservative Balanced Fund | 3.9 | -- | 5.3 | -- | 9.3 | -- | -7.3 | -- | 8.5 | -- | 7.1 | -- | 4.4 | -- | 6.4 | -- |
| *Conservative Balanced Fund Target Benchmark* | *4.0* | *--* | *4.8* | *--* | *8.7* | *--* | *-8.0* | *--* | *7.6* | *--* | *6.7* | *--* | *4.0* | *--* | *6.3* | *--* |
| FRS Select Moderate Balanced Fund | 1.2 | -- | 10.0 | -- | 17.2 | -- | -23.8 | -- | 7.4 | -- | 14.2 | -- | 6.8 | -- | 11.3 | -- |
| *Moderate Balanced Fund Target Benchmark* | *1.3* | *--* | *9.7* | *--* | *15.9* | *--* | *-24.5* | *--* | *7.0* | *--* | *14.7* | *--* | *6.8* | *--* | *11.4* | *--* |
| FRS Select Aggressive Balanced Fund | -0.9 | -- | 11.3 | -- | 20.9 | -- | -32.2 | -- | 8.2 | -- | 17.6 | -- | 8.6 | -- | 13.1 | -- |
| *Aggressive Balanced Fund Target Benchmark* | *-0.8* | *--* | *11.0* | *--* | *21.1* | *--* | *-32.4* | *--* | *7.5* | *--* | *18.6* | *--* | *8.5* | *--* | *14.1* | *--* |
| **Cash** | **0.2** | **1** | **0.3** | **2** | **0.3** | **41** | **2.4** | **46** | **5.4** | **2** | **5.2** | **1** | **3.5** | **1** | **1.4** | **1** |
| FRS Select Yield Plus Money Market Active Fund | 0.2 | 1 | 0.3 | 2 | 0.3 | 41 | 2.4 | 46 | 5.4 | 2 | 5.2 | 1 | 3.5 | 1 | 1.5 | 1 |
| *iMoneyNet 1st Tier Institutional Net Index* | *0.1* | *25* | *0.2* | *7* | *0.7* | *4* | *3.0* | *4* | *5.4* | *1* | *5.2* | *1* | *3.3* | *1* | *1.5* | *1* |
| **TIPS** | **13.6** | **--** | **6.4** | **--** | **11.3** | **--** | **-2.0** | **--** | **11.7** | **--** | **0.5** | **--** | **2.8** | **--** | **8.4** | **--** |
| FRS Select TIPS Fund | 13.6 | 9 | 6.4 | 28 | 11.3 | 27 | -2.0 | 46 | 11.7 | 19 | 0.5 | 34 | 2.8 | 22 | 8.4 | 35 |
| *Barclays Capital US TIPS* | *13.6* | *9* | *6.3* | *41* | *11.4* | *26* | *-2.4* | *54* | *11.6* | *20* | *0.4* | *43* | *2.8* | *20* | *8.5* | *27* |
| **Fixed Income** | **6.7** | **53** | **7.6** | **56** | **11.7** | **59** | **1.4** | **29** | **6.9** | **16** | **4.8** | **24** | **2.7** | **13** | **4.8** | **32** |
| FRS Select U.S. Bond Enhanced Index Fund | 7.9 | 75 | 6.7 | 97 | 6.5 | 59 | 5.9 | 32 | 7.1 | 18 | 4.3 | 58 | 2.5 | 57 | 4.3 | 98 |
| *Barclays Capital Aggregate Bond Index* | *7.8* | *76* | *6.5* | *97* | *5.9* | *60* | *5.2* | *33* | *7.0* | *20* | *4.3* | *57* | *2.4* | *59* | *4.3* | *98* |
| Pyramis Intermediate Duration Pool Fund | 5.9 | 70 | 7.0 | 67 | 11.9 | 58 | -1.7 | 43 | 6.0 | 42 | 4.8 | 26 | 2.2 | 48 | 3.9 | 70 |
| *Barclays Capital Int Aggregate* | *6.0* | *69* | *6.1* | *88* | *6.5* | *91* | *4.9* | *13* | *7.0* | *14* | *4.6* | *33* | *2.0* | *63* | *3.7* | *79* |
| FRS Select High Yield Fund | 6.0 | 10 | 13.6 | 77 | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- | -- |
| *Barclays Capital U.S. High Yield Ba-2% Issuer Cap* | *6.9* | *3* | *13.9* | *65* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* | *--* |
| PIMCO Total Return Fund | 4.0 | 91 | 8.7 | 33 | 13.7 | 48 | 4.7 | 15 | 8.9 | 2 | 3.9 | 82 | 2.8 | 11 | 5.0 | 27 |
| *Barclays Capital Aggregate Bond Index* | *7.8* | *17* | *6.5* | *81* | *5.9* | *92* | *5.2* | *10* | *7.0* | *15* | *4.3* | *44* | *2.4* | *30* | *4.3* | *54* |

# Calendar Year Performance

| Name | 2011 (%) | Rank | 2010 (%) | Rank | 2009 (%) | Rank | 2008 (%) | Rank | 2007 (%) | Rank | 2006 (%) | Rank | 2005 (%) | Rank | 2004 (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Domestic Equity** | **0.3** | **36** | **20.4** | **35** | **30.9** | **36** | **-36.5** | **40** | **5.2** | **51** | **14.1** | **64** | **8.2** | **32** | **12.9** | **49** |
| FRS Select U.S. Stock Market Index Fund | 1.0 | 44 | 17.1 | 12 | 28.6 | 42 | -37.2 | 53 | 5.2 | 60 | 15.7 | 37 | 6.2 | 52 | 12.0 | 35 |
| *Russell 3000 Index* | *1.0* | *44* | *16.9* | *13* | *28.3* | *43* | *-37.3* | *56* | *5.1* | *63* | *15.7* | *34* | *6.1* | *53* | *11.9* | *35* |
| FRS Select U.S. Large Value Stock Fund | 1.6 | 27 | 15.2 | 33 | 20.8 | 66 | -35.2 | 36 | -- | -- | -- | -- | -- | -- | -- | -- |
| *Russell 1000 Value Index* | *0.4* | *37* | *15.5* | *29* | *19.7* | *73* | *-36.8* | *57* | -- | -- | -- | -- | -- | -- | -- | -- |
| QMA Mid Cap Quantitative Core Fund | 0.1 | 22 | 28.9 | 13 | 36.5 | 50 | -36.8 | 27 | 8.3 | 55 | 11.9 | 53 | 11.6 | 42 | -- | -- |
| *S&P 400 MidCap* | *-1.7* | *35* | *26.6* | *26* | *37.4* | *46* | *-36.2* | *25* | *8.0* | *56* | *10.3* | *63* | *12.5* | *31* | -- | -- |
| FRS Select U.S. Large Growth Stock Active Fund | 1.2 | 25 | 13.6 | 70 | 41.5 | 25 | -37.3 | 25 | 11.9 | 66 | 4.1 | 84 | 13.3 | 16 | 4.6 | 88 |
| *Russell 1000 Growth Index* | *2.6* | *13* | *16.7* | *42* | *37.2* | *38* | *-38.4* | *36* | *11.8* | *66* | *9.1* | *38* | *5.3* | *70* | *6.3* | *73* |
| Pioneer Fund | -4.2 | 82 | 16.2 | 19 | 24.9 | 70 | -34.1 | 17 | 5.1 | 64 | 16.9 | 18 | 6.8 | 42 | 12.1 | 32 |
| *S&P 500 Index* | *2.1* | *22* | *15.1* | *31* | *26.5* | *54* | *-37.0* | *44* | *5.5* | *50* | *15.8* | *32* | *4.9* | *65* | *10.9* | *46* |
| Fidelity Growth Company Fund | 0.9 | 26 | 20.8 | 12 | 41.5 | 25 | -40.7 | 52 | 20.2 | 21 | 9.8 | 31 | 13.8 | 15 | 12.4 | 23 |
| *Russell 3000 Growth Index* | *2.2* | *18* | *17.6* | *33* | *37.0* | *38* | *-38.4* | *36* | *11.4* | *71* | *9.5* | *35* | *5.2* | *71* | *6.9* | *69* |
| American Beacon Small Cap Value Fund | -4.0 | 52 | 26.2 | 47 | 35.4 | 31 | -31.9 | 57 | -6.4 | 50 | 14.7 | 73 | 5.8 | 61 | -- | -- |
| *Russell 2000 Value Index* | *-5.5* | *63* | *24.5* | *72* | *20.6* | *91* | *-28.9* | *35* | *-9.8* | *79* | *23.5* | *9* | *4.7* | *74* | -- | -- |
| T. Rowe Price Small Cap Stock Fund | -0.1 | 29 | 32.5 | 21 | 38.5 | 37 | -33.3 | 7 | -1.7 | 90 | 12.8 | 44 | 8.4 | 37 | 18.8 | 20 |
| *Russell 2000 Index* | *-4.2* | *65* | *26.9* | *57* | *27.2* | *83* | *-33.8* | *7* | *-1.6* | *90* | *18.4* | *9* | *4.6* | *71* | *18.3* | *20* |
| Fidelity Low Priced Stock Fund | 0.2 | 11 | 21.0 | 74 | 39.4 | 29 | -36.0 | 26 | 3.4 | 69 | 18.0 | 15 | 8.9 | 53 | 22.5 | 13 |
| *Russell 2500 Value Index* | *-3.4* | *56* | *24.8* | *42* | *27.7* | *90* | *-32.0* | *14* | *-7.3* | *99* | *20.2* | *9* | *7.7* | *65* | *21.6* | *19* |
| **International/Global Equity** | **-11.3** | **25** | **10.1** | **63** | **34.8** | **43** | **-40.9** | **17** | **15.0** | **36** | **23.2** | **76** | **14.9** | **52** | **17.9** | **60** |
| FRS Select Foreign Stock Index Fund | -11.8 | 31 | 9.2 | 68 | 32.3 | 52 | -42.5 | 32 | 12.7 | 49 | 25.8 | 48 | 14.7 | 55 | 20.5 | 36 |
| *MSCI World ex USA* | *-12.2* | *35* | *8.9* | *70* | *33.7* | *47* | *-43.6* | *41* | *12.4* | *51* | *25.7* | *49* | *14.5* | *58* | *20.4* | *37* |
| American Funds New Perspective Fund | -7.4 | 48 | 13.0 | 49 | 37.7 | 32 | -37.7 | 24 | 16.3 | 30 | 20.1 | 53 | 11.5 | 56 | 14.5 | 62 |
| *MSCI World Index* | *-5.5* | *36* | *11.8* | *59* | *30.0* | *60* | *-40.7* | *48* | *9.0* | *59* | *20.1* | *53* | *10.0* | *64* | *15.2* | *55* |
| American Funds Euro-Pacific Growth Fund | -13.3 | 42 | 9.8 | 62 | 39.6 | 18 | -40.3 | 10 | 19.3 | 15 | 22.3 | 84 | 21.4 | 12 | -- | -- |
| *MSCI All Country World ex-U.S. Index* | *-13.3* | *43* | *11.6* | *44* | *32.5* | *42* | *-43.1* | *39* | *11.6* | *60* | *26.9* | *27* | *14.0* | *59* | -- | -- |

# Asset Allocation

| | Total Market Value | % of Portfolio | U.S. Equity | Non-U.S. Equity | Balanced | Fixed Income | TIPS | Cash |
|---|---|---|---|---|---|---|---|---|
| Balanced Funds | | | | | | | | |
| FRS Select Conservative Balanced Fund | $626,660,939 | 9.4% | | | $626,660,939 | | | |
| FRS Select Moderate Balanced Fund | $1,691,870,961 | 25.5% | | | $1,691,870,961 | | | |
| FRS Select Aggressive Balanced Fund | $514,820,204 | 7.8% | | | $514,820,204 | | | |
| Cash | | | | | | | | |
| FRS Select Yield Plus Money Market Active Fund | $921,202,884 | 13.9% | | | | | | $921,202,884 |
| TIPS | | | | | | | | |
| FRS Select TIPS Fund | $288,104,372 | 4.3% | | | | | $288,104,372 | |
| Fixed Income | | | | | | | | |
| FRS Select U.S. Bond Enhanced Index Fund | $148,002,354 | 2.2% | | | | $148,002,354 | | |
| Pyramis Intermediate Duration Pool Fund | $74,251,707 | 1.1% | | | | $74,251,707 | | |
| FRS Select High Yield Fund | $133,251,345 | 2.0% | | | | $133,251,345 | | |
| PIMCO Total Return Fund | $277,828,032 | 4.2% | | | | $277,828,032 | | |
| Domestic Equity | | | | | | | | |
| FRS Select U.S. Stock Market Index Fund | $229,260,232 | 3.5% | $229,260,232 | | | | | |
| FRS Select U.S. Large Value Stock Fund | $185,075,725 | 2.8% | $185,075,725 | | | | | |
| QMA Mid Cap Quantitative Core Fund | $256,450,202 | 3.9% | $256,450,202 | | | | | |
| FRS Select U.S. Large Growth Stock Active Fund | $77,940,867 | 1.2% | $77,940,867 | | | | | |
| Pioneer Fund | $129,522,387 | 1.9% | $129,522,387 | | | | | |
| Fidelity Growth Company Fund | $278,322,925 | 4.2% | $278,322,925 | | | | | |
| American Beacon Small Cap Value Fund | $121,542,363 | 1.8% | $121,542,363 | | | | | |
| T. Rowe Price Small Cap Stock Fund | $221,369,760 | 3.3% | $221,369,760 | | | | | |
| Fidelity Low Priced Stock Fund | $22,811,831 | 0.3% | $22,811,831 | | | | | |
| International/Global Equity | | | | | | | | |
| FRS Select Foreign Stock Index Fund | $122,600,549 | 1.8% | | $122,600,549 | | | | |
| American Funds New Perspective Fund | $169,420,449 | 2.6% | | $169,420,449 | | | | |
| American Funds Euro-Pacific Growth Fund | $152,011,720 | 2.3% | | $152,011,720 | | | | |
| **Total** | **$6,642,321,806** | **100.0%** | **$1,522,296,291** | **$444,032,717** | **$2,833,352,104** | **$633,333,438** | **$288,104,372** | **$921,202,884** |
| Percent of Total | | | 22.9% | 6.7% | 42.7% | 9.5% | 4.3% | 13.9% |

# Asset Allocation

| Asset Allocation as of 12/31/2011 | | | | | | | |
|---|---|---|---|---|---|---|---|
| | U.S. Equity | Non-U.S. Equity | U.S. Fixed Income | TIPS | Cash | Total | % of Total |
| FRS Select Conservative Balanced Fund | 37,599,656 | 50,132,875 | 213,064,719 | 106,532,360 | 219,331,329 | 626,660,939 | 9.4% |
| FRS Select Moderate Balanced Fund | 473,723,869 | 338,374,192 | 879,772,900 | | | 1,691,870,961 | 25.5% |
| FRS Select Aggressive Balanced Fund | 211,076,284 | 139,001,455 | 164,742,465 | | | 514,820,204 | 7.8% |
| **Total Balanced Funds** | **$ 722,399,809** | **$ 527,508,522** | **$ 1,257,580,084** | **$ 106,532,360** | **$ 219,331,329** | **$ 2,833,352,104** | **42.7%** |
| FRS Select Yield Plus Money Market Active Fund | | | | | 921,202,884 | 921,202,884 | 13.9% |
| **Total Cash** | **$ -** | **$ -** | **$ -** | **$ -** | **$ 921,202,884** | **$ 921,202,884** | **13.9%** |
| FRS Select TIPS Fund | - | - | - | 288,104,372 | - | 288,104,372 | 4.3% |
| **Total TIPS** | **$ -** | **$ -** | **$ -** | **$ 288,104,372** | **$ -** | **$ 288,104,372** | **4.3%** |
| FRS Select U.S. Bond Enhanced Index Fund | | | 148,002,354 | | | 148,002,354 | 2.2% |
| Pyramis Intermediate Duration Pool Fund | | | 74,251,707 | | | 74,251,707 | 1.1% |
| FRS Select High Yield Fund | | | 133,251,345 | | | 133,251,345 | 2.0% |
| PIMCO Total Return Fund | | | 277,828,032 | | | 277,828,032 | 4.2% |
| **Total Fixed Income** | **$ -** | **$ -** | **$ 633,333,438** | **$ -** | **$ -** | **$ 633,333,438** | **9.5%** |
| FRS Select U.S. Stock Market Index Fund | 229,260,232 | | | | | 229,260,232 | 3.5% |
| FRS Select U.S. Large Value Stock Fund | 185,075,725 | | | | | 185,075,725 | 2.8% |
| QMA Mid Cap Quantitative Core Fund | 256,450,202 | | | | | 256,450,202 | 3.9% |
| FRS Select U.S. Large Growth Stock Active Fund | 77,940,867 | | | | | 77,940,867 | 1.2% |
| Pioneer Fund | 129,522,387 | | | | | 129,522,387 | 1.9% |
| Fidelity Growth Company Fund | 278,322,925 | | | | | 278,322,925 | 4.2% |
| American Beacon Small Cap Value Fund | 121,542,363 | | | | | 121,542,363 | 1.8% |
| T. Rowe Price Small Cap Stock Fund | 221,369,760 | | | | | 221,369,760 | 3.3% |
| Fidelity Low Priced Stock Fund | 22,811,831 | | | | | 22,811,831 | 0.3% |
| **Total Domestic Equity** | **$ 1,522,296,291** | **$ -** | **$ -** | **$ -** | **$ -** | **$ 1,522,296,291** | **22.9%** |
| FRS Select Foreign Stock Index Fund | | 122,600,549 | | | | 122,600,549 | 1.8% |
| American Funds New Perspective Fund | 67,768,179 | 89,453,997 | 169,420 | | 12,028,852 | 169,420,449 | 2.6% |
| American Funds Euro-Pacific Growth Fund | 152,012 | 139,394,747 | 152,012 | | 12,312,949 | 152,011,720 | 2.3% |
| **Total International/Global Equity** | **$ 67,920,191** | **$ 351,449,293** | **$ 321,432** | **$ -** | **$ 24,341,801** | **$ 444,032,717** | **6.7%** |
| **Total Portfolio** | **$ 2,312,616,291** | **$ 878,957,815** | **$ 1,891,234,954** | **$ 394,636,732** | **$ 1,164,876,014** | **$ 6,642,321,806** | **100.0%** |
| **Percent of Total** | **34.82%** | **13.23%** | **28.47%** | **5.94%** | **17.54%** | **100.0%** | |

# Manager Scorecard

## Statistics Summary

### 3 Years Ending December 31, 2011

| | Annualized Return (%) | Annualized Standard Deviation | Sharpe Ratio | Tracking Error | Information Ratio | Up Market Capture Ratio (%) | Down Market Capture Ratio (%) |
|---|---|---|---|---|---|---|---|
| FRS Investment Plan | 9.65% | 10.20% | 0.94 | 0.54% | 1.04 | 103.23% | 99.66% |
| FRS Select Conservative Balanced Fund | 6.12% | 3.82% | 1.58 | 0.36% | 0.82 | 102.08% | 95.79% |
| FRS Select Moderate Balanced Fund | 9.24% | 10.36% | 0.88 | 0.67% | 0.63 | 103.73% | 101.18% |
| FRS Select Aggressive Balanced Fund | 10.05% | 13.83% | 0.72 | 0.87% | -0.03 | 101.00% | 101.04% |
| FRS Select Yield Plus Money Market Active Fund | 0.26% | 0.02% | 9.25 | 0.08% | -0.60 | 83.87% | -- |
| FRS Select TIPS Fund | 10.41% | 5.79% | 1.78 | 0.20% | 0.11 | 99.57% | 98.21% |
| FRS Select U.S. Bond Enhanced Index Fund | 7.05% | 2.85% | 2.45 | 0.18% | 1.51 | 102.67% | 96.20% |
| Pyramis Intermediate Duration Pool Fund | 8.25% | 2.99% | 2.74 | 1.20% | 1.72 | 134.60% | 120.04% |
| FRS Select High Yield Fund | -- | -- | -- | -- | -- | -- | -- |
| PIMCO Total Return Fund | 8.73% | 3.71% | 2.33 | 2.96% | 0.66 | 119.71% | 75.65% |
| FRS Select U.S. Stock Market Index Fund | 15.02% | 19.66% | 0.76 | 0.09% | 1.46 | 100.45% | 99.93% |
| FRS Select U.S. Large Value Stock Fund | 12.23% | 21.04% | 0.58 | 1.39% | 0.50 | 100.60% | 98.66% |
| QMA Mid Cap Quantitative Core Fund | 20.79% | 23.42% | 0.88 | 2.25% | 0.54 | 109.58% | 103.40% |
| FRS Select U.S. Large Growth Stock Active Fund | 17.61% | 17.90% | 0.98 | 2.90% | -0.14 | 96.35% | 98.09% |
| Pioneer Fund | 11.58% | 19.68% | 0.58 | 2.85% | -0.89 | 95.74% | 104.54% |
| Fidelity Growth Company Fund | 19.94% | 19.28% | 1.03 | 3.57% | 0.52 | 115.23% | 106.28% |
| American Beacon Small Cap Value Fund | 17.91% | 26.65% | 0.67 | 3.51% | 1.58 | 109.28% | 94.81% |
| T. Rowe Price Small Cap Stock Fund | 22.39% | 24.21% | 0.92 | 2.56% | 2.65 | 105.57% | 90.23% |
| Fidelity Low Priced Stock Fund | 19.11% | 19.73% | 0.96 | 7.02% | 0.52 | 78.25% | 77.48% |
| FRS Select Foreign Stock Index Fund | 8.42% | 23.28% | 0.36 | 2.58% | -0.04 | 104.05% | 102.23% |
| American Funds New Perspective Fund | 12.98% | 19.44% | 0.66 | 3.56% | 0.52 | 98.00% | 93.81% |
| American Funds Euro-Pacific Growth Fund | 9.94% | 21.78% | 0.45 | 4.55% | 0.29 | 99.01% | 96.44% |

The three-year performance history is not available for the FRS Select High Yield Fund. The inception date for the fund is January 2010.

# Appendix

# Market Returns

| | Fourth Quarter | Annualized Periods Ending 12/31/11 | | | | |
|---|---|---|---|---|---|---|
| | | 1-Year | 3-Year | 5-Year | 10-Year | 15-Year |
| **Domestic Stock Indices:** | | | | | | |
| Dow Jones US Total Stock Index | 12.1 | 1.1 | 15.2 | 0.2 | 3.9 | 5.8 |
| S&P 500 Index | 11.8 | 2.1 | 14.1 | -0.3 | 2.9 | 5.5 |
| Russell 3000 Index | 12.1 | 1.0 | 14.9 | 0.0 | 3.5 | 5.7 |
| Russell 1000 Value Index | 13.1 | 0.4 | 11.5 | -2.6 | 3.9 | 6.3 |
| Russell 1000 Growth Index | 10.6 | 2.6 | 18.0 | 2.5 | 2.6 | 4.5 |
| Russell MidCap Value Index | 13.4 | -1.4 | 18.2 | 0.0 | 7.7 | 8.9 |
| Russell MidCap Growth Index | 11.2 | -1.7 | 22.1 | 2.4 | 5.3 | 6.5 |
| Russell 2000 Value Index | 16.0 | -5.5 | 12.4 | -1.9 | 6.4 | 8.0 |
| Russell 2000 Growth Index | 15.0 | -2.9 | 19.0 | 2.1 | 4.5 | 3.9 |
| **Domestic Bond Indices:** | | | | | | |
| Barclays Capital Aggregate Index | 1.1 | 7.8 | 6.8 | 6.5 | 5.8 | 6.3 |
| Barclays Capital Govt/Credit Index | 1.2 | 8.7 | 6.6 | 6.5 | 5.9 | 6.4 |
| Barclays Capital Long Govt/Credit Index | 2.6 | 22.5 | 11.2 | 9.7 | 8.5 | 8.4 |
| Barclays Capital 1-3 Year Govt/Credit Index | 0.2 | 1.6 | 2.7 | 4.0 | 3.6 | 4.6 |
| Barclays Capital U.S. MBS Index | 0.9 | 6.2 | 5.8 | 6.5 | 5.7 | 6.3 |
| Barclays Capital High Yield Index | 6.5 | 5.0 | 24.1 | 7.5 | 8.9 | 6.9 |
| Barclays Capital Universal Index | 1.4 | 7.4 | 7.7 | 6.4 | 6.0 | 6.4 |
| **Real Estate Indices:** | | | | | | |
| NCREIF Property Index | 3.0 | 14.3 | 2.4 | 3.1 | 8.1 | 9.4 |
| NCREIF ODCE Index | 2.7 | 15.0 | -2.7 | -1.1 | 5.2 | 7.3 |
| Dow Jones Real Estate Securities Index | 15.3 | 8.9 | 21.7 | -2.2 | 10.1 | 9.0 |
| FTSE NAREIT US Real Estate Index | 15.3 | 8.3 | 21.0 | -1.4 | 10.2 | 8.9 |
| **Foreign/Global Stock Indices:** | | | | | | |
| MSCI All Country World Index | 7.2 | -7.3 | 12.0 | -1.9 | 4.2 | 4.5 |
| MSCI All Country World IMI | 7.2 | -7.9 | 12.8 | -1.6 | 4.9 | 4.6 |
| MSCI All Country World ex-U.S. Index | 3.7 | -13.7 | 10.7 | -2.9 | 6.3 | 4.4 |
| MSCI All Country World ex-U.S. IMI | 3.3 | -14.3 | 11.5 | -2.7 | 6.9 | 4.3 |
| MSCI All Country World ex-U.S. Small Cap Index | 0.4 | -18.5 | 18.5 | -1.7 | 10.6 | 5.3 |
| MSCI EAFE Index | 3.3 | -12.1 | 7.6 | -4.7 | 4.7 | 3.4 |
| MSCI EAFE IMI | 2.9 | -12.6 | 8.4 | -4.6 | 5.3 | 3.6 |
| MSCI EAFE Index (in local currency) | 4.1 | -12.2 | 4.7 | -6.6 | 0.7 | 2.3 |
| MSCI Emerging Markets IMI | 3.8 | -19.5 | 20.7 | 2.6 | 13.8 | 5.1 |
| **Foreign Bond Indices:** | | | | | | |
| Citigroup World Gov't Bond Index | -0.5 | 5.2 | 4.9 | 7.2 | 8.4 | 5.5 |
| Citigroup Hedged World Gov't Bond Index | 0.6 | 4.1 | 3.0 | 4.3 | 4.4 | 5.7 |
| **Cash Equivalents:** | | | | | | |
| Treasury Bills (30-Day) | 0.0 | 0.0 | 0.1 | 1.1 | 1.5 | 2.5 |
| EnnisKnupp STIF Index | 0.0 | 0.2 | 0.4 | 1.8 | 2.2 | 3.3 |
| **Inflation Index:** | | | | | | |
| Consumer Price Index | -0.5 | 3.0 | 2.4 | 2.3 | 2.5 | 2.4 |

# Benchmark Descriptions

**Balanced Benchmarks** - A weighted average composite of the underlying components' benchmarks for each fund.

**iMoneyNet 1st Tier Institutional Net Index** - An index made up of the entire universe of money market mutual funds. The index currently represents over 1,300 funds, or approximately 99 percent of all money fund assets.

**Barclays Capital Inflation Index** - Measures the performance of the U.S. Treasury Inflation-Protected Securities ("TIPS") market.

**Barclays Capital Aggregate Bond Index** - A market value-weighted index consisting of government bonds, SEC-registered corporate bonds and mortgage-related and asset-backed securities with at least one year to maturity and an outstanding par value of $250 million or greater. This index is a broad measure of the performance of the investment grade U.S. fixed income market.

**Barclays Capital Intermediate Aggregate Bond Index** - A market value-weighted index consisting of U.S. Treasury securities, corporate bonds and mortgage-related and asset-backed securities with one to ten years to maturity and an outstanding par value of $250 million or greater.

**Barclays Capital U.S. High Yield Ba-2% Issuer Cap Index** - An index composed of non-investment grade corporate debt denominated in U.S. dollars. The issues have to have an outstanding par value of $150 million or greater and at least one year of maturity remaining.

**Russell 3000 Index** - A capitalization-weighted index consisting of the 3,000 largest publicly traded U.S. stocks by capitalization. This index is a broad measure of the performance of the aggregate domestic equity market.

**Russell 3000 Growth Index** - Measures the performance of those Russell 3000 companies with higher price-to-book ratios and higher forecasted growth values.

**Russell 1000 Value Index** - An index that measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower I/B/E/S growth forecasts.

**Russell 1000 Growth Index** - An index that measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher I/B/E/S growth forecasts.

# Benchmark Descriptions

**Russell 2000 Value Index** - A capitalization-weighted index representing those companies within the Russell 2000 Index with lower price-to-book ratios and lower I/B/E/S earnings growth forecasts.

**Russell 2000 Index** - An index that measures the performance of approximately 2000 small capitalization stocks.

**Russell 2500 Value Index** - A capitalization-weighted index representing those companies within the Russell 2500 Index with lower price-to-book ratios and lower I/B/E/S earnings growth forecasts.

**S&P 400 Mid-Cap Index** - A market capitalization-weighted index of stocks in all major industries in the mid-range of the U.S. stock market.

**S&P 500 Index** - A capitalization-weighted stock index consisting of 500 of the largest publicly traded U.S. stocks by capitalization.

**MSCI All Country World ex-US Index** - A capitalization-weighted index consisting of 23 developed and 21 emerging countries, but excluding the U.S.

**MSCI All Country World Index** - A capitalization-weighted index of stocks representing approximately 46 developed and emerging countries, including the U.S. and Canadian markets.

**MSCI World ex-U.S. Index** - A capitalization-weighted index of stocks representing 22 developed country stock markets, including Canada and excluding the U.S. market.

# Description of Universes

**FRS Select Yield Plus Money Market Active Fund** - A money market universe calculated and provided by Morningstar.

**FRS Select TIPS Fund** - An inflation-protected bond universe calculated and provided by Morningstar.

**FRS Select U.S. Bond Enhanced Index Fund** - A long-term bond fixed income universe calculated and provided by Morningstar.

**Pyramis Intermediate Duration Pool Fund** - A broad intermediate-term fixed income universe calculated and provided by Morningstar.

**FRS Select High Yield Fund** - A high yield bond fixed income universe calculated and provided by Morningstar.

**PIMCO Total Return Fund** - A broad intermediate-term fixed income universe calculated and provided by Morningstar.

**FRS Select U.S. Stock Market Index Fund** - A large-cap blend universe calculated and provided by Morningstar.

**FRS Select U.S. Large Value Stock Fund** - A large-cap value universe calculated and provided by Morningstar.

**QMA Mid Cap Quantitative Core Fund** - A mid-cap universe calculated and provided by Morningstar.

**FRS Select U.S. Large Growth Stock Active Fund** - A large-cap growth universe calculated and provided by Morningstar.

**Pioneer Fund** - A large-cap blend universe calculated and provided by Morningstar.

**Fidelity Growth Company Fund** - A large-cap growth universe calculated and provided by Morningstar.

**American Beacon Small Cap Value Fund** - A small-cap value universe calculated and provided by Morningstar.

# Description of Universes

**T. Rowe Price Small Cap Stock Fund** - A small-cap growth universe calculated and provided by Morningstar.

**Fidelity Low Priced Stock Fund** - A mid-cap blend universe calculated and provided by Morningstar.

**FRS Select Foreign Stock Index Fund** - A foreign blend universe calculated and provided by Morningstar.

**American Funds New Perspective Fund** - A global stock universe calculated and provided by Morningstar.

**American Funds Euro-Pacific Growth Fund** - A foreign large blend universe calculated and provided by Morningstar.

Hewitt ennisknupp

An Aon Company

# Lawton Chiles Endowment Fund

Fourth Quarter 2011

**Hewitt EnnisKnupp, Inc.**
10 South Riverside Plaza, Suite 1600
Chicago, IL 60606
phone: 1-312-715-1700
fax: 1-312-715-1952
www.hewittennisknupp.com

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| 19 | Fixed Income |
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| 27 | Cash Equivalents |
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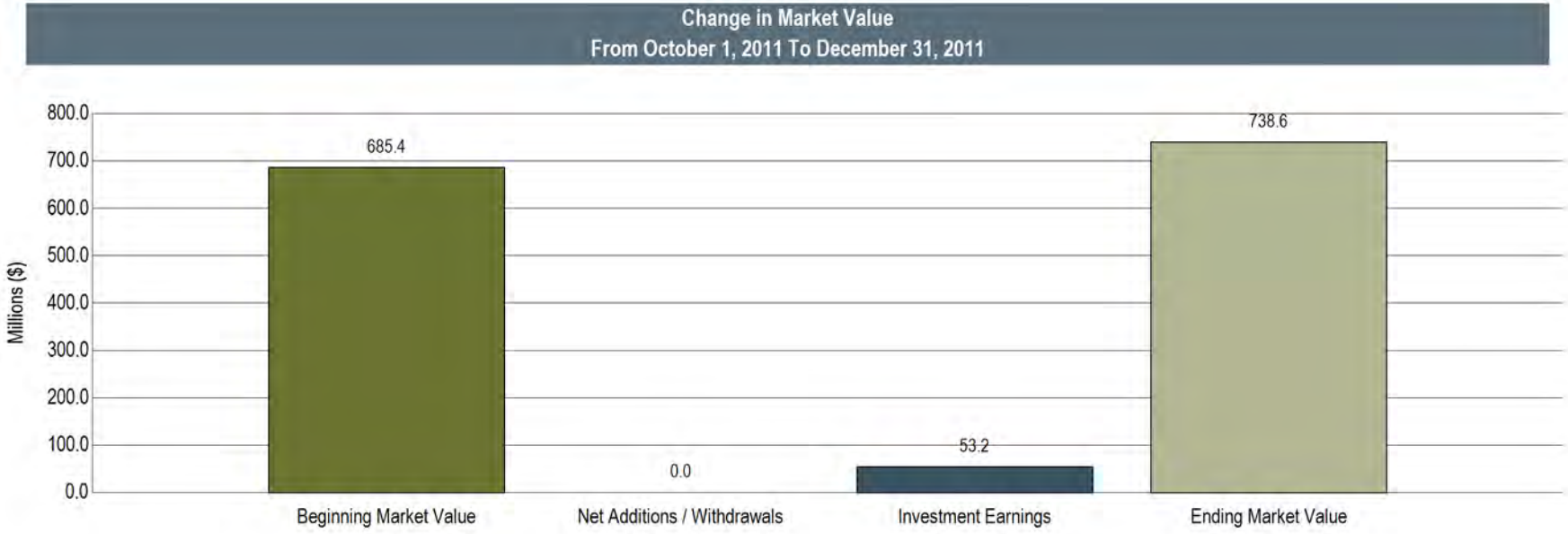
# LCEF Total Fund

# Plan Summary




## Summary of Cash Flows

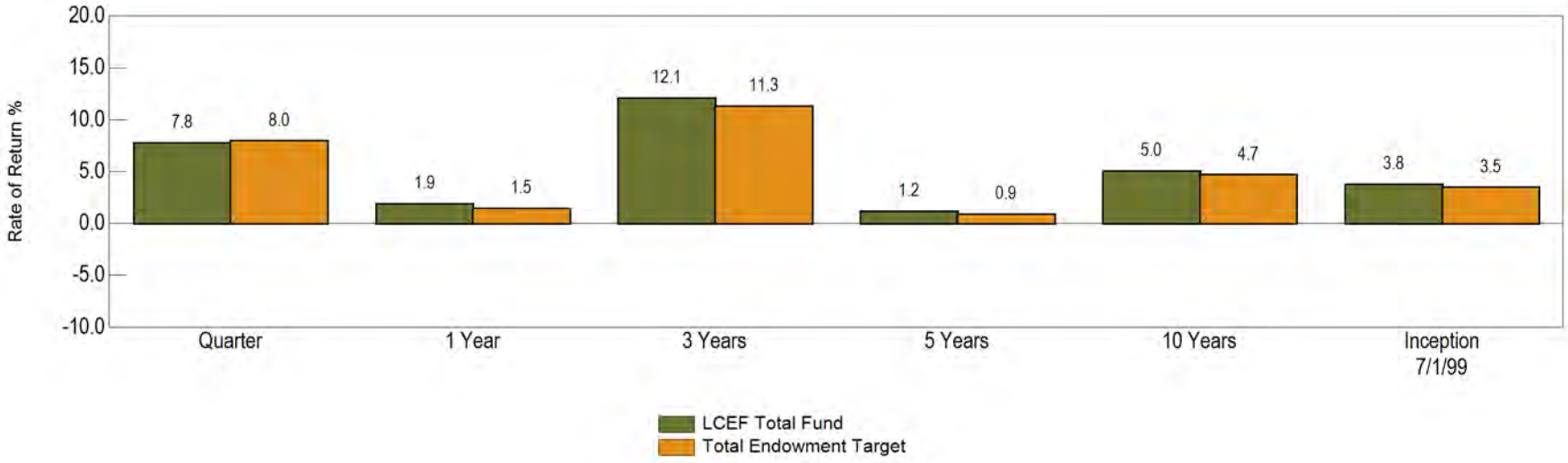
| Sources of Portfolio Growth | Fourth Quarter | Fiscal YTD* |
|---|---|---|
| Beginning Market Value | $685,382,630 | $767,566,265 |
| Net Additions/Withdrawals | $0 | $0 |
| Investment Earnings | $53,249,035 | -$28,934,600 |
| Ending Market Value | $738,631,665 | $738,631,665 |

*Period July 2011 - December 2011

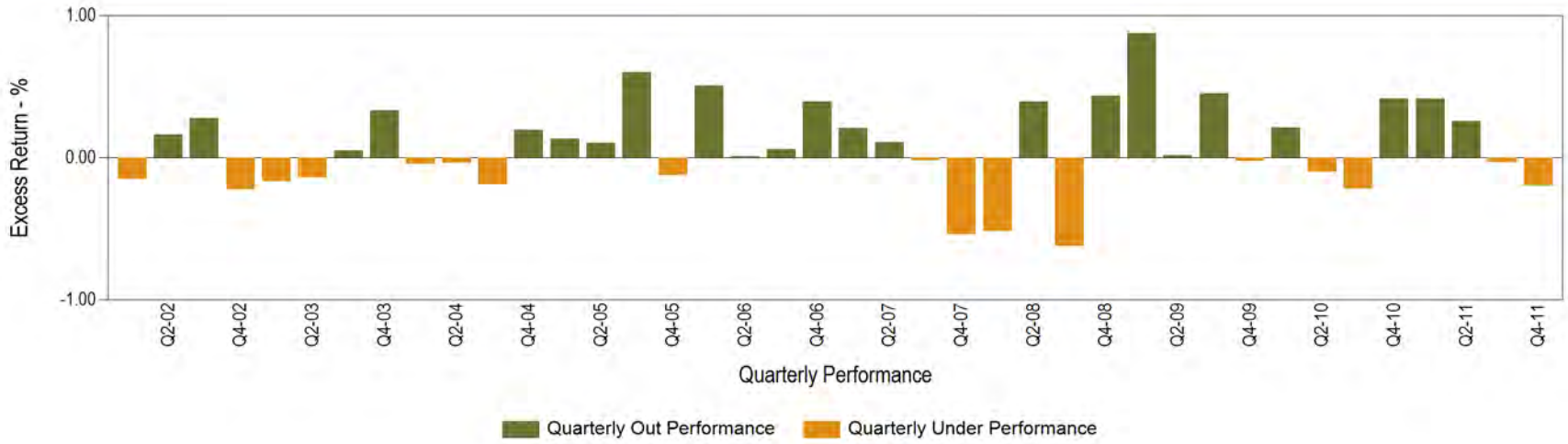
# Plan Performance

Benchmark: Total Endowment Target

## Return Summary




## Quarterly Excess Performance



# Trailing Period Performance

| Name | Market Value ($) | % of Portfolio | Policy % | 2011 Q4 (%) | Rank | Ending December 31, 2011 1 Yr (%) | Rank | 3 Yrs (%) | Rank | 5 Yrs (%) | Rank | 10 Yrs (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **LCEF Total Fund** | **738,631,665** | **100.0** | **100.0** | **7.8** | **1** | **1.9** | **31** | **12.1** | **8** | **1.2** | **65** | **5.0** | **56** |
| *Total Endowment Target* | | | | *8.0* | *1* | *1.5* | *34* | *11.3* | *16* | *0.9* | *72* | *4.7* | *69* |
| **Domestic Equity** | **438,450,175** | **59.4** | **59.0** | **12.0** | **20** | **0.8** | **28** | **14.9** | **45** | **-0.1** | **48** | **3.3** | **59** |
| *Russell 3000 ex-Tobacco* | | | | *12.0* | *23* | *0.6* | *35* | *14.7* | *47* | *-0.2* | *49* | *3.3* | *59* |
| **Foreign Equity** | **85,126,769** | **11.5** | **12.0** | **3.1** | **75** | **-9.7** | **14** | **13.8** | **17** | **-3.0** | **75** | **6.2** | **31** |
| *MSCI ACWI ex-U.S. IMI ex-Tobacco* | | | | *3.2* | *74* | *-14.6* | *76* | *11.4* | *39* | *-2.8* | *67* | *6.4* | *26* |
| **Fixed Income** | **123,688,571** | **16.7** | **17.0** | **1.1** | **78** | **7.6** | **32** | **6.4** | **85** | **6.4** | **68** | **5.9** | **45** |
| *Barclays Capital Aggregate Bond Index* | | | | *1.1* | *78* | *7.8* | *29* | *6.8* | *83* | *6.5* | *66* | *5.8* | *49* |
| **TIPS** | **83,979,859** | **11.4** | **11.0** | **2.7** | **--** | **13.6** | **--** | **10.9** | **--** | **8.5** | **--** | **8.0** | **--** |
| *Barclays Capital U.S. TIPS* | | | | *2.7* | *--* | *13.6* | *--* | *10.4* | *--* | *8.0* | *--* | *7.6* | *--* |
| **Cash Equivalents** | **7,386,190** | **1.0** | **1.0** | **0.0** | **--** | **0.1** | **--** | **1.5** | **--** | **2.1** | **--** | **2.3** | **--** |
| *S&P US AAA & AA Rated GIP 30D* | | | | *0.0* | *--* | *0.2* | *--* | *0.4* | *--* | *1.6* | *--* | *2.1* | *--* |

Benchmark and universe descriptions are provided in the Appendix.

# Calendar Year Performance

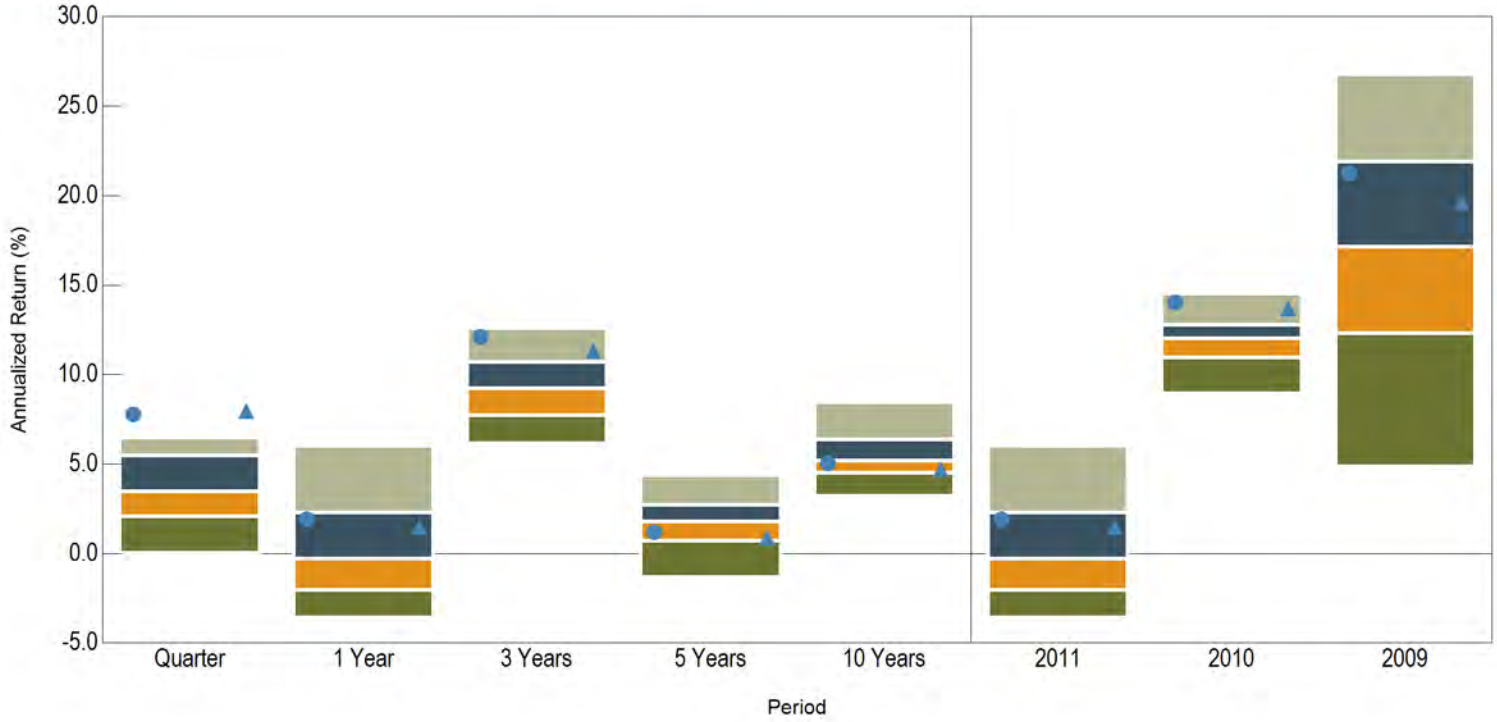
| Name | 2011 (%) | Rank | 2010 (%) | Rank | 2009 (%) | Rank | 2008 (%) | Rank | 2007 (%) | Rank | 2006 (%) | Rank | 2005 (%) | Rank | 2004 (%) | Rank | 2003 (%) | Rank | 2002 (%) | Rank |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **LCEF Total Fund** | **1.9** | **31** | **14.0** | **11** | **21.2** | **28** | **-29.2** | **74** | **6.3** | **92** | **15.0** | **40** | **7.4** | **69** | **12.0** | **54** | **25.0** | **25** | **-10.9** | **66** |
| *Total Endowment Target* | *1.5* | *34* | *13.7* | *14* | *19.6* | *35* | *-28.9* | *74* | *6.5* | *89* | *14.0* | *52* | *6.7* | *80* | *12.1* | *51* | *24.9* | *25* | *-11.0* | *66* |
| **Domestic Equity** | **0.8** | **28** | **17.0** | **48** | **28.5** | **52** | **-37.4** | **46** | **5.0** | **71** | **14.6** | **43** | **5.7** | **77** | **11.9** | **72** | **30.6** | **72** | **-21.6** | **72** |
| *Russell 3000 ex-Tobacco* | *0.6* | *35* | *16.8* | *51* | *28.4* | *53* | *-37.5* | *47* | *5.0* | *71* | *15.6* | *29* | *5.9* | *72* | *11.8* | *73* | *30.9* | *65* | *-21.8* | *74* |
| **Foreign Equity** | **-9.7** | **14** | **16.6** | **15** | **39.8** | **36** | **-49.0** | **99** | **14.3** | **61** | **28.4** | **12** | **21.2** | **6** | **16.2** | **83** | **39.4** | **38** | **-15.3** | **57** |
| *MSCI ACWI ex-U.S. IMI ex-Tobacco* | *-14.6* | *76* | *12.7* | *54* | *43.8* | *28* | *-46.1* | *71* | *16.5* | *38* | *26.6* | *18* | *16.6* | *42* | *20.8* | *29* | *40.9* | *19* | *-14.9* | *52* |
| **Fixed Income** | **7.6** | **32** | **7.0** | **73** | **4.6** | **85** | **5.8** | **14** | **7.3** | **43** | **4.4** | **35** | **2.7** | **24** | **4.4** | **69** | **4.1** | **90** | **11.0** | **2** |
| *Barclays Capital Aggregate Bond Index* | *7.8* | *29* | *6.5* | *75* | *5.9* | *78* | *5.2* | *20* | *7.0* | *50* | *4.3* | *37* | *2.4* | *54* | *4.3* | *70* | *4.1* | *90* | *10.3* | *6* |
| **TIPS** | **13.6** | **--** | **6.1** | **--** | **13.3** | **--** | **-2.0** | **--** | **12.4** | **--** | **0.8** | **--** | **2.9** | **--** | **8.8** | **--** | **8.4** | **--** | **17.0** | **--** |
| *Barclays Capital U.S. TIPS* | *13.6* | *--* | *6.3* | *--* | *11.4* | *--* | *-2.4* | *--* | *11.6* | *--* | *0.4* | *--* | *2.8* | *--* | *8.5* | *--* | *8.4* | *--* | *16.6* | *--* |
| **Cash Equivalents** | **0.1** | **--** | **2.0** | **--** | **2.6** | **--** | **0.5** | **--** | **5.4** | **--** | **5.2** | **--** | **3.3** | **--** | **1.4** | **--** | **1.2** | **--** | **1.7** | **--** |
| *S&P US AAA & AA Rated GIP 30D* | *0.2* | *--* | *0.3* | *--* | *0.7* | *--* | *2.3* | *--* | *4.7* | *--* | *5.1* | *--* | *3.4* | *--* | *1.4* | *--* | *1.1* | *--* | *1.7* | *--* |

# Universe Comparison

Benchmark: Total Endowment Target

Universe: Endowments Net

## Ending December 31, 2011



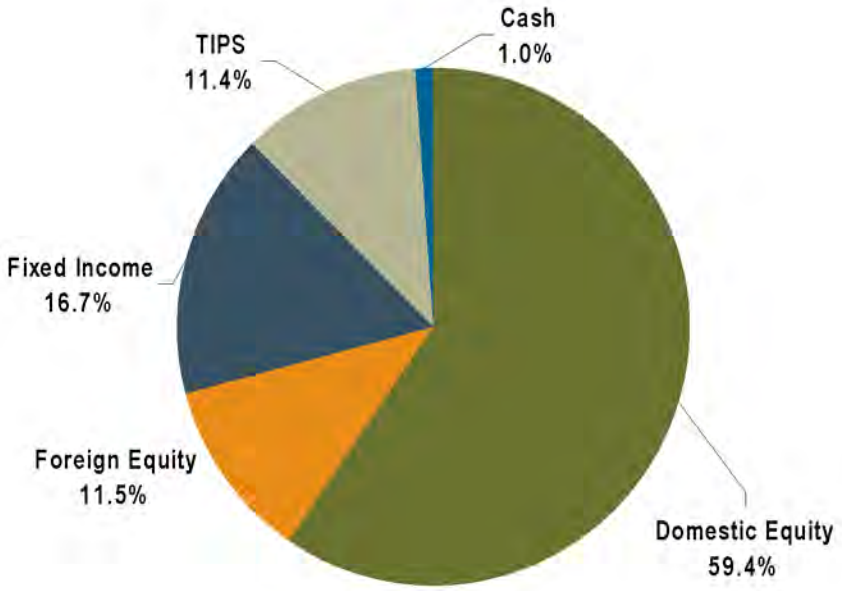

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **5th Percentile** | 6.5 | | 6.0 | | 12.6 | | 4.4 | | 8.4 | | 6.0 | | 14.5 | | 26.8 | |
| **25th Percentile** | 5.5 | | 2.3 | | 10.7 | | 2.8 | | 6.4 | | 2.3 | | 12.8 | | 21.9 | |
| **Median** | 3.5 | | -0.3 | | 9.2 | | 1.8 | | 5.2 | | -0.3 | | 12.0 | | 17.2 | |
| **75th Percentile** | 2.1 | | -2.0 | | 7.7 | | 0.8 | | 4.5 | | -2.0 | | 11.0 | | 12.3 | |
| **95th Percentile** | 0.1 | | -3.6 | | 6.2 | | -1.3 | | 3.2 | | -3.6 | | 9.0 | | 4.9 | |
| **# of Portfolios** | 96 | | 83 | | 79 | | 68 | | 54 | | 83 | | 78 | | 81 | |
| ● **LCEF Total Fund** | 7.8 | (1) | 1.9 | (31) | 12.1 | (8) | 1.2 | (65) | 5.0 | (56) | 1.9 | (31) | 14.0 | (11) | 21.2 | (28) |
| ▲ **Total Endowment Target** | 8.0 | (1) | 1.5 | (34) | 11.3 | (16) | 0.9 | (72) | 4.7 | (69) | 1.5 | (34) | 13.7 | (14) | 19.6 | (35) |

# Universe Asset Allocation Comparison

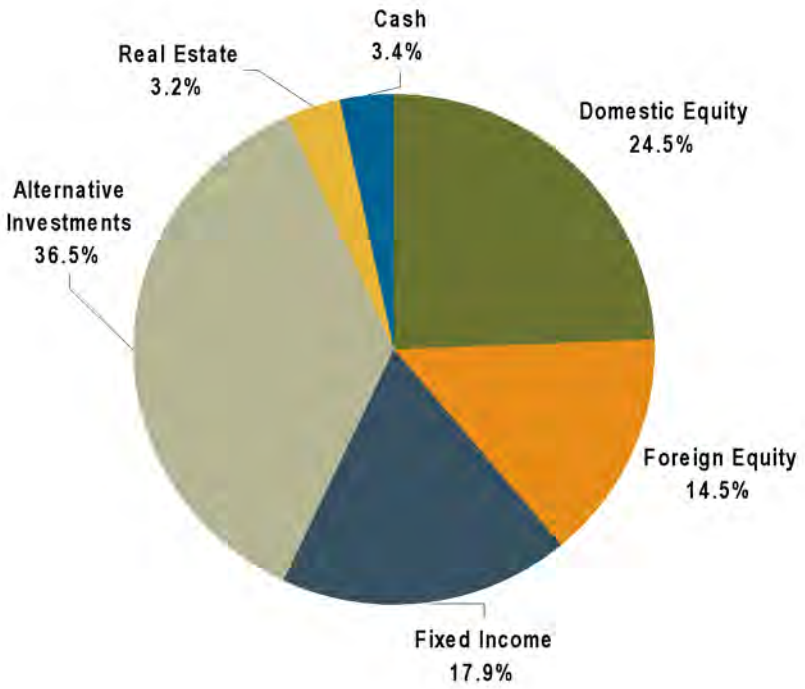
Benchmark: Total Endowment Target

Universe: Endowments Net

**LCEF Total Fund**




**BNY Mellon Endowment Universe**

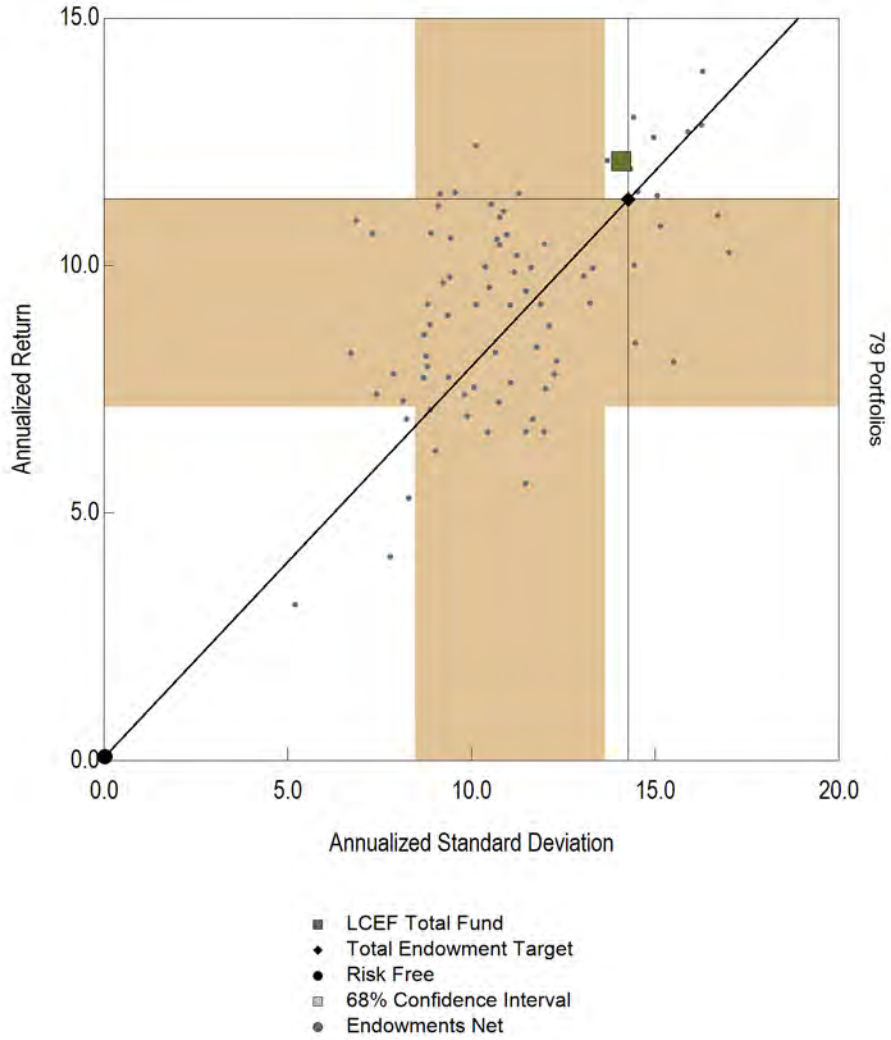


# Risk Profile

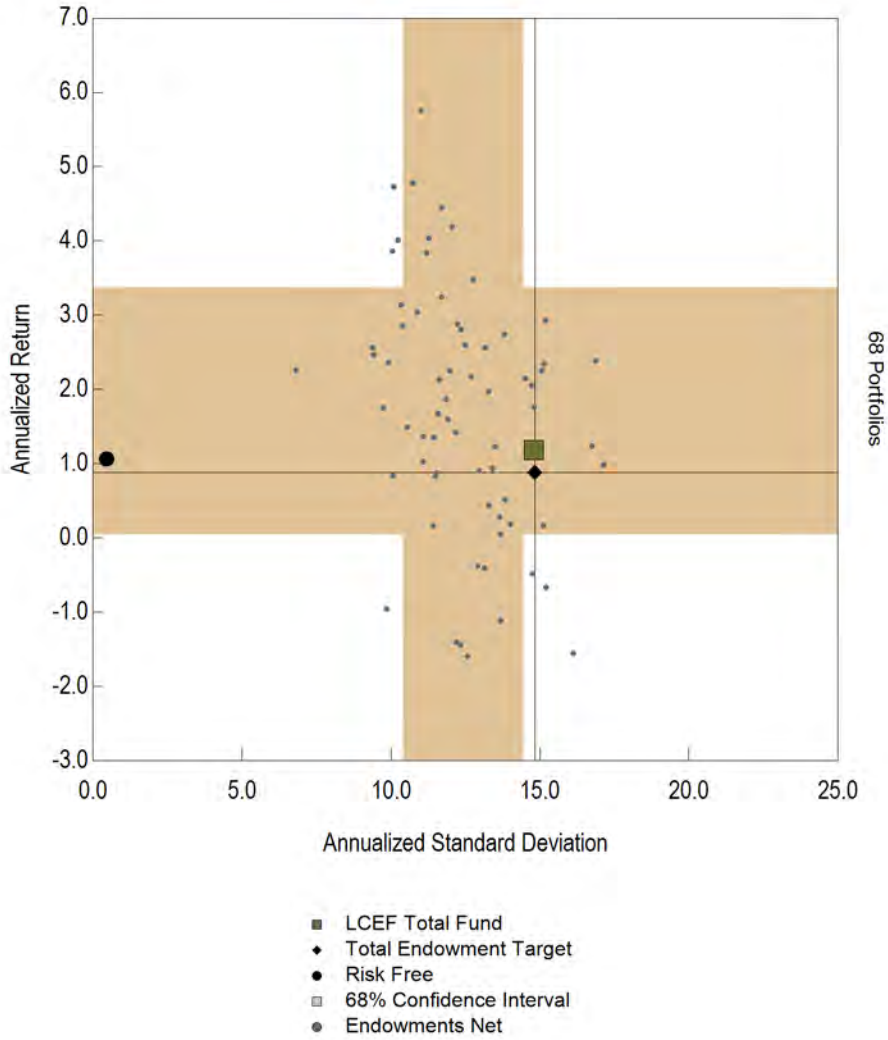
Benchmark: Total Endowment Target

Universe: Endowments Net

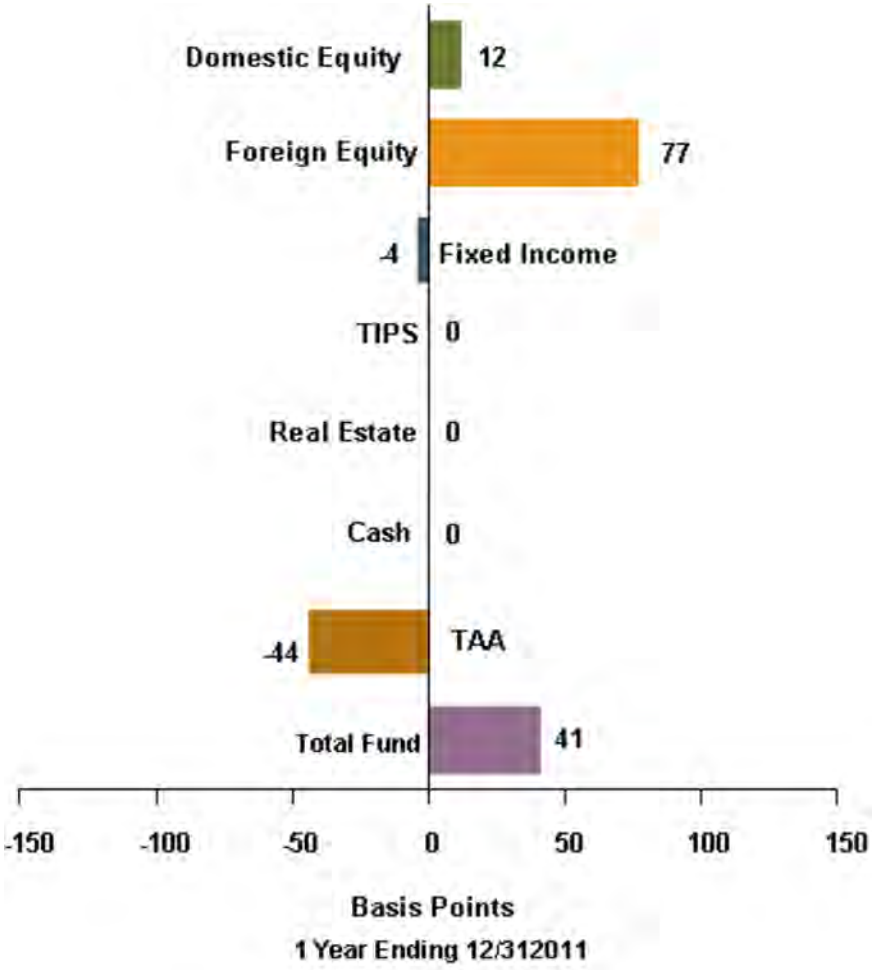
## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011

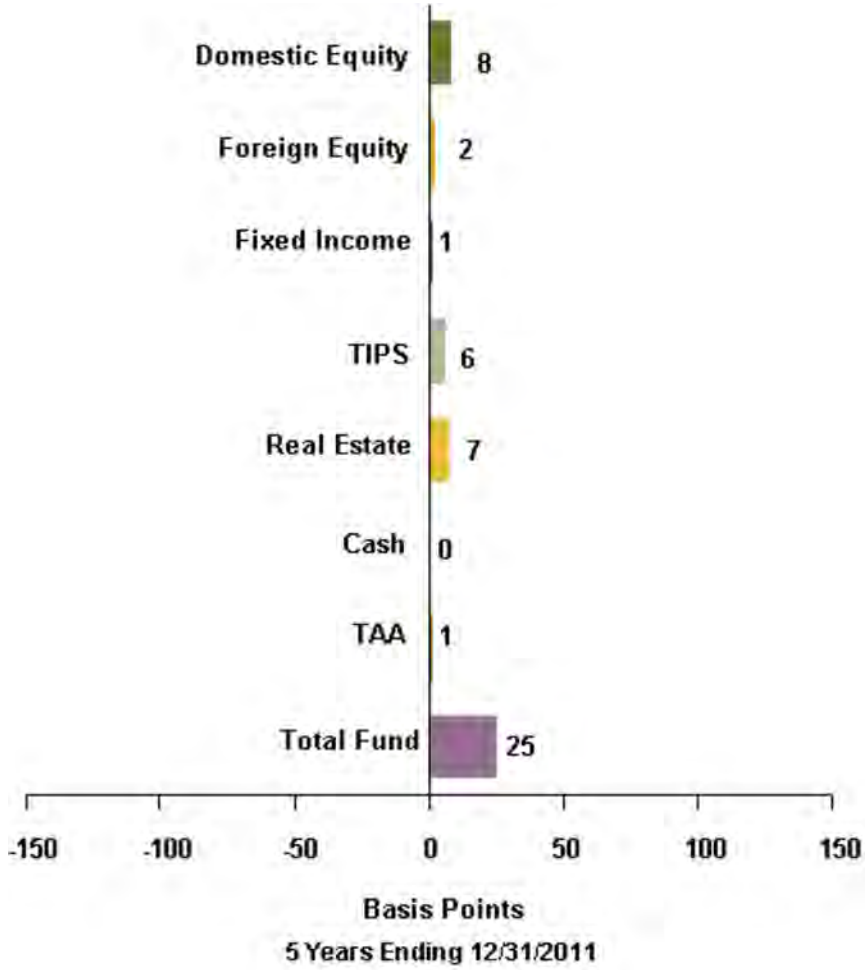



## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011



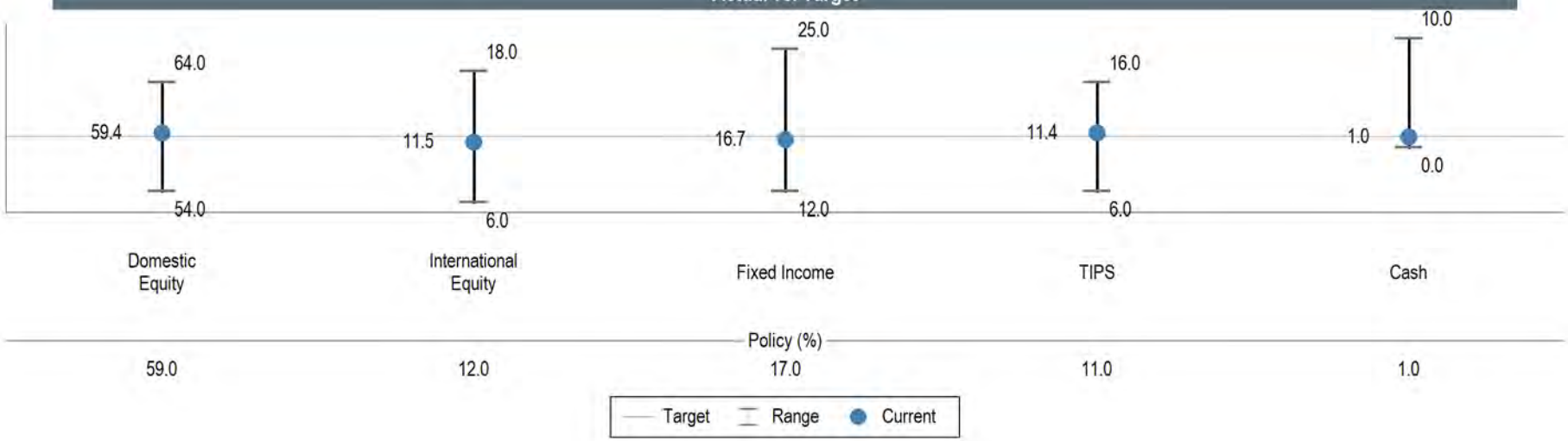
# Attribution



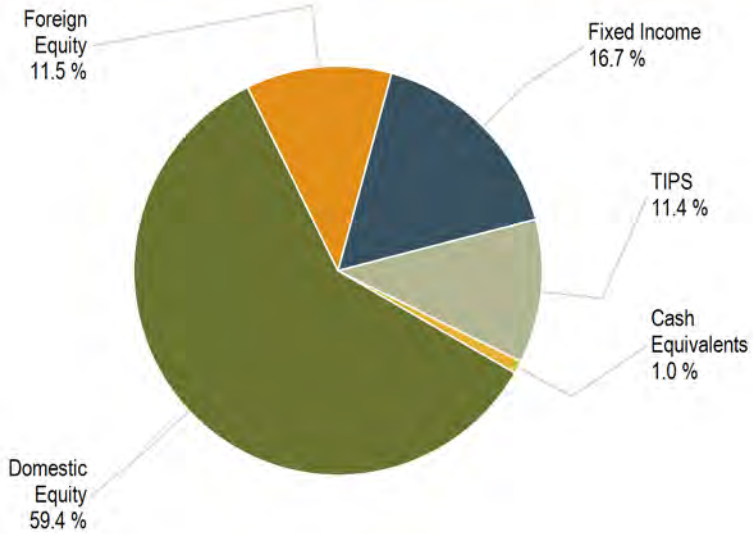



# Asset Allocation

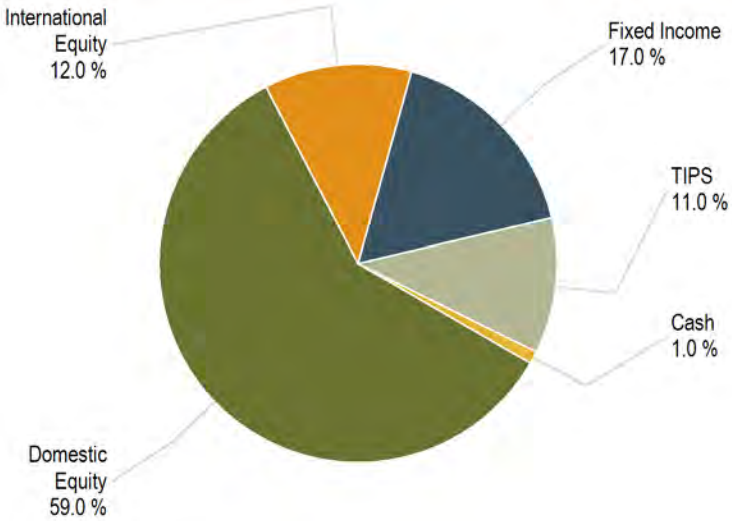
## Actual vs. Target




## Allocation




## Target Allocation

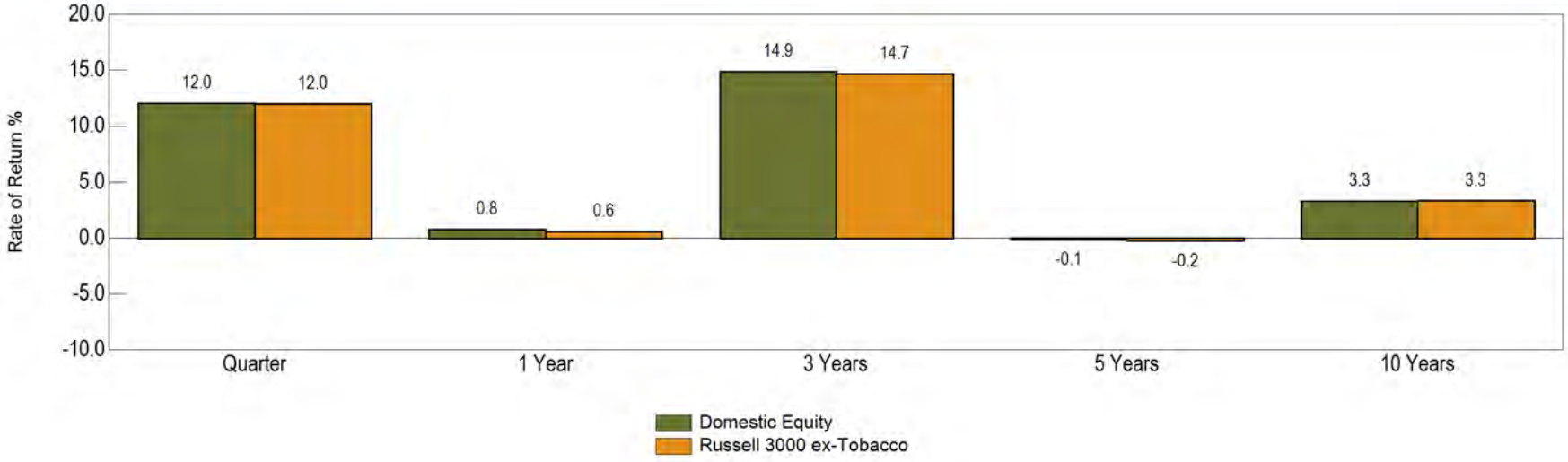


# Domestic Equity

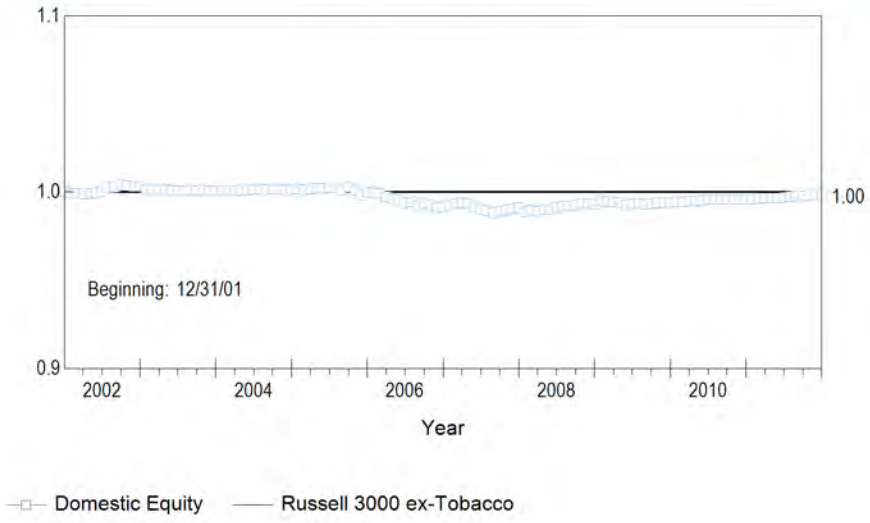
# Overview

Benchmark: Russell 3000 ex-Tobacco

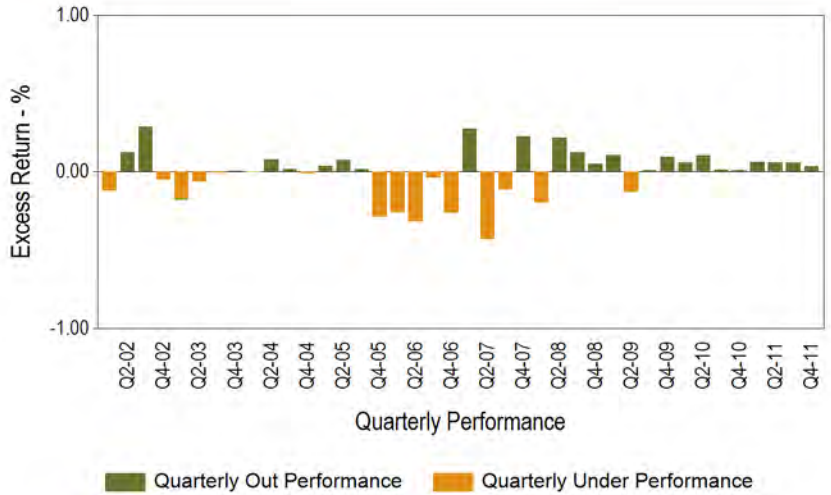
## Return Summary




## Ratio of Cumulative Wealth



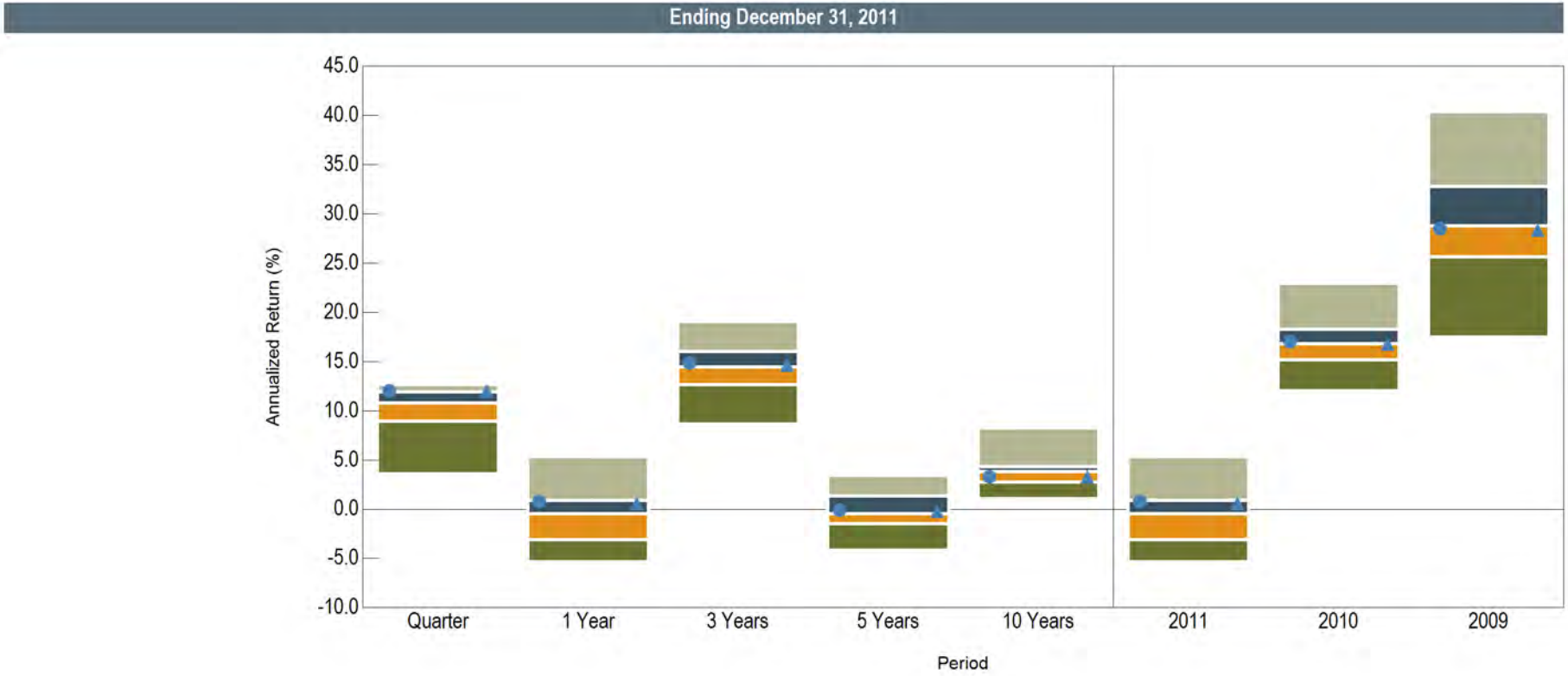

## Quarterly Excess Performance



# Universe Comparison

Benchmark: Russell 3000 ex-Tobacco

Universe: Endowments - US Eq Net



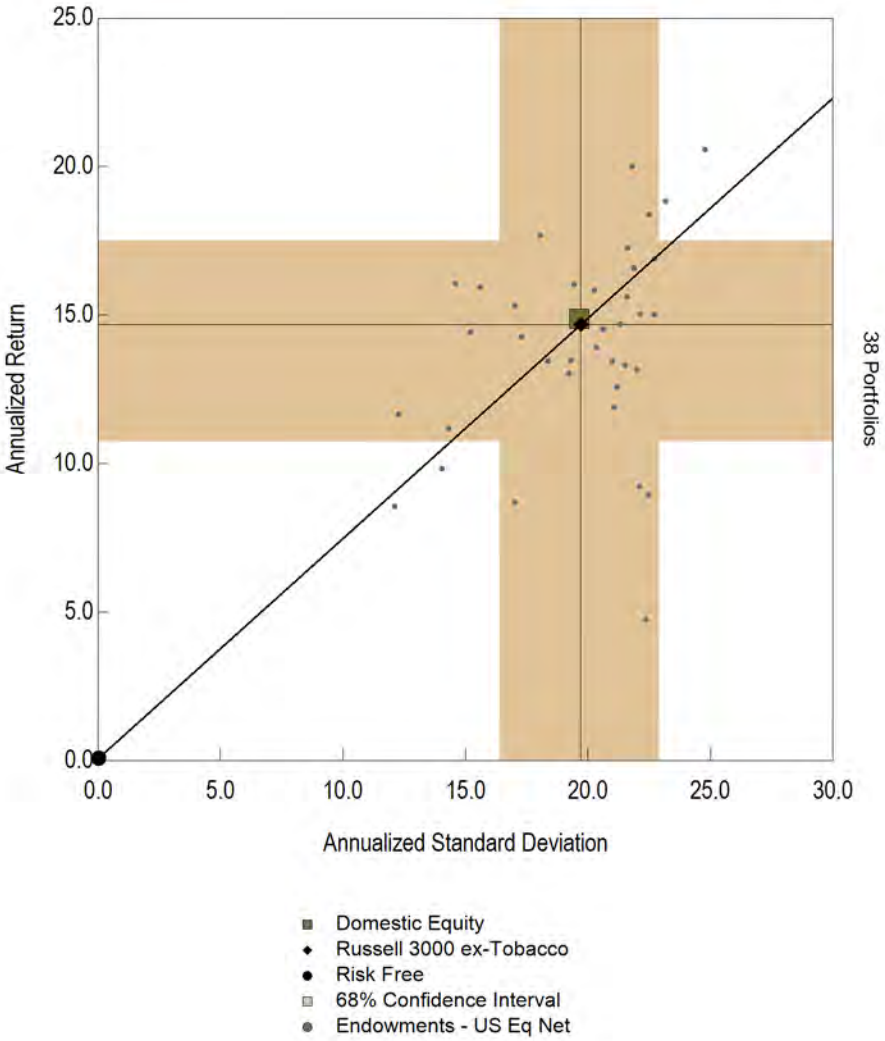

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5th Percentile | 12.6 | | 5.3 | | 19.0 | | 3.4 | | 8.2 | | 5.3 | | 22.9 | | 40.4 | |
| 25th Percentile | 12.0 | | 1.0 | | 16.1 | | 1.4 | | 4.4 | | 1.0 | | 18.3 | | 32.8 | |
| Median | 10.9 | | -0.4 | | 14.5 | | -0.4 | | 3.9 | | -0.4 | | 16.8 | | 28.8 | |
| 75th Percentile | 9.0 | | -3.0 | | 12.7 | | -1.4 | | 2.8 | | -3.0 | | 15.2 | | 25.7 | |
| 95th Percentile | 3.7 | | -5.3 | | 8.7 | | -4.1 | | 1.1 | | -5.3 | | 12.1 | | 17.5 | |
| # of Portfolios | 66 | | 51 | | 38 | | 31 | | 18 | | 51 | | 43 | | 43 | |
| ● Domestic Equity | 12.0 | (20) | 0.8 | (28) | 14.9 | (45) | -0.1 | (48) | 3.3 | (59) | 0.8 | (28) | 17.0 | (48) | 28.5 | (52) |
| ▲ Russell 3000 ex-Tobacco | 12.0 | (23) | 0.6 | (35) | 14.7 | (47) | -0.2 | (49) | 3.3 | (59) | 0.6 | (35) | 16.8 | (51) | 28.4 | (53) |

# Risk Profile

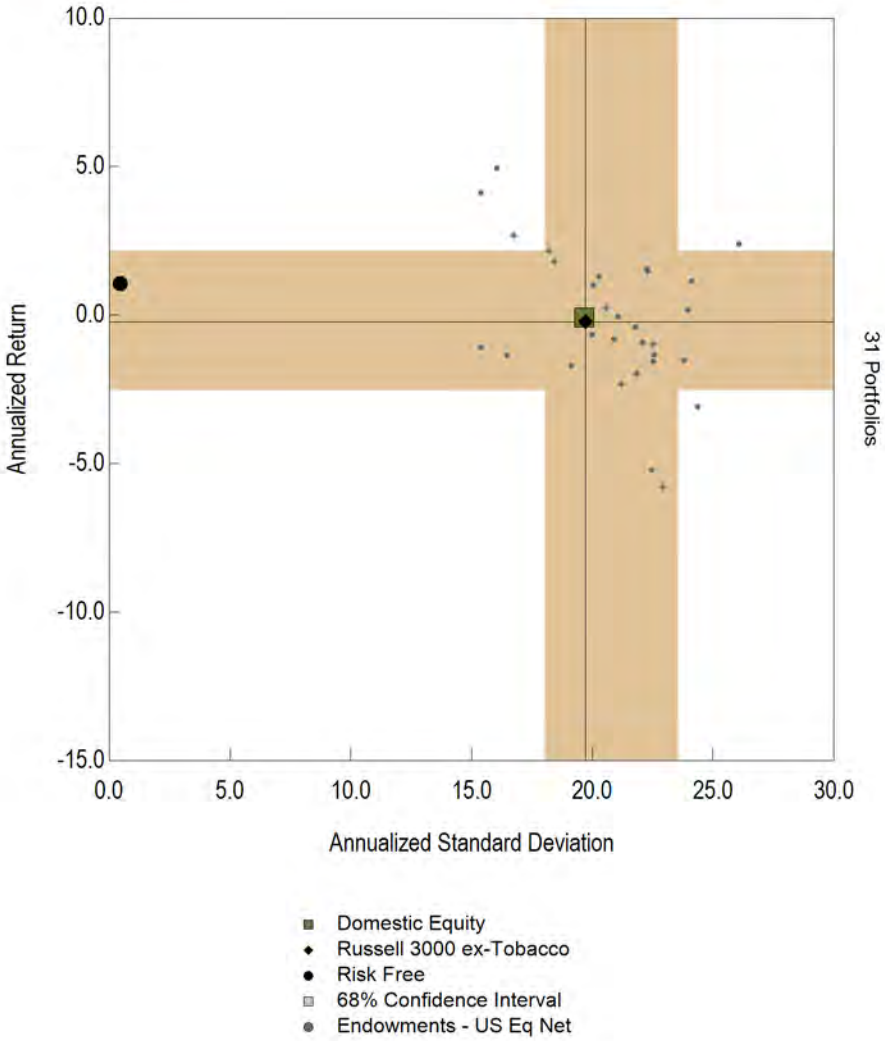
Benchmark: Russell 3000 ex-Tobacco

Universe: Endowments - US Eq Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011

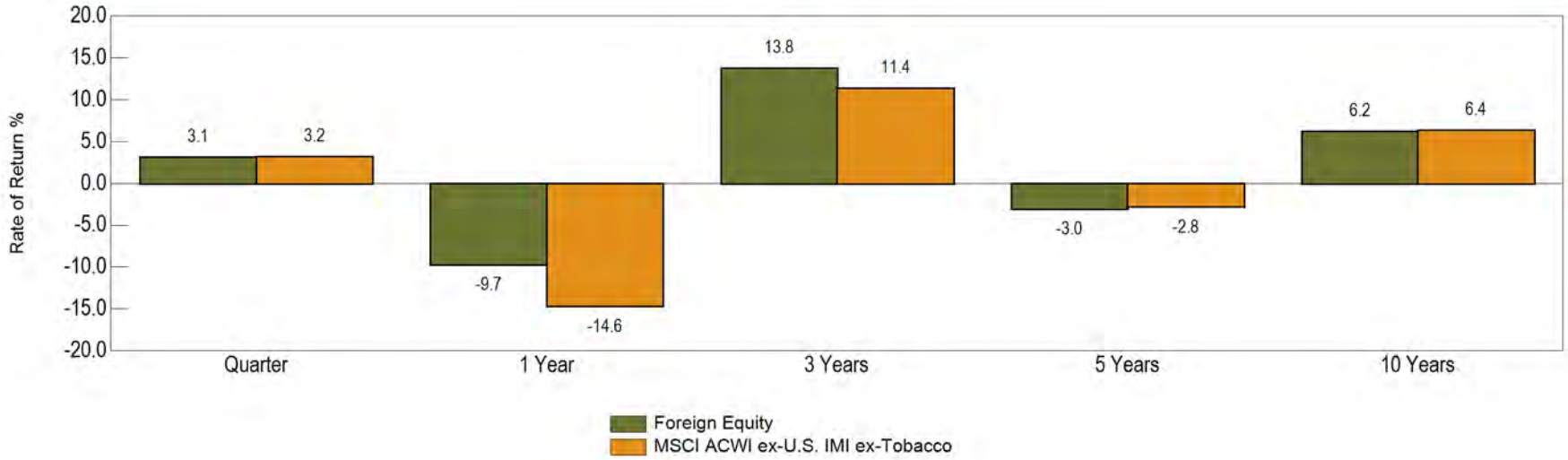


# Foreign Equity

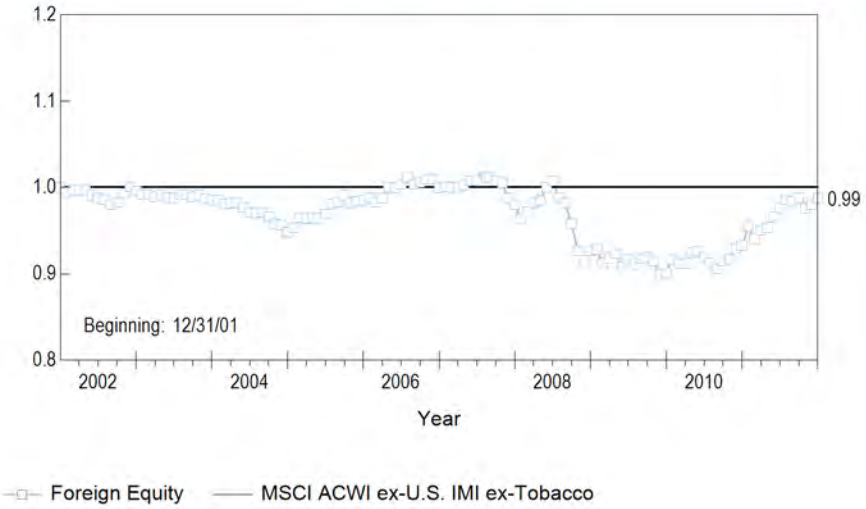
# Overview

Benchmark: MSCI ACWI ex-U.S. IMI ex-Tobacco

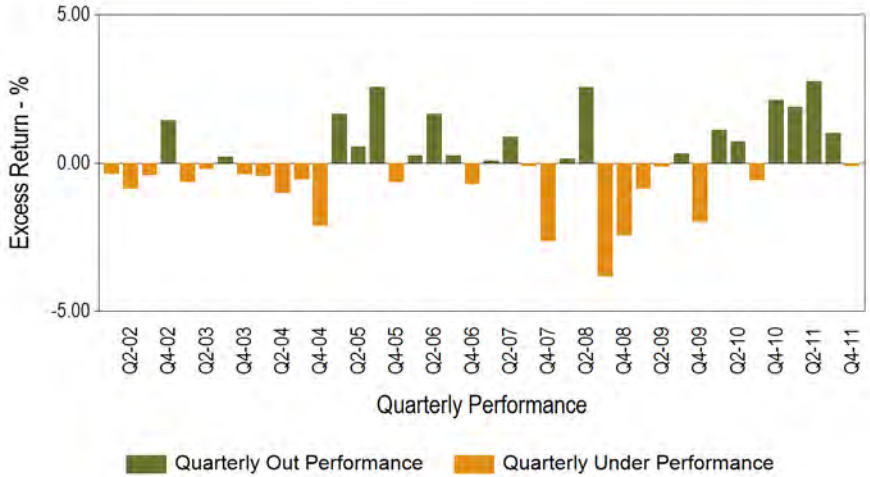
## Return Summary




## Ratio of Cumulative Wealth




## Quarterly Excess Performance

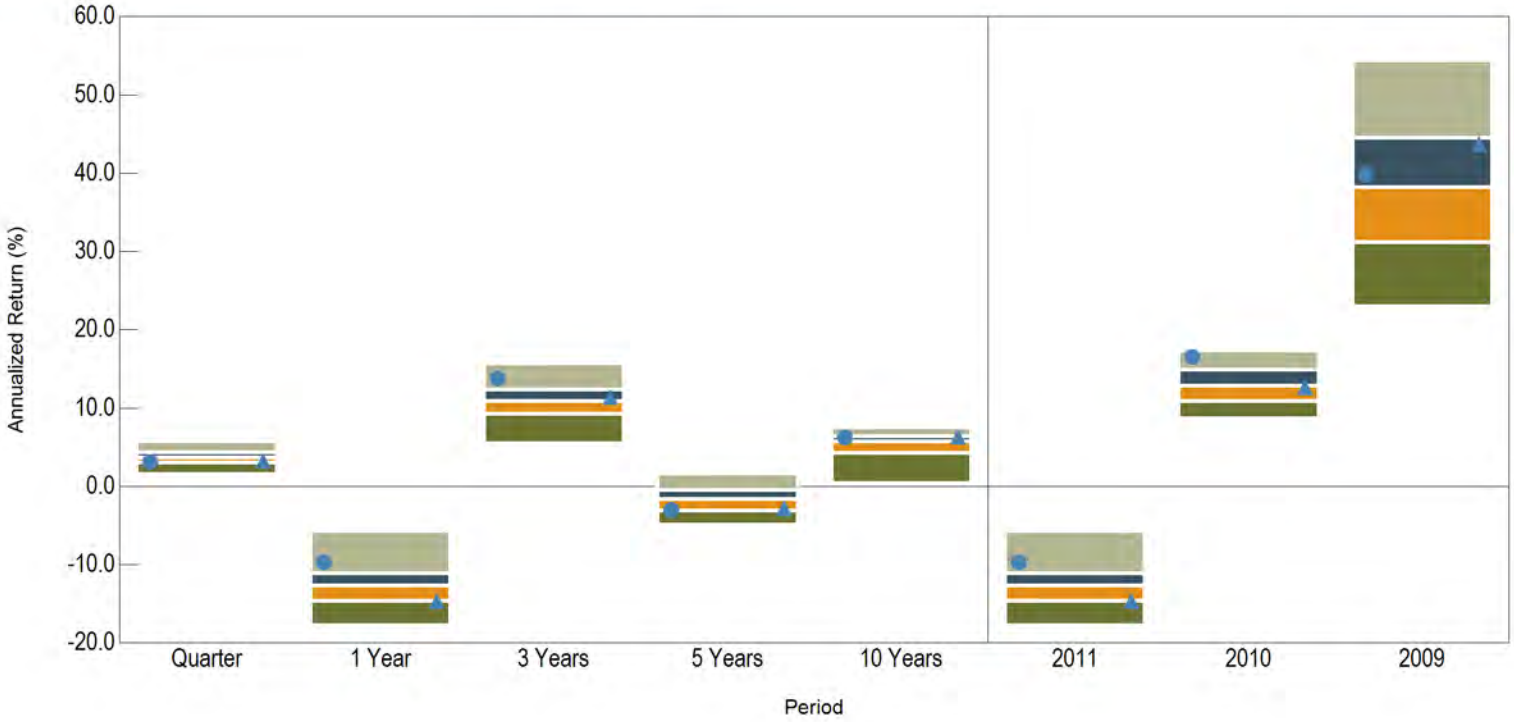


# Universe Comparison

Benchmark: MSCI ACWI ex-U.S. IMI ex-Tobacco

Universe: Endowments - Non-US Eq Net

## Ending December 31, 2011



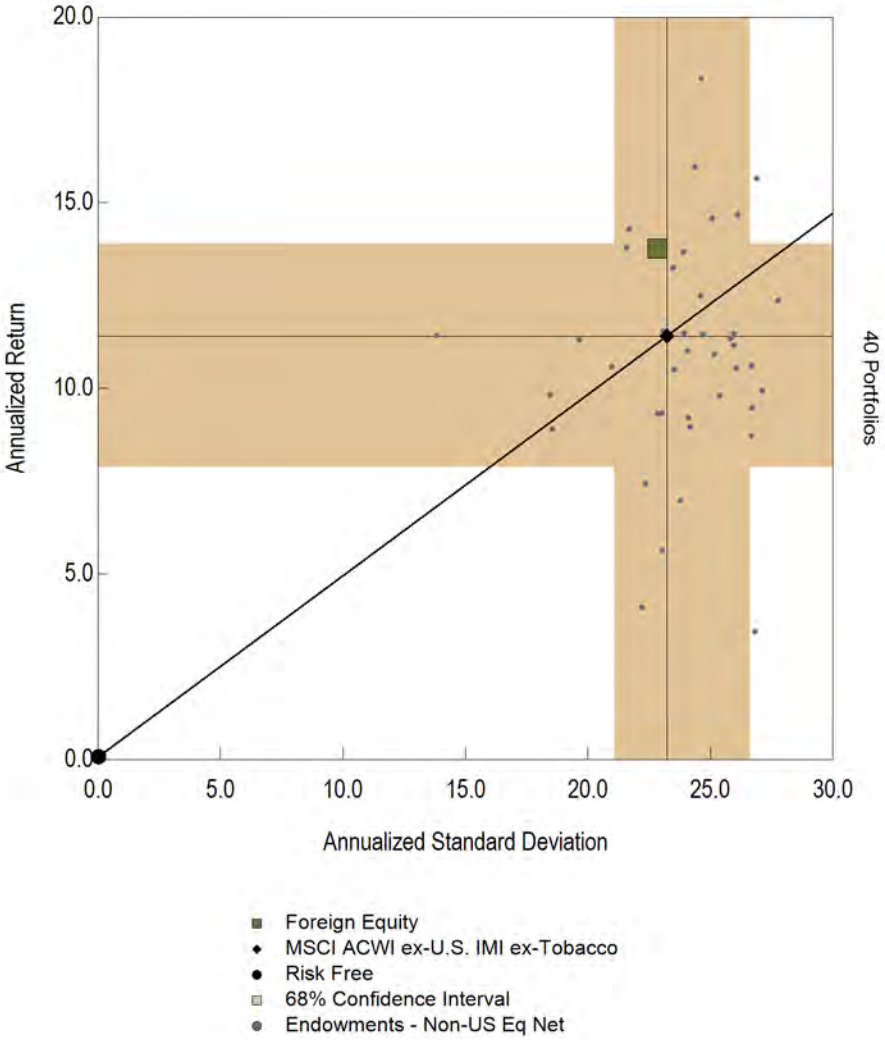

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5th Percentile | 5.7 | | -5.7 | | 15.7 | | 1.6 | | 7.5 | | -5.7 | | 17.3 | | 54.4 | |
| 25th Percentile | 4.4 | | -11.0 | | 12.4 | | -0.4 | | 6.4 | | -11.0 | | 15.0 | | 44.6 | |
| Median | 3.8 | | -12.6 | | 11.0 | | -1.6 | | 5.8 | | -12.6 | | 12.9 | | 38.3 | |
| 75th Percentile | 3.1 | | -14.6 | | 9.3 | | -3.0 | | 4.3 | | -14.6 | | 11.0 | | 31.2 | |
| 95th Percentile | 1.6 | | -17.7 | | 5.6 | | -4.9 | | 0.5 | | -17.7 | | 8.7 | | 23.1 | |
| # of Portfolios | 63 | | 51 | | 40 | | 34 | | 18 | | 51 | | 46 | | 48 | |
| ● Foreign Equity | 3.1 | (75) | -9.7 | (14) | 13.8 | (17) | -3.0 | (75) | 6.2 | (31) | -9.7 | (14) | 16.6 | (15) | 39.8 | (36) |
| ▲ MSCI ACWI ex-U.S. IMI ex-Tobacco | 3.2 | (74) | -14.6 | (76) | 11.4 | (39) | -2.8 | (67) | 6.4 | (26) | -14.6 | (76) | 12.7 | (54) | 43.8 | (28) |

# Risk Profile

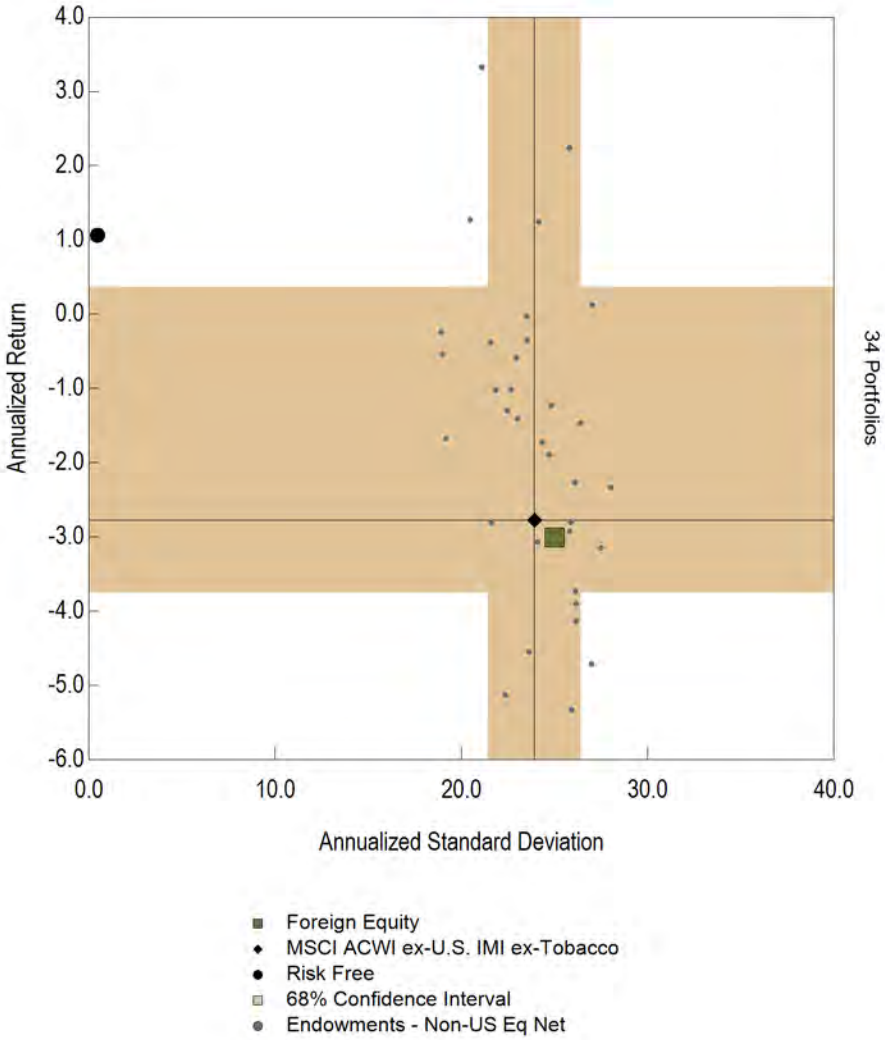
Benchmark: MSCI ACWI ex-U.S. IMI ex-Tobacco

Universe: Endowments - Non-US Eq Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011

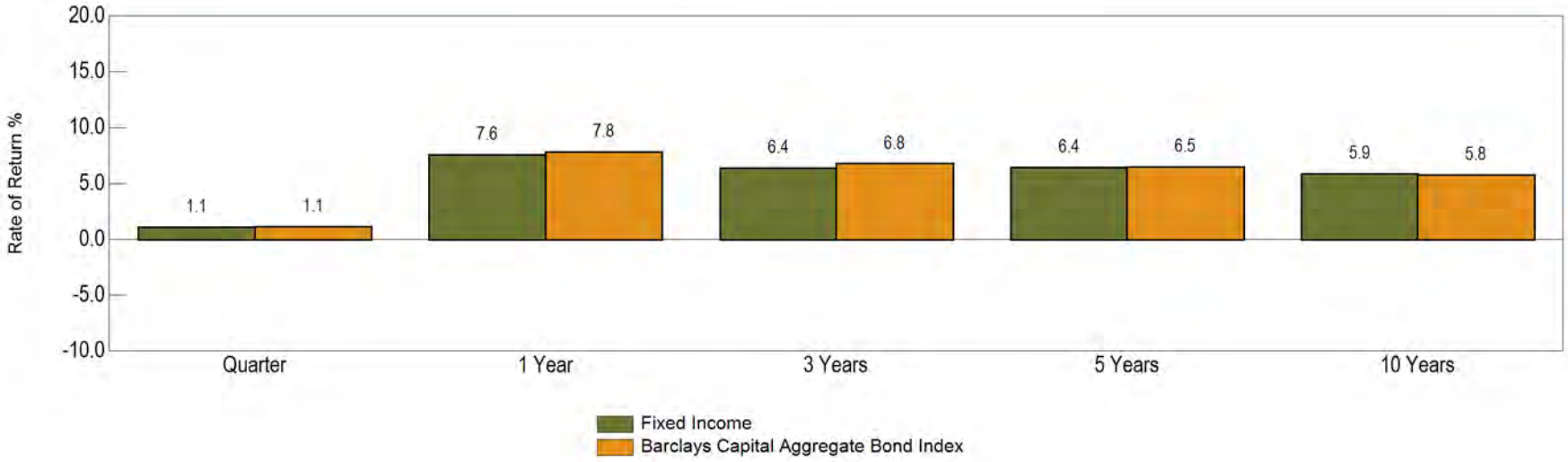


# Fixed Income

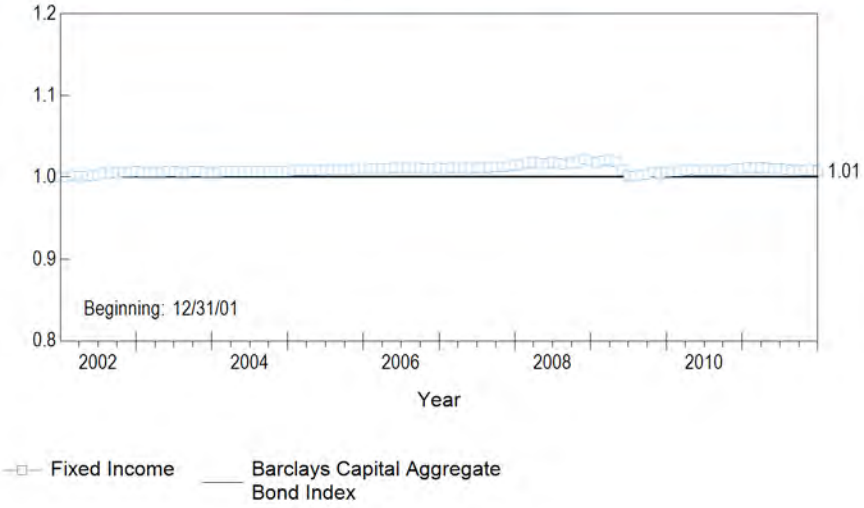
# Overview

Benchmark: Barclays Capital Aggregate Bond Index

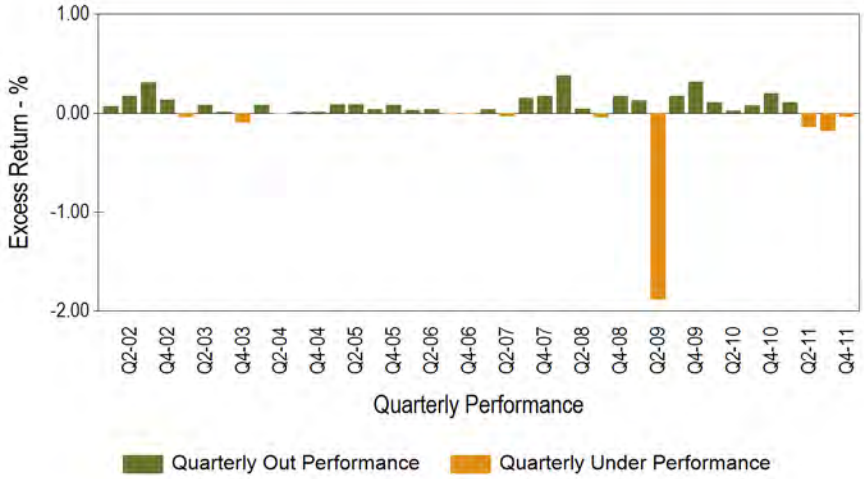
## Return Summary




## Ratio of Cumulative Wealth




## Quarterly Excess Performance

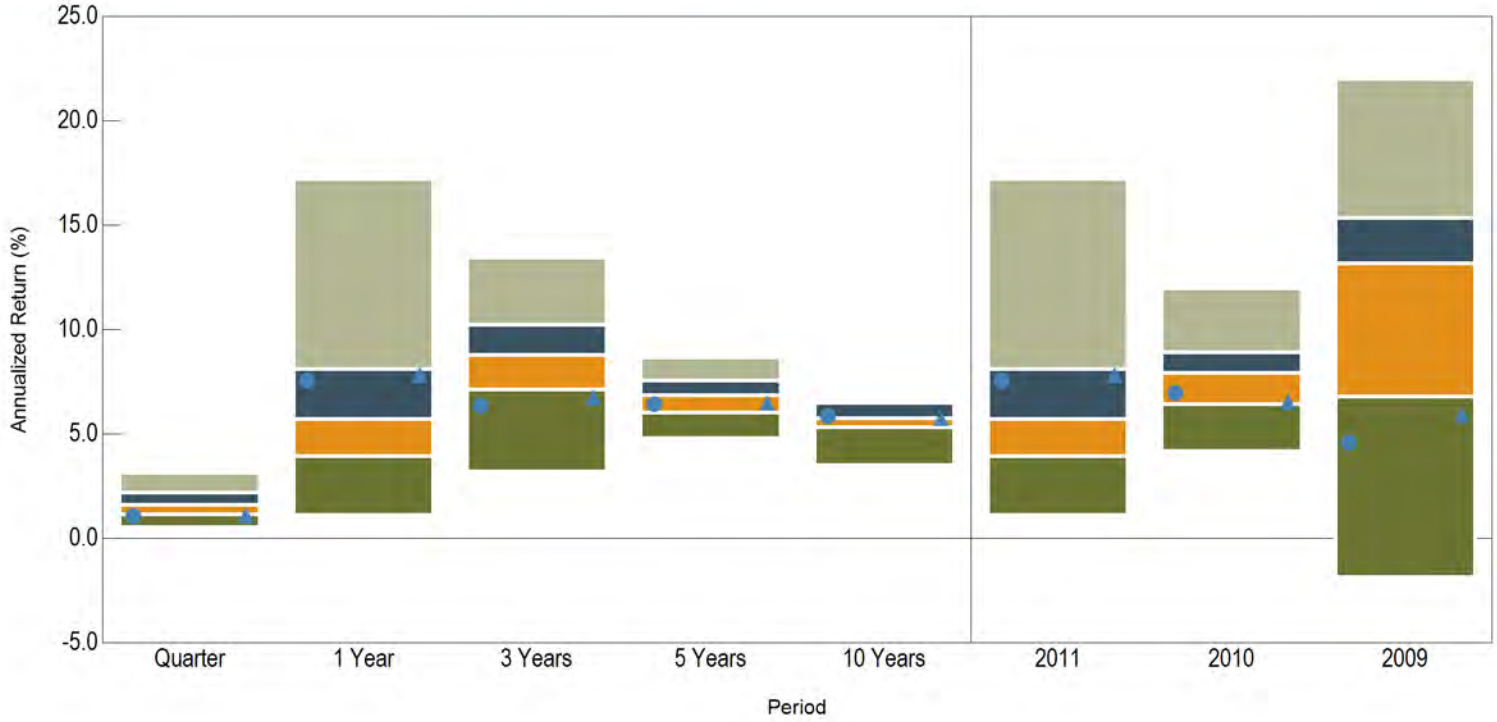


# Universe Comparison

Benchmark: Barclays Capital Aggregate Bond Index

Universe: Endowments - US FI Net

## Ending December 31, 2011



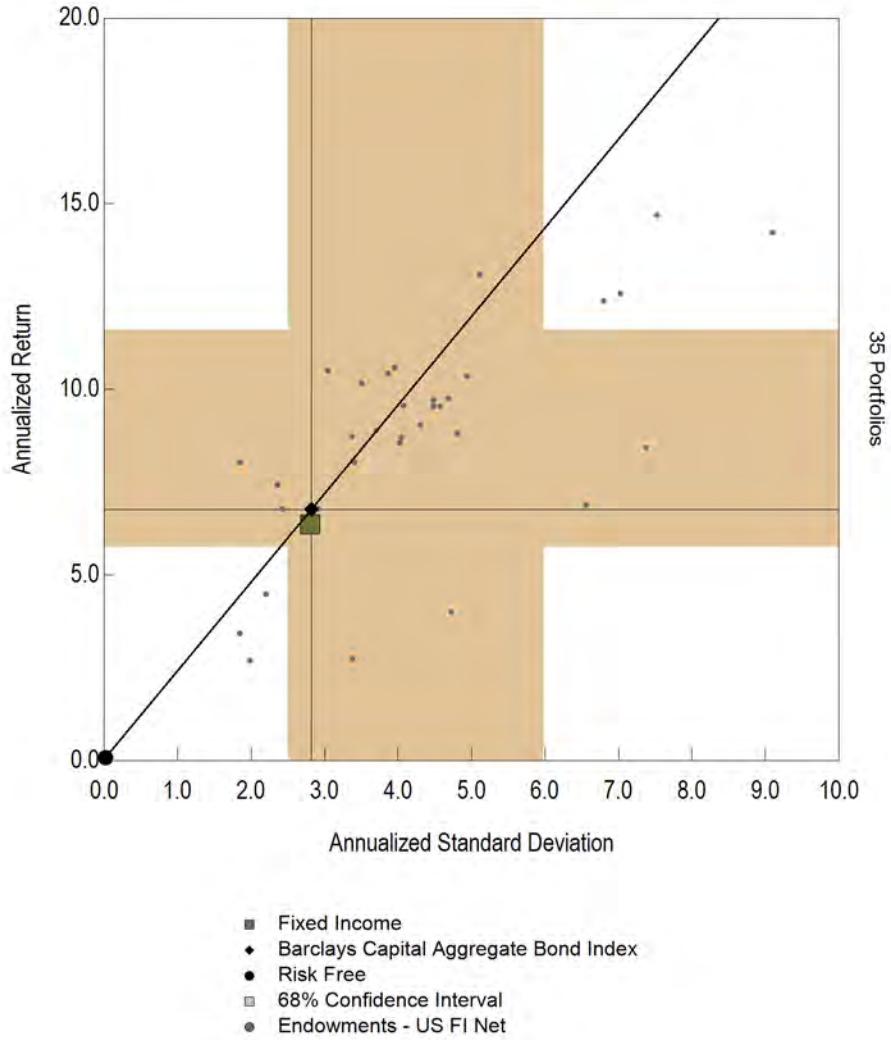

| | Return (Rank) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **5th Percentile** | 3.1 | | 17.2 | | 13.4 | | 8.7 | | 6.6 | | 17.2 | | 12.0 | | 22.0 | |
| **25th Percentile** | 2.2 | | 8.1 | | 10.3 | | 7.6 | | 6.5 | | 8.1 | | 8.9 | | 15.4 | |
| **Median** | 1.6 | | 5.7 | | 8.8 | | 6.9 | | 5.8 | | 5.7 | | 8.0 | | 13.2 | |
| **75th Percentile** | 1.2 | | 4.0 | | 7.2 | | 6.1 | | 5.3 | | 4.0 | | 6.4 | | 6.8 | |
| **95th Percentile** | 0.6 | | 1.2 | | 3.2 | | 4.8 | | 3.5 | | 1.2 | | 4.2 | | -1.8 | |
| **# of Portfolios** | 65 | | 49 | | 35 | | 26 | | 19 | | 49 | | 41 | | 46 | |
| ● **Fixed Income** | 1.1 | (78) | 7.6 | (32) | 6.4 | (85) | 6.4 | (68) | 5.9 | (45) | 7.6 | (32) | 7.0 | (73) | 4.6 | (85) |
| ▲ **Barclays Capital Aggregate Bond Index** | 1.1 | (78) | 7.8 | (29) | 6.8 | (83) | 6.5 | (66) | 5.8 | (49) | 7.8 | (29) | 6.5 | (75) | 5.9 | (78) |

# Risk Profile

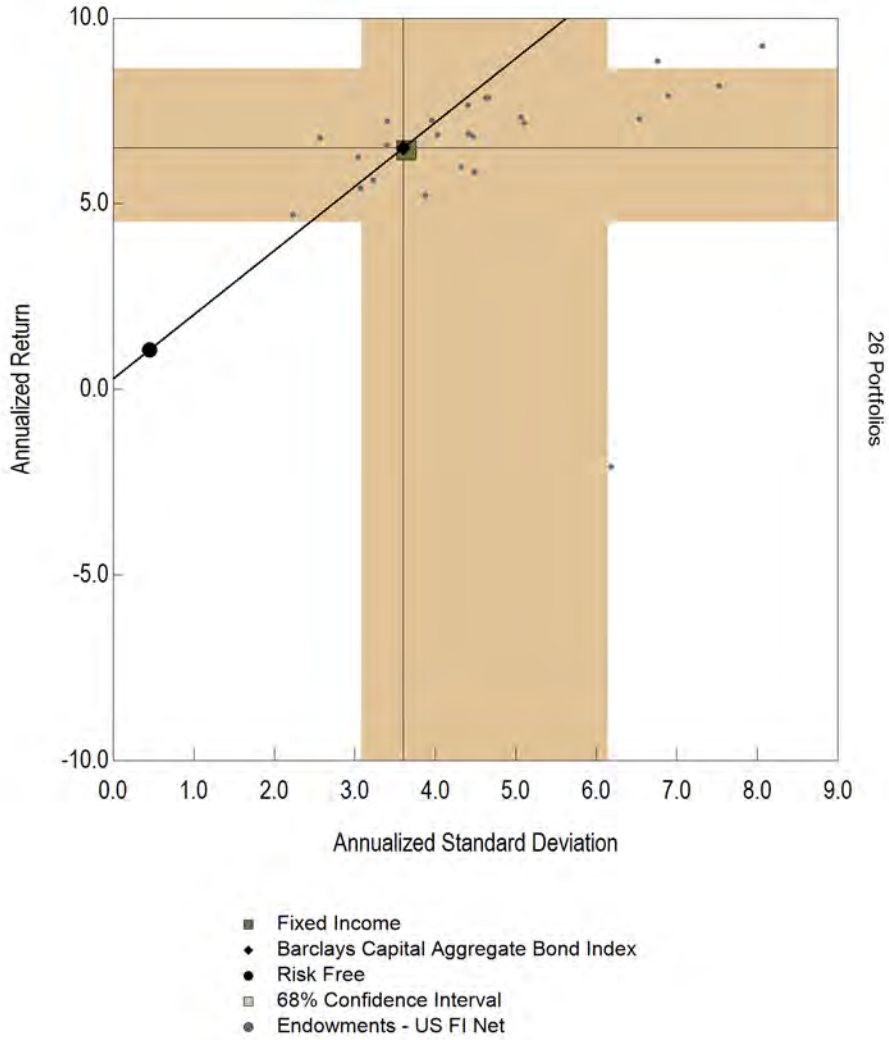
Benchmark: Barclays Capital Aggregate Bond Index

Universe: Endowments - US FI Net

## Annualized Return vs. Annualized Standard Deviation
3 Years Ending December 31, 2011




## Annualized Return vs. Annualized Standard Deviation
5 Years Ending December 31, 2011

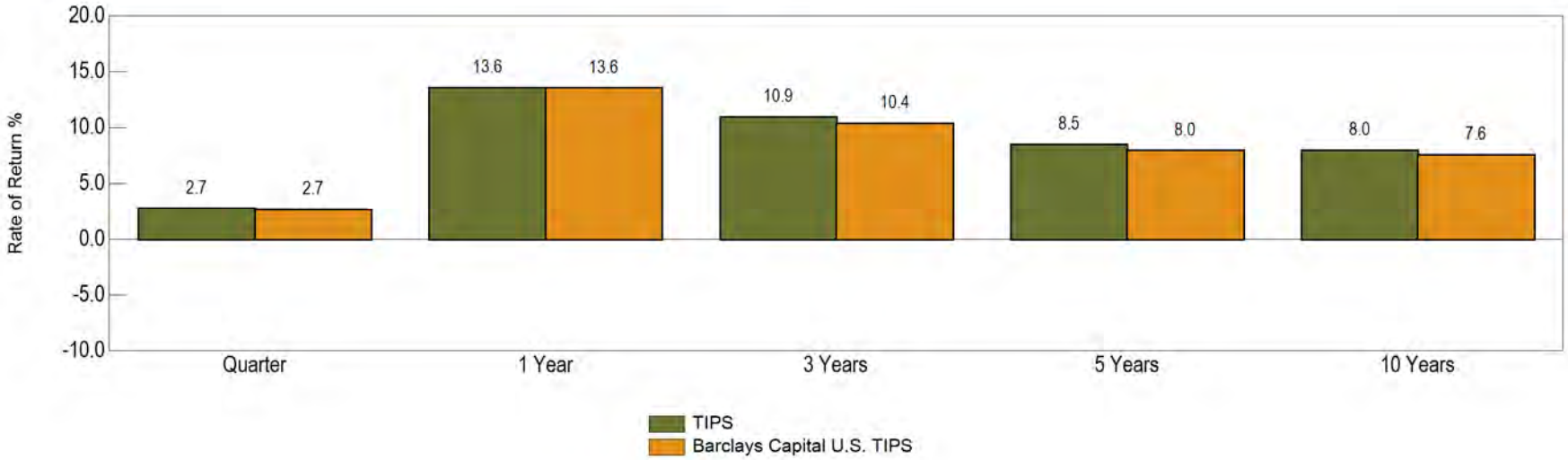


# TIPS

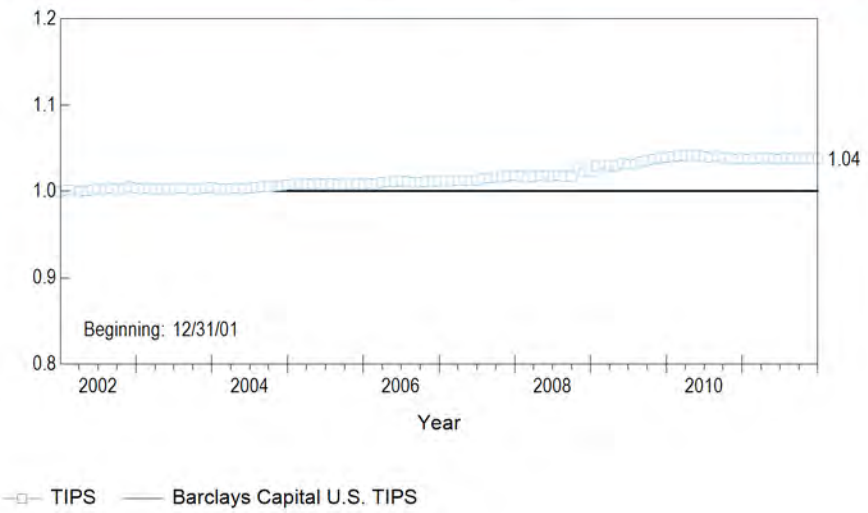
# Overview

Benchmark: Barclays Capital U.S. TIPS

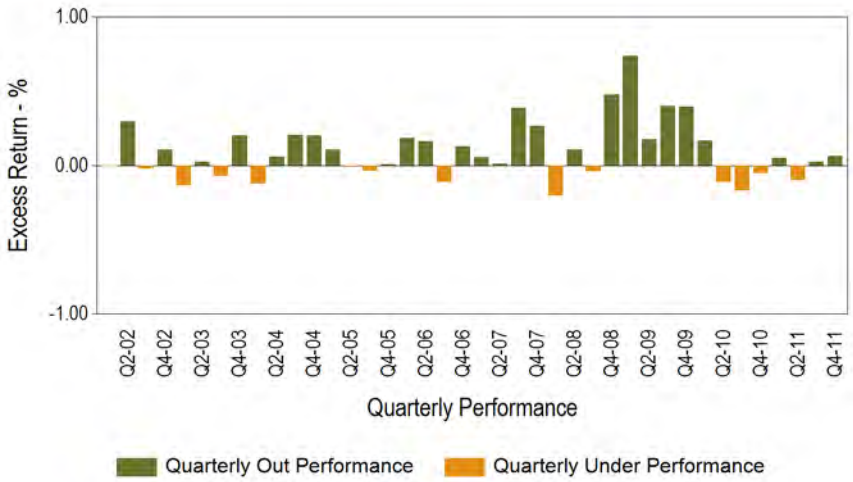
## Return Summary




## Ratio of Cumulative Wealth

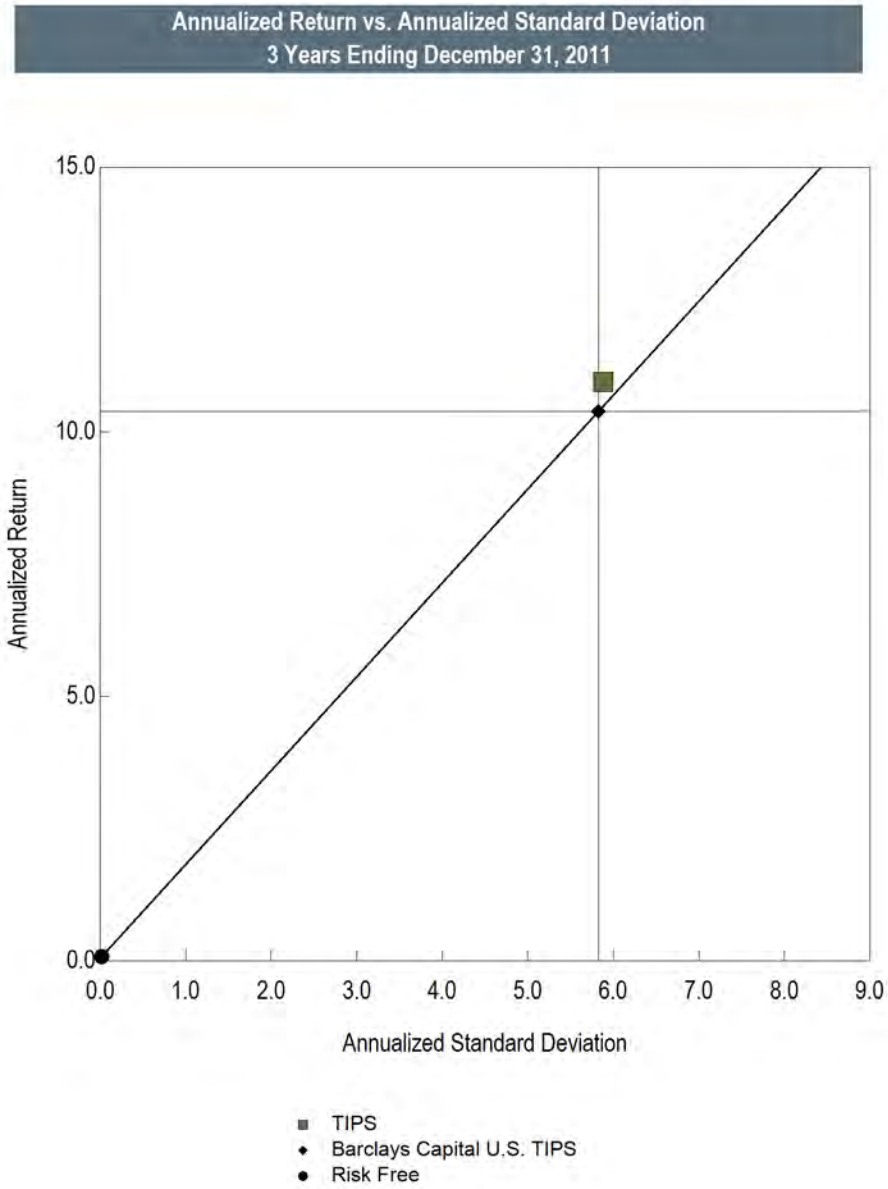


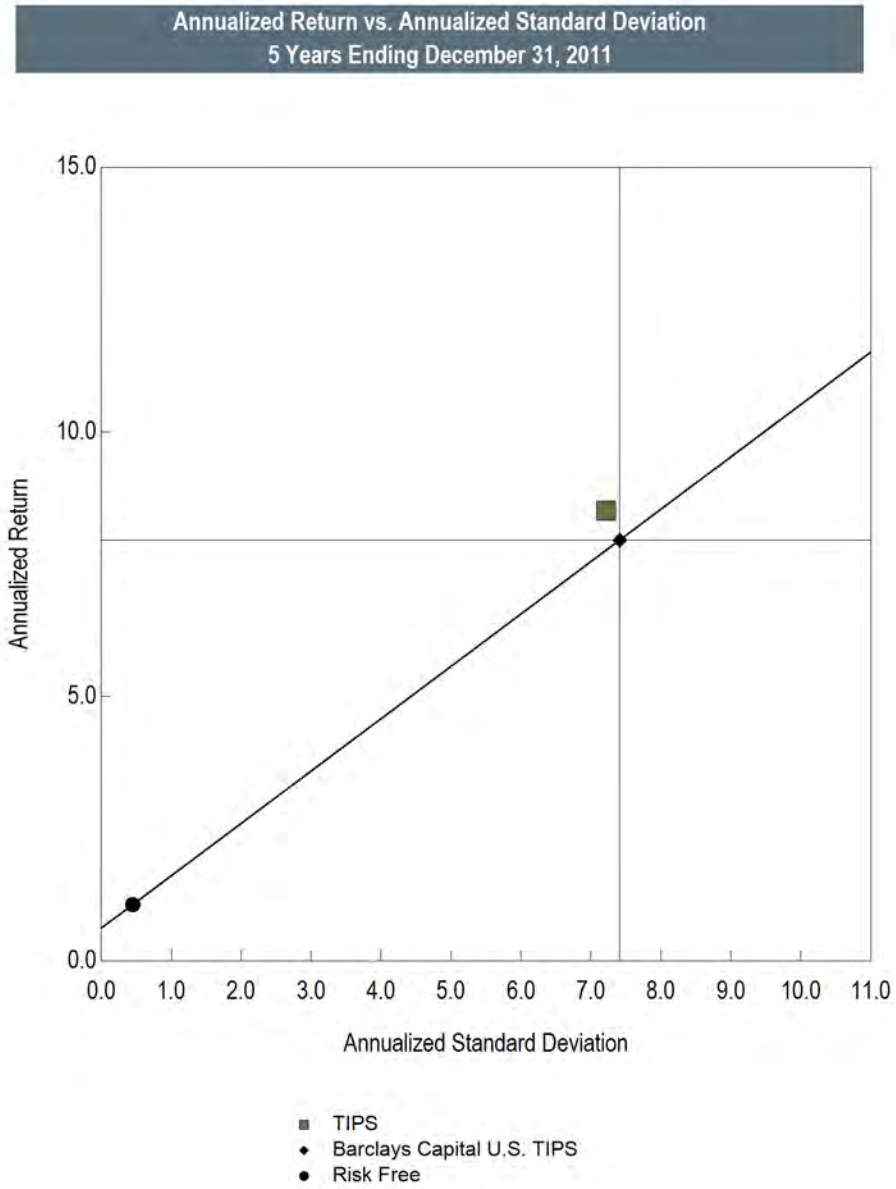

## Quarterly Excess Performance



# Risk Profile

Benchmark: Barclays Capital U.S. TIPS



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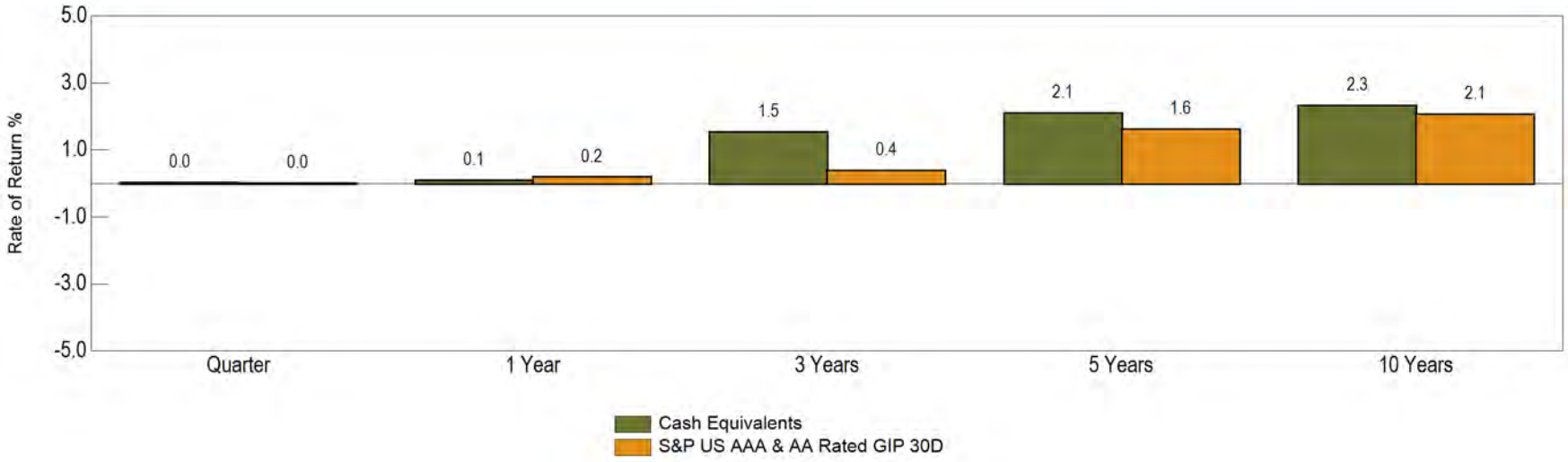
# Cash Equivalents

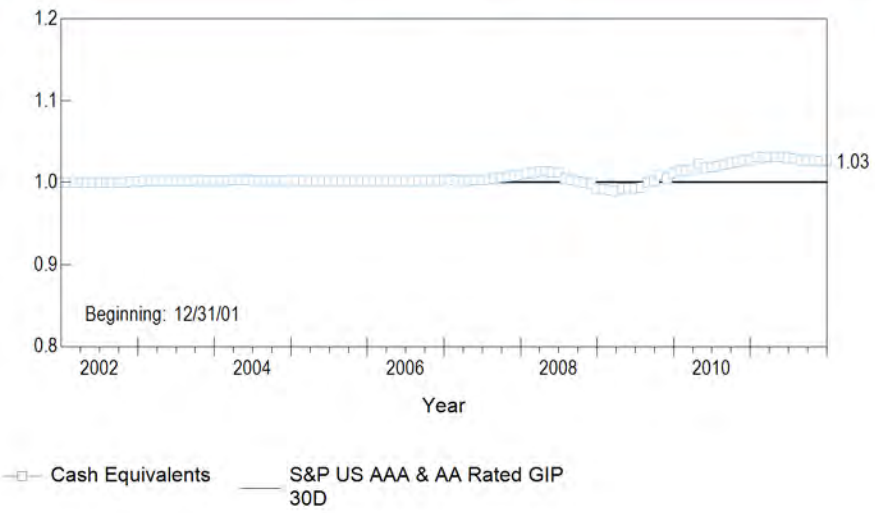
# Overview

Benchmark: S&P US AAA & AA Rated GIP 30D

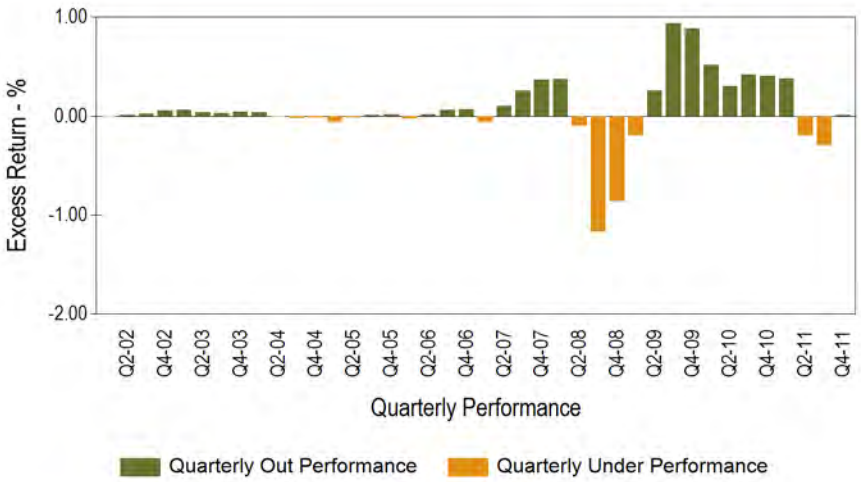
## Return Summary




## Ratio of Cumulative Wealth

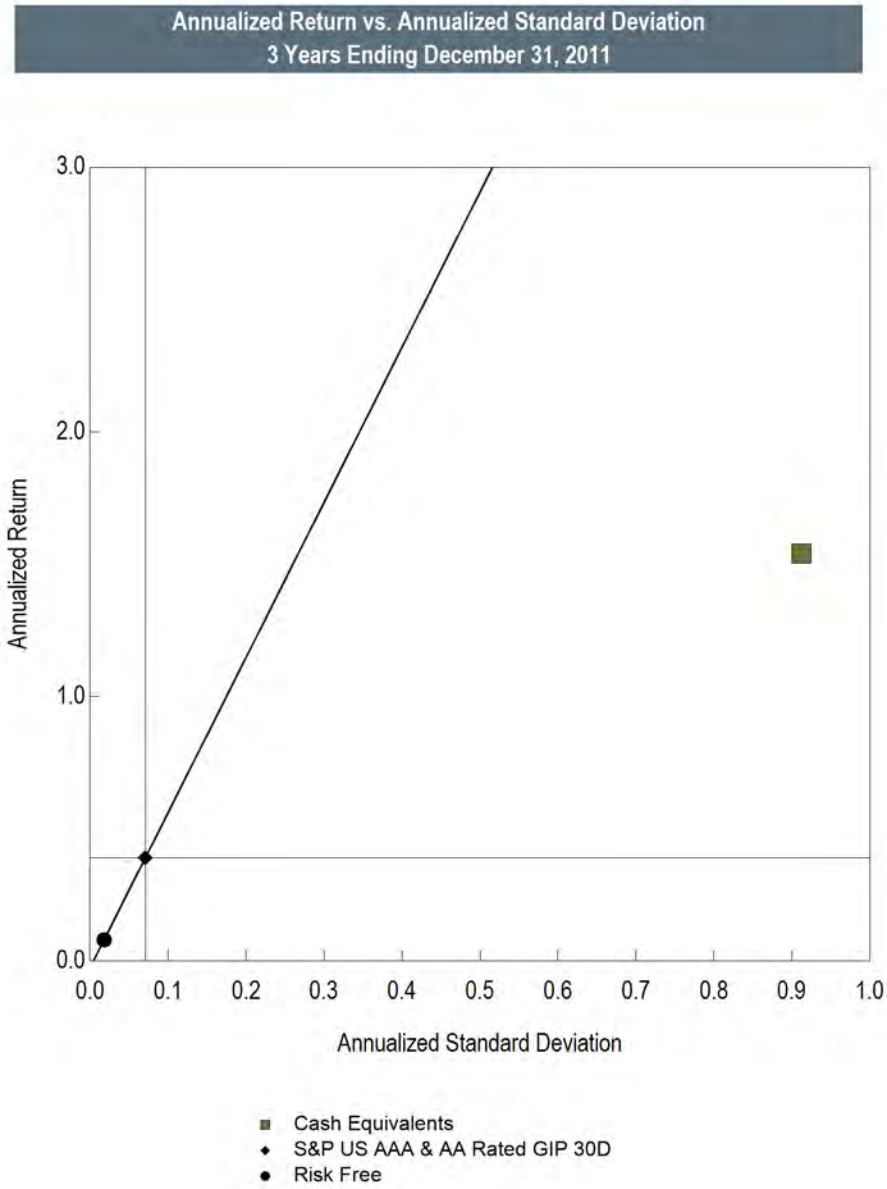


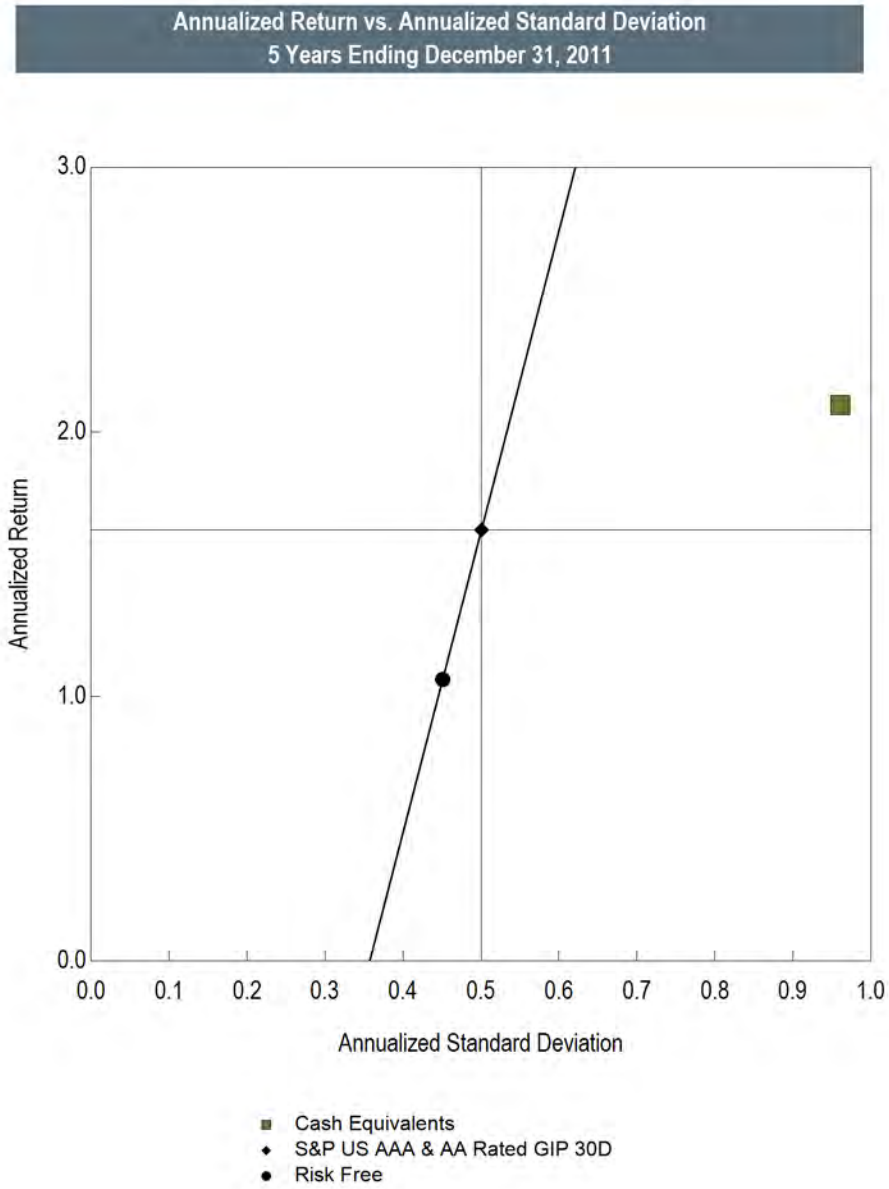

## Quarterly Excess Performance



# Risk Profile

Benchmark: S&P US AAA & AA Rated GIP 30D



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# Appendix

# Securities Lending

## Lawton Chiles Endowment Fund

| | LOANS | | |
|---|---|---|---|
| Lending Agent | Lendable Base | Market Value on Loan | % on Loan |
| Bank of New York Mellon | $593,295,907 | $74,846,959 | 12.62% |
| ClearLend (formerly Wachovia) | --- | --- | --- |
| Total Lawton Chiles Endowment Fund | $593,295,907 | $74,846,959 | 12.62% |

| | REINVESTMENT | | |
|---|---|---|---|
| Lending Agent | Book Value | Market Value | Unrealized Gain/(Loss) |
| Bank of New York Mellon | $76,848,919 | $76,839,581 | ($9,338) |
| ClearLend (formerly Wachovia) | --- | --- | --- |
| Total Lawton Chiles Endowment Fund | $76,848,919 | $76,839,581 | ($9,338) |

# Market Returns

| | Fourth Quarter | Annualized Periods Ending 12/31/11 | | | | |
|---|---|---|---|---|---|---|
| | | 1-Year | 3-Year | 5-Year | 10-Year | 15-Year |
| **Domestic Stock Indices:** | | | | | | |
| Dow Jones US Total Stock Index | 12.1 | 1.1 | 15.2 | 0.2 | 3.9 | 5.8 |
| S&P 500 Index | 11.8 | 2.1 | 14.1 | -0.3 | 2.9 | 5.5 |
| Russell 3000 Index | 12.1 | 1.0 | 14.9 | 0.0 | 3.5 | 5.7 |
| Russell 1000 Value Index | 13.1 | 0.4 | 11.5 | -2.6 | 3.9 | 6.3 |
| Russell 1000 Growth Index | 10.6 | 2.6 | 18.0 | 2.5 | 2.6 | 4.5 |
| Russell MidCap Value Index | 13.4 | -1.4 | 18.2 | 0.0 | 7.7 | 8.9 |
| Russell MidCap Growth Index | 11.2 | -1.7 | 22.1 | 2.4 | 5.3 | 6.5 |
| Russell 2000 Value Index | 16.0 | -5.5 | 12.4 | -1.9 | 6.4 | 8.0 |
| Russell 2000 Growth Index | 15.0 | -2.9 | 19.0 | 2.1 | 4.5 | 3.9 |
| **Domestic Bond Indices:** | | | | | | |
| Barclays Capital Aggregate Index | 1.1 | 7.8 | 6.8 | 6.5 | 5.8 | 6.3 |
| Barclays Capital Govt/Credit Index | 1.2 | 8.7 | 6.6 | 6.5 | 5.9 | 6.4 |
| Barclays Capital Long Govt/Credit Index | 2.6 | 22.5 | 11.2 | 9.7 | 8.5 | 8.4 |
| Barclays Capital 1-3 Year Govt/Credit Index | 0.2 | 1.6 | 2.7 | 4.0 | 3.6 | 4.6 |
| Barclays Capital U.S. MBS Index | 0.9 | 6.2 | 5.8 | 6.5 | 5.7 | 6.3 |
| Barclays Capital High Yield Index | 6.5 | 5.0 | 24.1 | 7.5 | 8.9 | 6.9 |
| Barclays Capital Universal Index | 1.4 | 7.4 | 7.7 | 6.4 | 6.0 | 6.4 |
| **Real Estate Indices:** | | | | | | |
| NCREIF Property Index | 3.0 | 14.3 | 2.4 | 3.1 | 8.1 | 9.4 |
| NCREIF ODCE Index | 2.7 | 15.0 | -2.7 | -1.1 | 5.2 | 7.3 |
| Dow Jones Real Estate Securities Index | 15.3 | 8.9 | 21.7 | -2.2 | 10.1 | 9.0 |
| FTSE NAREIT US Real Estate Index | 15.3 | 8.3 | 21.0 | -1.4 | 10.2 | 8.9 |
| **Foreign/Global Stock Indices:** | | | | | | |
| MSCI All Country World Index | 7.2 | -7.3 | 12.0 | -1.9 | 4.2 | 4.5 |
| MSCI All Country World IMI | 7.2 | -7.9 | 12.8 | -1.6 | 4.9 | 4.6 |
| MSCI All Country World ex-U.S. Index | 3.7 | -13.7 | 10.7 | -2.9 | 6.3 | 4.4 |
| MSCI All Country World ex-U.S. IMI | 3.3 | -14.3 | 11.5 | -2.7 | 6.9 | 4.3 |
| MSCI All Country World ex-U.S. Small Cap Index | 0.4 | -18.5 | 18.5 | -1.7 | 10.6 | 5.3 |
| MSCI EAFE Index | 3.3 | -12.1 | 7.6 | -4.7 | 4.7 | 3.4 |
| MSCI EAFE IMI | 2.9 | -12.6 | 8.4 | -4.6 | 5.3 | 3.6 |
| MSCI EAFE Index (in local currency) | 4.1 | -12.2 | 4.7 | -6.6 | 0.7 | 2.3 |
| MSCI Emerging Markets IMI | 3.8 | -19.5 | 20.7 | 2.6 | 13.8 | 5.1 |
| **Foreign Bond Indices:** | | | | | | |
| Citigroup World Gov't Bond Index | -0.5 | 5.2 | 4.9 | 7.2 | 8.4 | 5.5 |
| Citigroup Hedged World Gov't Bond Index | 0.6 | 4.1 | 3.0 | 4.3 | 4.4 | 5.7 |
| **Cash Equivalents:** | | | | | | |
| Treasury Bills (30-Day) | 0.0 | 0.0 | 0.1 | 1.1 | 1.5 | 2.5 |
| EnnisKnupp STIF Index | 0.0 | 0.2 | 0.4 | 1.8 | 2.2 | 3.3 |
| **Inflation Index:** | | | | | | |
| Consumer Price Index | -0.5 | 3.0 | 2.4 | 2.3 | 2.5 | 2.4 |

# Benchmark Descriptions

**LCEF Total Fund**

Total Endowment Target - A weighted blend of the individual asset class target benchmarks.

**Total Domestic Equity**

Russell 3000 Index ex-Tobacco - An index that measures the performance of the 3,000 stocks that make up the Russell 1000 and Russell 2000 Indices, while excluding tobacco companies.

**Total Foreign Equity**

MSCI ACWI ex-U.S. IMI ex-Tobacco - A capitalization-weighted index representing 44 countries, but excluding the United States. The Index includes 23 developed and 21 emerging market countries, and excludes tobacco companies.

**Total Fixed Income**

Barclays Capital Aggregate Bond Index - A market value-weighted index consisting of the Barclays Capital Credit, Government, and Mortgage-Backed Securities Indices. The Index also includes credit card, auto, and home equity loan-backed securities. This Index is the broadest available measure of the aggregate investment grade U.S. fixed income market.

**Total TIPS**

Barclays Capital U.S. TIPS - A market value-weighted index consisting of U.S. Treasury Inflation-Protected Securities with one or more years remaining until maturity with total outstanding issue size of $500 million or more.

**Total Cash Equivalents**

S&P U.S. AAA & AA Rated GIP 30 Day - An unmanaged market index representative of the Local Government Investment Pool.

# Universe Descriptions

**LCEF Total Fund**

A universe comprised of 96 total endowment portfolio returns, net of fees, calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $191.7 billion as of quarter-end and the average market value was $1.7 billion.

**Total Domestic Equity**

A universe comprised of 66 total domestic equity portfolio returns, net of fees, of endowment plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $49.0 billion as of quarter-end and the average market value was $458.0 million.

**Total Foreign Equity**

A universe comprised of 63 total foreign equity portfolio returns, net of fees, of endowment plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $18.6 billion as of quarter-end and the average market value was $185.8 million.

**Total Fixed Income**

A universe comprised of 65 total fixed income portfolio returns, net of fees, of endowment plans calculated and provided by BNY Mellon Performance & Risk Analytics. Aggregate assets in the universe comprised $24.4 billion as of quarter-end and the average market value was $253.7 million.

# Explanation of Exhibits

**Quarterly and Cumulative Excess Performance** - The vertical axis, excess return, is a measure of fund performance less the return of the primary benchmark. The horizontal axis represents the time series. The quarterly bars represent the underlying funds' relative performance for the quarter.

**Risk-Return Graph** - The horizontal axis, annualized standard deviation, is a statistical measure of risk, or the volatility of returns. The vertical axis is the annualized rate of return. As investors generally prefer less risk to more risk and always prefer greater returns, the upper left corner of the graph is the most attractive place to be. The line on this exhibit represents the risk and return tradeoffs associated with market portfolios, or index funds.

**Ratio of Cumulative Wealth Graph** - An illustration of a portfolio's cumulative, un-annualized performance relative to that of its benchmark. An upward-sloping line indicates superior fund performance versus its benchmark. Conversely, a downward-sloping line indicates underperformance by the fund. A flat line is indicative of benchmark-like performance.

**Performance Comparison - Universe Comparison** - An illustration of the distribution of returns for a particular asset class. The component's return is indicated by the circle and its performance benchmark by the triangle. The top and bottom borders represent the 5th and 95th percentiles, respectively. The solid line indicates the median while the dotted lines represent the 25th and 75th percentiles.

End of Section

**MINUTES**
**INVESTMENT ADVISORY COUNCIL**
**DECEMBER 5, 2011**

**A meeting of the Investment Advisory Council (IAC) was held on Monday, December 5, 2011, in the Hermitage Room of the State Board of Administration of Florida (SBA), Tallahassee, Florida.**

**Members Present:** **Rob Gidel, Chair**
**David Grain, Vice Chair**
**Les Daniels**
**Martin Garcia**
**John Hill**
**John Jaeb**
**Chuck Newman**
**Michael Price**
**Gary Wendt**

## CALL TO ORDER/APPROVAL OF MINUTES

**Mr. Rob Gidel, Chair, called the meeting to order at 1:00 PM. Mr. Gidel introduced newly appointed IAC members Gary Wendt and Michael Price. Mr. Gidel requested a motion to approve the minutes of the September 19, 2011, IAC meeting. Mr. Chuck Newman made the motion to approve the minutes; seconded by Mr. John Hill; approved without objection.**

**Mr. Garcia inquired concerning lack of mention in the minutes related to the question of responding to Senator Fasano's information requests in his individual capacity versus his legislative committee capacity. Mr. Garcia suggested the minutes be amended to include points concerning the discussion that if Senator Mike Fasano had gone through the legislative process as opposed to asking in his individual capacity, that the records he requested would be produced cost free and that there would be certain hurdles and barriers that would not apply. Mr. Gidel asked if there were any objections. Seeing none, Mr. Grain moved to amend the minutes accordingly. The motion was seconded by Mr. Daniels; and the minutes were approved, as amended, without objection.**

## OPENING REMARKS/REPORTS

**Mr. Ash Williams, Executive Director and Chief Investment Officer, opened his comments with the current funding level of the pension fund, brief comments concerning the expanded investment authority the SBA is seeking from the legislature, and the new content, format, and meeting materials for IAC meetings. Mr. Williams introduced two new Senior Investment Officers, Steve Spook, Real Estate, and Katy Wojciechowski, Fixed Income, and reported on the status of the searches for the Senior Investment Officer for Private Equity & Strategic Investments and the Inspector General positions.**

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**MAJOR INITIATIVES UPDATE**

**Mr. Kevin SigRist, Deputy Executive Director, began his presentation by highlighting the risk management and compliance report and asked that Eric Nelson, Chief Risk and Compliance Officer explain the report for the new IAC members. Mr. Nelson provided an overview of the report. Mr. Gary Wendt requested clarification of an investment exception which was explained by Mr. Nelson as a minor "below the floor of policy" violation. Mr. SigRist also added to the discussion on the exception.**

**Mr. SigRist discussed Hewitt EnnisKnupp's work on the asset-liability presentation for the March 2012 IAC meeting and timing issues related to an early legislative session as a result of the redistricting process. He indicated that the early legislative session may give the SBA a preview of possible benefit changes that could be enacted which could impact the findings. Mr. Mike Sebastian from Hewitt EnnisKnupp provided comments concerning changes in expected returns and risk premium.**

**Mr. SigRist commented on current vendor searches, including the Master Global Custodian, Total Fund Risk Model, Clearing Broker, and Order Management System.**

**Mr. SigRist then provided follow-up information from the November 14, 2011, meeting concerning the Executive Director and CIO responsibilities related to investment manager acquisitions. Policy was amended so that in the event of conflicts of interest at the Executive Director level, the Deputy Executive Director would have final approval authority in manager/fund/property selection; consistent with the recommendation of Hewitt EnnisKnupp. Questions were posed by IAC members and answered by staff.**

**MAJOR MANDATE PERFORMANCE REVIEWS**

**Mr. Mike Sebastian, and Ms. Kristen Doyle with Hewitt EnnisKnupp were in attendance. Mr. Sebastian presented the quarterly investment performance review of the major mandates, asset class performance and analytics. Mr. Sebastian summarized the performance of the major mandates relative to benchmarks as good, suggesting successful implementation of investment policies. Mr. Sebastian also provided observations about the FRS defined contribution plan and a shift away from riskier asset classes.**

**Ms. Kristen Doyle provided an economic and financial market update of the third quarter 2011.**

**Mr. Sebastian provided an update on the FRS Pension Plan asset classes and asset liability process and cash flows. The presentation then focused on benchmarks for asset classes and performance. Peer comparisons were presented for informational purposes. Questions were posed and answered. The presentation also focused on cost comparisons, showing the FRS Pension Plan to be a low cost provider of its services. The FRS Investment Plan performance, allocation, costs and participation were also presented, followed by questions and answers.**

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**Ms. Doyle presented on the Florida Hurricane Catastrophe Fund focusing on performance and cash flows. The presentation then moved to the Lawton Chiles Endowment Fund, focusing on cash flows, asset allocations and performance. Ms. Doyle concluded her presentation with an overview of Florida PRIME, focusing on performance, cash flows, and transfers from Fund B.**

**PUBLIC MARKETS PROGRAM REVIEW**

**Mr. Kevin SigRist provided context on the annual public markets program review, highlighting the recent change from Wilshire to Mercer as the SBA's public market consultant.**

**Mr. Brian Birnbaum, Mercer, provided the Council with his personal background, as well as that of Mercer and the scope of services Mercer is providing, including manager ratings. A question was posed concerning the ratings which was addressed. The presentation also focused on initial observations with respect to public market portfolios in the FRS. Mercer presented general observations on the Pension Plan and on the Investment Plan. A question was posed concerning fixed income and answered. Comments closed with plans for future presentations, as which point comments from the IAC were made and addressed by Mr. Birnbaum.**

**COMPLIANCE PROGRAM REVIEW**

**Mr. Ash Williams provided background concerning the SBA's risk and compliance policies, processes, controls and governance. Recently, the Trustees expressed interest in having outside independent review of how the board approaches and manages risk. The scope and timing of the review was coordinated between the Trustees and the Audit Committee. The Audit Committee hired Crowe Horwath to evaluate the progress the SBA has made in implementing recommendations. Mr. SigRist recommended that two issues of the analysis identified be addressed by the IAC.**

**Mr. Gregg Anderson and Mr. Alan Fisk with Crowe Horwath were in attendance. Mr. Fisk provided an overview of the services provided and turned the presentation over to Mr. Anderson. Mr. Anderson provided a high level overview of the issues researched, focusing on reporting relationships. Ms. Flerida Rivera-Alsing, Chief Audit Executive, explained the background leading up to the hiring of Crowe Horwath and the scope of work to be performed, and that the scope was dictated by the Trustees. Discussion among IAC members, SBA staff, Audit Committee staff, and Crowe Horwath ensued.**

**Mr. Eric Nelson explained his access to various reporting entities and details of the responsibilities of the Risk and Compliance unit. Continued dialogue among IAC members determining actions they were asked to make resulted in a motion by Mr. Daniels that the IAC opine that there is not an issue with the current structure of the SBA, and the IAC encourages various audit and compliance staff to continue an open dialogue with the IAC. The motion was**

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**seconded by Mr. Grain, and passed with Messrs. Garcia and Newman abstaining due to lack of available information.**

**Mr. Gidel, prior to moving to the next agenda item indicated that he anticipated circulating a letter to the members of the IAC responding to the CFO's request, memorializing the discussion and suggestions of the IAC.**

## UPDATE OF FRS INVESTMENT PLAN INVESTMENT POLICY STATEMENT

**Mr. Kevin SigRist, Deputy Executive Director, presented proposed ministerial changes to the Investment Policy Statements for the FRS Investment Plan and other minor changes resulting from changes made during the 2011 legislative session. Mr. Grain moved the changes, which were seconded by Mr. Newman and approved without objection.**

## AUDIENCE COMMENTS/2012 MEETINGS/CLOSING REMARKS

**Mr. Gidel circulated a draft letter in response to CFO Atwater's inquiry regarding the compliance issue addressed earlier in the meeting to IAC members for input. Following a discussion, minor changes to the letter were suggested and agreed upon.**

**Mr. Garcia raised the issue of the reaffirmation of the Executive Director, and made a motion to recommend to the Trustees for the reaffirmation of Mr. Williams. The motion to include the IAC recommendation that the Trustees reappoint the Executive Director & CIO was approved unanimously.**

**Mr. Garcia requested an update for the IAC on the status of the public records request by Senator Mike Fasano, to which Ms. Maureen Hazen, General Counsel, provided summary statistics.**

**Mr. Gidel closed with acknowledging the service of Mr. John Jaeb and Mr. John Hill whose terms were expiring. Both Mr. Jaeb and Mr. Hill provided comments.**

**The next meeting will be March 2012 in Tallahassee. The meeting adjourned at 4:20 PM.**

**(Further meeting information can be found in the written transcripts of the meeting kept by the State Board of Administration.)**

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**AS SECRETARY**

**ASH WILLIAMS**
**EXECUTIVE DIRECTOR & CIO**

# MEMORANDUM

**To:** Board of Trustees

**From:** Roger Wishner, Chairman
Participant Local Government Advisory Council (PLGAC)

**Date:** March 5, 2012

**Subject:** Quarterly Update – Florida PRIME

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The Participant Local Government Advisory Council (the "Council") is scheduled to meet on March 8, 2012. The Council continues to oversee the operations and investment management of Florida PRIME.

**CASH FLOWS / PERFORMANCE**

- Over the quarter ending December 31, 2011, participant deposits totaled $6.7 billion; participant withdrawals totaled $5.1 billion, for a net increase of approximately $1.6 billion.
- During the 4th quarter, Florida PRIME delivered an aggregate $4.7 million in investment earnings.
- Performance of Florida PRIME has been strong over short and long-term time periods. For the period ending December 31, 2011, Florida PRIME generated *excess* returns (performance above the pool's benchmark) of approximately 20 basis points (0.20%, annualized) over the last three months, and 16 basis points (0.16%) over the last 12 months.

**POOL CHARACTERISTICS**

- As of December 31, 2011, the total market value of Florida PRIME was $7.8 billion.
- As of December 31, 2011, the investment pool had a 7 Day SEC Yield equal to 0.28%, a Weighted Average Maturity (WAM) equal to 36.7 days, and a Weighted Average Life (WAL or Spread WAM) equal to 67.5 days.

**PARTICIPANT COMMUNICATIONS & SERVICES**

- During the 1st quarter of calendar year 2012, the SBA will roll out a new Learning Management System (LMS) for Florida PRIME participants, offering an array of accounting and investment courses online.

**FUND B**

- Fund B continues to pay principal and interest, with cumulative distributions to participants of $1,703,525,000 through the December 2011 monthly distribution.
- As of December 31, 2011, 84.8 percent of the original principal in Fund B has been returned to participants.

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ASH WILLIAMS
EXECUTIVE DIRECTOR & CIO

Date: March 5, 2012

To: Board of Trustees
From: Rodolfo Engmann, Audit Committee Chair RAE
Subject: Quarterly Audit Committee Report

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The State Board of Administration (the SBA) Audit Committee met on January 10, 2012 and February 13, 2012. Following are the results of those SBA Audit Committee meetings and audit activities during the past three months.

External Audit

1. We discussed the results of Ernst & Young's financial statement audits of the SBA's wholly-owned companies with a September 30, 2011 year-end. We also reviewed the related financial statements, and reports on agreed upon procedures reports, tax compliance, internal control over financial reporting, and compliance with debt agreements.

2. We received an update from Crowe Horwath on the status of the financial statement audit of the four special purpose entities of the SBA.

3. We received the audit reports issued by two government audit groups: (a) Auditor General on the financial statement audit of Local Government Surplus Funds Trust Fund (an external investment pool) and (b) Office of Program Policy Analysis & Government Accountability on the Florida Growth Fund.

   There were neither adverse opinions, nor items for management's attention as a result of the aforementioned work.

SBA Internal Audit

We reviewed the second quarter follow-up audit report which included recommendations from six reports: Office of Internal Audit (OIA) Fixed Income Operational Audit - Trading Activities, OIA Memo No. 2007-02, Test of the State Board of Administration (SBA) Disaster Recovery Plan Performed at the Alternate People Site, OIA Financial Reporting Process, OIA Accounts Payable Operational Audit, OIA Fixed Income - Securities Lending 3rd Follow-up Audit, and OIA Fixed Income Trading Activities Follow-up Audit.

The Chief Audit Executive (CAE) provided a report on progress related to the OIA Annual Audit Plan (AAP) for the fiscal year 2011-2012. The CAE also presented for our approval the revised AAP for 2011-2012. The revision was primarily due to resignations of two auditors. We approved the revised AAP.

The CAE provided an overview of the continuous auditing and electronic work paper software that the OIA plans to implement in the coming fiscal year to improve coverage, efficiency, and security of OIA work papers.

We also approved the requests from the CAE to engage external audit firms to audit financial statements of one of the joint ventures of the SBA and to follow-up on certain recommendations related to information technology.

Open Recommendations

The tables below show the progress made on open recommendations. Additional details related to open recommendations are presented in Appendices 1, 2 and 3.

**CATEGORY "A" RECOMMENDATIONS**

| | As of 11/4/2011 | Changes from 11/4 to 2/29 | As of 2/29/2012 |
|---|---|---|---|
| Total Number of Recommendations | 379 | 0 | 379 |
| Closed Recommendations | (300) | (13) | (313) |
| **Open Recommendations** | 79 | (13) | **66** |

**CATEGORY "B" RECOMMENDATIONS**

| | As of 11/4/2011 | Changes from 11/4 to 2/29 | As of 2/29/2012 |
|---|---|---|---|
| Total Number of Recommendations | 135 | 8 | 143 |
| Closed Recommendations | (23) | (13) | (36) |
| **Open Recommendations** | 112 | (5) | **107** |

Category "A" refers to recommendations made either by internal or external auditors. OIA monitors and performs follow-up procedures on these recommendations in accordance with the *IIA Standard* 2500.A1.[1] In certain cases, follow-up procedures are performed by external auditors.

[1] *Standard 2500.A1- The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.*

Category "B" refers to recommendations made by consultants resulting from an assessment of a program or activity such as governance, risk management, compliance, ethics, disaster recovery preparedness program, etc. The OIA monitors the disposition of these recommendations in accordance with the *IIA Standard* 2500.C1[2]. Please note that the *IIA Standard* does **not** require the CAE to establish a follow-up process for consulting engagements, but the OIA does take into account the disposition of these recommendations when performing a risk assessment for purposes of establishing the nature, timing, and scope of audit engagements involving the affected areas.

Of the 107 open items in Category "B", 65 are reported as not yet implemented. Sixty two (62) of the 65 not yet implemented recommendations are primarily involved with the work conducted by Crowe Horwath and their follow-up of governance work conducted by Deloitte. These items will be part of a distinct follow up progress by the Chief Risk and Compliance Officer (addressed below). The remaining three open items pertain to work done by BDA Global in 2010. The SBA engaged BDA Global in 2010 to conduct a review to determine if its Continuity of Operations Program (COOP) provides reasonable assurance that the SBA has the ability to timely recover from a major disruption or disaster and continue critical business functions as defined by the goals of the program. During the February 13, 2012 Audit Committee meeting, we instructed the Chief Risk and Compliance Officer to work with the SBA to come to a final determination of the, then six, high risk remaining open items. On February 24, 2012, the Chief Risk and Compliance Officer reported that three of the six open items have been closed and work continues on the remaining three. The Audit Committee will further assess this work as part of our next regularly scheduled meeting on May 14, 2012.

Enterprise Risk Management and Compliance

At the direction of the Trustees, the SBA Audit Committee hired Crowe Horwath to evaluate the progress made by the SBA relative to its Compliance Program. We received, evaluated, and processed SBA management responses to Crowe Horwath report.

In addition to the OIA monitoring open recommendations as Category "B" items (as described above), the Audit Committee has asked the Chief Risk and Compliance Officer to provide a detailed quarterly report regarding the progress of the implementation of Crowe Horwath's recommendations.

Furthermore, the Audit Committee assessed the changes in the role of the Chief Risk and Compliance Officer initiated by the Crowe Horwath recommendations, and processed by the SBA, Investment Advisory Council (IAC) and the Trustees. As a result of this assessment, the Audit Committee has refined our quarterly reporting process of the Chief Risk and Compliance Officer to include a separate report regarding the progress of the Enterprise Risk Management (ERM) program as it also relates to the system of internal controls surrounding the preparation of financial statements as defined by the Committee of Sponsoring Organization's (COSO) "Enterprise Risk Management-Integrated Framework, September 2004".

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[2] *Standard 2500.C1-The internal audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.*

**APPENDIX 1**
**STATUS OF CATEGORY "A" RECOMMENDATIONS**
**AS OF 2/29/12**

**1. OPEN RECOMMENDATIONS BY YEAR & RISK RATING**

| Year | Risk Rating: High | Medium | Low | Total | % |
|---|---|---|---|---|---|
| 2007 | 2 | 0 | 0 | 2 | 3.0% |
| 2010 | 5 | 8 | 0 | 13 | 19.7% |
| 2011 | 21 | 14 | 16 | 51 | 77.3% |
| | 28 | 22 | 16 | 66 | |
| | 42% | 33% | 24% | | |

**2. DETAILS OF OPEN RECOMMENDATIONS**

| Report Title | Report Date | Risk Rating: High | Medium | Low | Total | Status: NYI | PIRP | OTV | Total | % |
|---|---|---|---|---|---|---|---|---|---|---|
| Fixed Income Trading Activities | 3/27/2007 | 1 | | | 1 | | | 1 | 1 | 1.5% |
| Disaster Recovery Plan | 7/31/2007 | 1 | | | 1 | 1 | | | 1 | 1.5% |
| Financial Reporting | 6/9/2010 | 4 | 1 | | 5 | 3 | 1 | 1 | 5 | 7.6% |
| Real Estate 3rd Follow-up | 8/23/2010 | 1 | | | 1 | | 1 | | 1 | 1.5% |
| Clifton Gunderson 1st Follow-up | 10/22/2010 | | 1 | | 1 | | | 1 | 1 | 1.5% |
| EY - Fiscal Year 2009-10 FRS Audit | 12/17/2010 | | 6 | | 6 | 5 | | 1 | 6 | 9.1% |
| Accounts Payable | 2/15/2011 | | 1 | | 1 | 1 | | | 1 | 1.5% |
| Real Estate 4th Follow-up | 7/13/2011 | 10 | | | 10 | 10 | | | 10 | 15.2% |
| EY SBA Network Security Assessment | 9/27/2011 | | 3 | 2 | 5 | 1 | | 4 | 5 | 7.6% |
| EY SBA Security Assessments | 9/29/2011 | 11 | 10 | 14 | 35 | 2 | | 33 | 35 | 53.0% |
| | | 28 | 22 | 16 | 66 | 23 | 2 | 41 | 66 | |

**Category A** - **Recommendations made either by internal or external auditors. OIA monitors and performs follow-up procedures on these recommendations in accordance with the *IIA Standard 2500. A.1*[3] In certain cases, follow-up procedures are performed by external auditors.**

**NYI** - **Not Yet Implemented**
**PIRP** - **Partially Implemented and the Remainder is in Progress**
**OTV** - **OIA To Verify**

[3] *Standard 2500.A1- The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.*

**APPENDIX 2**
**STATUS OF CATEGORY "B" RECOMMENDATIONS**
**AS OF 2/29/12**

## 1. OPEN RECOMMENDATIONS BY YEAR & RISK RATING

| Year | Risk Rating: High | Medium | Low | Total | % |
|---|---|---|---|---|---|
| 2009 | 5 | 4 | 7 | 16 | 15.0% |
| 2010 | 18 | 9 | 1 | 28 | 26.1% |
| 2011 | 2 | 38 | 23 | 63 | 58.9% |
| | 25 | 51 | 31 | **107** | |
| | 23% | 48% | 29% | | |

## 2. DETAILS OF OPEN RECOMMENDATIONS

| Report Title | Report Date | Risk Rating: High | Medium | Low | Total | Status: NYI | PIRP | IMP | Total | % |
|---|---|---|---|---|---|---|---|---|---|---|
| Deloitte & Touche Phase I | 1/15/2009 | 3 | 4 | 7 | 14 | | 13 | 1 | 14 | 13.1% |
| Deloitte & Touche Phase II | 6/16/2009 | 2 | | | 2 | 1 | 1 | | 2 | 1.9% |
| Deloitte & Touche Phase III | 3/11/2010 | | 9 | 1 | 10 | 1 | | 9 | 10 | 9.3% |
| BDA Global - Disaster Recovery | 8/23/2010 | 18 | | | 18 | 3 | | 15 | 18 | 16.8% |
| Crowe Horwath - Compliance Review | 10/21/2011 | 2 | 38 | 23 | 63 | 60 | | 3 | 63 | 58.9% |
| | | 25 | 51 | 31 | **107** | 65 | 14 | 28 | **107** | |

**Category B** - **Recommendations made by consultants resulting from an assessment of a program or activity such as governance, risk management, compliance, ethics, disaster recovery preparedness program, etc. OIA monitors the disposition of these recommendations in accordance with the *IIA Standard 2500.C1.*** [4]

**NYI** - **Not Yet Implemented**
**PIRP** - **Partially Implemented and the Remainder is in Progress**
**IMP** - **Implemented,** as represented by SBA management

[4] *Standard 2500.C1-The internal audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.*

**APPENDIX 3**
**STATUS OF ALL RECOMMENDATIONS (CATEGORIES A & B COMBINED)**
**AS OF 2/29/12**

**1. OPEN RECOMMENDATIONS BY YEAR & RISK RATING**

| Year | Risk Rating: High | Medium | Low | Total | % |
|---|---|---|---|---|---|
| 2007 | 2 | 0 | 0 | 2 | 1.2% |
| 2009 | 5 | 4 | 7 | 16 | 9.2% |
| 2010 | 23 | 17 | 1 | 41 | 23.7% |
| 2011 | 23 | 52 | 39 | 114 | 65.9% |
| | 53 | 73 | 47 | **173** | |
| | 31% | 42% | 27% | | |

**2. DETAILS OF OPEN RECOMMENDATIONS**

| Report Title | Report Date | Risk Rating: High | Medium | Low | Total | Status: NYI | PIRP | OTV | IMP | Total | % |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Fixed Income Trading Activities | 3/27/2007 | 1 | | | 1 | | | 1 | | 1 | 0.6% |
| Disaster Recovery Plan | 7/31/2007 | 1 | | | 1 | 1 | | | | 1 | 0.6% |
| Deloitte & Touche Phase I | 1/15/2009 | 3 | 4 | 7 | 14 | | 13 | | 1 | 14 | 8.1% |
| Deloitte & Touche Phase II | 6/16/2009 | 2 | | | 2 | 1 | 1 | | | 2 | 1.2% |
| Deloitte & Touche Phase III | 3/11/2010 | | 9 | 1 | 10 | 1 | | | 9 | 10 | 5.8% |
| Financial Reporting | 6/9/2010 | 4 | 1 | | 5 | 3 | 1 | 1 | | 5 | 2.9% |
| BDA Global - Disaster Recovery | 8/23/2010 | 18 | | | 18 | 3 | | | 15 | 18 | 10.2% |
| Real Estate 3rd Follow-up | 8/23/2010 | 1 | | | 1 | | 1 | | | 1 | 0.6% |
| Clifton Gunderson 1st Follow-up | 10/22/2010 | | 1 | | 1 | | | 1 | | 1 | 0.6% |
| EY - Fiscal Year 2009-10 FRS Audit | 12/17/2010 | | 6 | | 6 | 5 | | 1 | | 6 | 3.5% |
| Accounts Payable | 2/15/2011 | | 1 | | 1 | 1 | | | | 1 | 0.6% |
| Real Estate 4th Follow-up | 7/13/2011 | 10 | | | 10 | 10 | | | | 10 | 5.8% |
| EY SBA Network Security Assessment | 9/27/2011 | | 3 | 2 | 5 | 1 | | 4 | | 5 | 2.9% |
| EY SBA Security Assessments | 9/29/2011 | 11 | 10 | 14 | 35 | 2 | | 33 | | 35 | 20.2% |
| Crowe Horwath - Compliance Review | 10/21/2011 | 2 | 38 | 23 | 63 | 60 | | | 3 | 63 | 36.4% |
| | | 53 | 73 | 47 | **173** | 88 | 16 | 41 | 28 | **173** | |

**NYI** - **Not Yet Implemented**
**PIRP** - **Partially Implemented and the Remainder is in Progress**
**OTV** - **OIA To Verify**
**IMP** - **Implemented,** as represented by SBA management

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ASH WILLIAMS
EXECUTIVE DIRECTOR & CIO

# MEMORANDUM

**To:** Ashbel C. Williams, Executive Director & CIO

**From:** Maureen M. Hazen, General Counsel Maureen M. Hazen

**Date:** March 5, 2012

**Subject:** Office of General Counsel: Standing Report to Trustees
For Period November 16, 2011 – February 29, 2012

## SBA Agreements.

During the period covered by this report, the General Counsel's Office drafted, reviewed and negotiated: (i) 19 new contracts – including 1 trading agreement for Fixed Income, 7 private equity investments, 1 real estate investment and 1 strategic investment (timber); and (ii) 102 contract amendments, addenda or renewals.

## SBA Litigation.

(a) Passive. As of February 29, 2012, the SBA was a putative, passive member of the class in 569 active and open securities class actions. From November 16, 2011 through February 29, 2012[1], the SBA collected recoveries in the amount of $10,940,809.24 as a passive member in 50 securities class actions.

(b) Active.

(i) The SBA continues to conduct and participate in discovery in the litigation styled *Abu Dhabi Commercial Bank v. Morgan Stanley & Co.*

(ii) On June 20, 2011, various plaintiffs filed a complaint against the Trustees and the Secretary of DMS challenging the constitutionality of Senate Bill 2100 (the legislation mandating the deduction of 3% of employees' salaries for contribution into the Florida Retirement System). The Court heard the case (through dispositive motions) on October 26, 2011 but has yet to issue a ruling. (A similar case was subsequently filed in August, 2011 with a different court.)

[1] The portion of recoveries attributable to the month of February are preliminary.

(iii) The SBA settled its state law claims against AIG in exchange for $4,000,000 and the right to file a claim in the class action. The SBA continues to engage in settlement discussions with the remaining defendant.

(iv) On January 17, 2012, the SBA was served a complaint (along with other defendants) filed in the U.S. Bankruptcy Court, Southern District of New York alleging damages for intentional and constructive fraudulent transfers under applicable state law and seeking the return of proceeds received by all defendants that tendered stock in a leveraged merger of Lyondell Chemical Company (which subsequently declared bankruptcy). The SBA received approximately $32 million in connection with stock tendered in the leveraged merger. The SBA intends to defend vigorously against the allegations raised in this complaint

(c) FRS Investment Plan. During the period from November 16, 2011 through February 29, 2012, the General Counsel's Office monitored and/or managed the following cases for the Florida Retirement System Investment Plan (formerly, the Defined Contribution program). The SBA issued fourteen (14) Final Orders, received notice of filing of seven (7) new cases, continued to litigate thirteen (13) cases that were pending during the periods covered by previous reports and defended two (2) appellate cases.

**Other Matters.**

(a) Public Records Requests. During the period covered by this report, the General Counsel's Office received 24 new public records requests, continued to work on 7 open requests and provided responses to 27 requests.

(b) SBA Rules. (i) On February 12, 2012, a Notice of Proposed Rule was filed to repeal Rule 19-7.001 (Purpose) and to adopt Rule 19-7.002, F.A.C., the Investment Policy Guidelines for the Local Government Surplus Funds Trust Fund and the Fund B Surplus Funds Trust Fund. (ii) On February 29, 2012, the SBA notified the Office of Fiscal Accountability and Regulatory Reform ("OFARR") that the SBA intends to file a Notice of Rule Development for (A) Rule 19-9.001, the Investment Policy Statement for the FRS Investment Plan, (B) Rules 19-13.001, 13.002, 13.003 to update the references to the FRS Investment Plan, and (C) Rule 19-14.001, the most recent version of the Investment Policy Statement on Support of Certain Non-FRS Defined Contribution Programs. (ii) In previous periods, the SBA reviewed 53 existing SBA departmental rules (i.e. not involving the FRS Investment Plan or Florida PRIME) and identified several that warrant changes and/or clarification. During the period covered by this report, SBA staff continued to work on this rule re-write project.

(c) Dodd-Frank Rules. During the period covered by this report, the CFTC finalized two (2) rules under Title VII of the Dodd-Frank Act relating to regulation of OTC derivatives that may affect the SBA. First, the CFTC rules will require that "Major Swap Participants" register with the CFTC by becoming members of the National Futures Association. Because the CFTC has yet to adopt a final rule defining the term "Major Swap Participant," it is unclear whether the SBA will be subject to this registration requirement. Second, the CFTC published final rules adopting business conduct requirements for swaps dealers, which include additional criteria for swap dealers acting as counterparties to Special Entities (which include governmental entities and governmental benefit plans, among other entities). The CFTC and the SEC contemplate adopting further final rules during second quarter 2012.

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**AS SECRETARY**

**ASH WILLIAMS**
**EXECUTIVE DIRECTOR & CIO**

# MEMORANDUM

**To:** Ash Williams

**From:** Michael McCauley

**Date:** March 5, 2012

**Subject:** Board of Trustees Meeting – Standing Report / Investment Programs & Governance

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**CORPORATE GOVERNANCE & PROXY VOTING OVERSIGHT GROUP**

The SBA's Corporate Governance & Proxy Voting Oversight Group (Proxy Committee) met last on December 21, 2011 and is scheduled to meet next on March 29, 2012. The Proxy Committee continues to discuss ongoing governance issues including the volume and trends for recent proxy votes, governance factors within global equity markets, regulatory developments, and company research tied to the Protecting Florida's Investments Act (PFIA).

**GLOBAL EQUITY PROXY VOTING**

During the trailing 12 months ending December 31, 2011, the SBA executed 7,630 votes on public company proxies covering 70,306 individual voting items, covering director elections, audit firm ratifications, executive compensation plans, mergers, acquisitions, and other management- and shareowner-proposals. On all executed proxy votes, the SBA voted "for" 72.9 percent, with 21.4 percent cast "against" the management-recommended vote. The table below provides major statistics on the SBA's proxy voting activities through the last 12 months ending December 31, 2011:

| | |
|---|---|
| **Votes in Favor of Directors**<br>**77.3%** (FY2011=76.7%) | **Votes with Management**<br>**78.6%** (FY2011=78.9%) |
| **Votes in Favor of Auditors**<br>**89.2%** (FY2011=90.0%) | **Total Ballot Items Voted**<br>**70,306** (FY2011=56,536) |
| **Votes in Favor of All Governance Proposals**<br>**71.7%** (FY2011=71%) | **Total Proxies Voted**<br>**7,630** (FY2011=6,138) |

The significant increase in the volume of proxy votes during the last few months of fiscal year 2011 and into early fiscal year 2012 is related to the SBA's expansion of internal voting activities covering the majority of externally-managed global portfolios.

**2012 ANNUAL REPORT ON CORPORATE GOVERNANCE**

The SBA's Annual Report on Corporate Governance was released on February 15, 2012. This year's report covers our governance activities during and after global proxy seasons, and has two new sections focused on global say-on-pay and global equity proxy voting. A copy of the report is available on the SBA website.

**UPDATES TO SBA 2012 CORPORATE GOVERNANCE PRINCIPLES & PROXY VOTING GUIDELINES**

Amended Guideline: This updated guideline deals with the newly enacted process allowing investors the ability the submit shareowner proposals to implement procedures to nominate investor-selected candidates to the board of directors.

⇨ **Proxy Access: FOR**

In late 2009, the SEC proposed to allow shareowners the right to place director candidates within the company's proxy materials. "By making it easier for shareholders to replace directors, proxy access can contribute to making directors more accountable to shareholders and more attentive to their interests."[1] The SBA supported this proposal, which would have set an access default with the freedom to opt-out to a no-access regime. Additional reforms occurred in August 2009, dramatically changing Delaware Law governing the ability of shareowners to nominate directors and make other nomination oriented changes to a company's bylaws. Delaware General Corporation Law ("DGCL") Section 112 permits shareowners to adopt bylaws that require the corporation to include shareowner nominees for board election and permits the right to be conditioned on several factors. Section 113 of the DGCL permits shareowners to adopt bylaws that require the reimbursement of expenses incurred by a shareowner in connection with a proxy solicitation, again, with certain permitted conditions.[1] Some observers view proxy access without a corresponding solicitation reimbursement mechanism to be less than optimal and represent a shortcoming in the ability of shareowners to have meaningful input into selecting their own director representatives.

In July 2011, the SEC rule covering a mandatory proxy access default (Rule 14a-11) was legally overturned. The SEC's corresponding Rule 14a-8(i)(8) covering the adoption of proxy access mechanisms through individual shareowner resolutions, commonly referred to as "private ordering," was implemented in September 2011. Shareowners in the United States are now permitted to require companies to include shareowner proposals regarding proxy access procedures in company proxy materials beginning in 2012. Such proposals may be submitted either as precatory (advisory) proposals or binding proposals.

The SBA will generally vote FOR proposals that allow significant company shareowners access to management's proxy material in order to nominate their own candidates to the board of directors. The original 2009 proposal contained within SEC Rule 14a-11, requiring a three percent ownership and a three year holding period, is considered a reasonable benchmark against which individual shareowner proposals can be compared.

Factors to be assessed by the SBA include, but are not limited to:

- Ownership thresholds stipulated by the proposal;
- Maximum proportion of the full board that shareowners may nominate in a single year; and
- Other procedural matters, such as listing order within the proxy, ownership certification requirements, etc.

Proposals that require an investor (or group of investors) to own a meaningful percentage of the company's voting stock, generally defined as greater than one percent, are favored. Proposals that require ownership for meaningful periods of time, generally defined as greater than one year, are favored. The SBA may vote AGAINST proposals which contain burdensome or otherwise restrictive requirements, such as ownership or holding thresholds which are set at impractical levels.

1 Bebchuk, Lucian A. and Scott Hirst, "Private Ordering and the Proxy Debate." Harvard Law School. Discussion Paper No. 653. 11/2009 Available at SSRN: http://papers.ssrn.com/abstract=1513408.

New Guideline: this new guideline deals with changes to a corporate charter (or bylaws) that can restrict an investor's ability to pursue legal remedy.

⇨ **Exclusive Judicial Forum Provisions: CASE-BY-CASE**

In a March 2010 opinion, the Delaware Court of Chancery provided an opportunity for any Delaware corporation to establish the Court as the exclusive forum for "intra-entity" corporate disputes, such as claims of breach of fiduciary duty. Such claims have been used to overturn directors' business judgments on mergers, and other matters. Early adopters of the exclusive forum provision chose to enact bylaw provisions without seeking shareowner approval. However, the Galaviz v. Berg decision by the U.S. District Court for Northern California provided that Oracle's exclusive forum provision was unenforceable, in part due to Oracle's failure to bring the provision before shareowners. Subsequently, a number of U.S. companies have decided to bring the exclusive forum provision to a shareowner vote and others have amended their charter or by-law provisions.[1]

The SBA generally opposes restrictions on shareowner ability to pursue derivative claims and to participate in the selection of appropriate venue. Standard access to the court system is considered to be a fundamental shareowner right. Companies should not attempt to restrict the venue for shareowner claims by adopting charter or bylaw

provisions that seek to establish an exclusive judicial forum without shareowner approval. Therefore, the SBA generally votes AGAINST management proposals to establish exclusive forum, and votes FOR shareowner proposals requesting that exclusive forum provisions be approved by shareowners. As with many other voting decisions, the SBA will critically examine the company's rationale for limiting shareowners' rights to legal remedy, including choice of venue, and any material harm that may have been caused by related litigation outside its jurisdiction of incorporation.

[1] Claudia H. Allen, "Deleware Corporations—Can Delaware Forum Selection Clauses in Charters or Bylaws Keep Litigation in the Court of Chancery?," April 18. 2011

**REGULATORY DEVELOPMENTS & OTHER COMMENTARY**

During December 2011, SBA staff co-signed a series of letters to eight companies that have ignored, for two or more consecutive years, majority-vote-winning shareowner proposals, and also lack an independent chair and/or true majority vote standard for uncontested director elections. The letters ask each board to name independent chairs and/or adopt majority voting for directors. The goal is to ensure that an independent board member leads a review of the winning shareowner proposals and that owners have a way to provide feedback to the board and hold directors accountable for their actions. Each letter also includes a request for a dialogue between company directors and a group of Council members. The companies receiving letters included: Ball, Franklin Street Properties, Graco, Hospitality Properties Trust, Mac-Gray, Neurocrine Biosciences, Pioneer Natural Resources and Vornado Realty Trust.

On January 31, 2012, SBA staff was a signatory on a letter to the Japanese Ministry of Justice on its request for Public Comments on the Interim Proposal concerning Revision of the Japan Companies Act (the 'Act'). The letter is a direct result of the fraud at Olympus Corp., and provides feedback to the Japanese Ministry of Justice's consultation on possible changes to the Act. The consultation covered key issues designed to strengthen the independence of outside directors on Japanese boards, structural changes to potential board forms, and the responsibilities of statutory auditors and audit committees.

On February 13, 2012, SBA staff signed on to a letter to SEC Chairman Mary Schapiro recommending the SEC bring a strong investor focus to its work programs by addressing a set of priorities over the next 12 months. The letter highlighted the following priorities: 1) universal proxy access; 2) creation of the investor advisory committee; 3) executive compensation; 4) international financial reporting standards (IFRS); 5) credit rating agencies; and 6) sustainability and board diversity disclosures.

On February 29, 2012, SBA staff submitted a comment letter to the Public Company Accounting Oversight Board (PCAOB) providing feedback on its proposed auditing standard related to communication with audit committees. The letter supports PCAOB proposals to improve the communication between the external auditor and the audit committee, focused on strengthened communications covering significant accounting matters, unusual transactions, and requiring the audit committee to provide written acknowledgement of the scope of the audit engagement.

**STATE BOARD OF ADMINISTRATION OF FLORIDA**

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**TALLAHASSEE, FLORIDA 32308**
**(850) 488-4406**

**POST OFFICE BOX 13300**
**32317-3300**

**RICK SCOTT**
**GOVERNOR**
**AS CHAIRMAN**

**JEFF ATWATER**
**CHIEF FINANCIAL OFFICER**
**AS TREASURER**

**PAM BONDI**
**ATTORNEY GENERAL**
**AS SECRETARY**

**ASH WILLIAMS**
**EXECUTIVE DIRECTOR & CIO**

# MEMORANDUM

DATE: March 5, 2012

TO: Ash Williams

FROM: Eric Nelson

SUBJECT: Trustee Update – March 2012

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Attached is Risk Management and Compliance's quarterly summarized compliance report as of December 30, 2011 for transmission to the Trustees, Investment Advisory Council and Audit Committee. Where possible, compliance data being reported on is the most currently available information as of the date of this memorandum.

Additionally, the following is a brief status report of Risk Management and Compliance activities and initiatives completed or in progress during the period 12/1/11 through 3/5/12:

- Implemented response to the Crowe Horwath compliance program review recommendation pertaining to governance issue associated with the Chief Risk and Compliance Officer (CRCO) reporting line. Language was added to various Trustee approved investment policy statements effective February 9, 2012 codifying CRCO routine informational reporting requirements to the Trustees, Investment Advisory Council and Audit Committee, as well as establishing a requirement that the selection, termination and compensation of the CRCO will be affirmed by the Trustees.

- Implementation work continues on the BarraOne total fund risk system with active participation by internal staff and Barra personnel. Processes for modeling non-standard assets (e.g. swaps, private equity, real estate, etc.) are approaching the final stages of completion. Interface between custodian bank and Barra is up and running, and data is flowing smoothly. Report specifications are being finalized, and historical data is in the process of being loaded for each month of Fiscal Year 2011/12. Targeted completion timeframe is Spring 2012.

- In response to a recommendation received from Crowe Horwath, a "tone at the top" survey was designed and sent to SBA staff in December 2011. The purpose of the survey was to assess the adequacy of the SBA's control environment, which is the foundation for all other components of internal control. The survey consisted of 24 questions derived

from COSO's "Internal Control – Integrated Framework" and covered topics such as ethics and culture, compliance, accountability, communications, decision making, etc. 170 employee responses were received and tabulated into various graphical depictions, and the results were communicated to senior management, posted on the SBA's intranet for staff viewing, and forwarded to and discussed with the Audit Committee at their meeting on February 13, 2012.

- Conducted two strategic planning meetings in January with senior management. The Director of Enterprise Risk Management facilitated sessions evaluating current strategic goals and objectives, reviewing feedback received from tone at the top survey, and discussing potential priorities going forward. We are currently compiling a list of initiatives and projects from all business units and have individually gathered feedback on potential strategic risks from senior management as well as upper middle management. The next strategic planning session planned for April will focus on assessing any legislative impacts to SBA and evaluating feedback received on strategic risk assessments.

- Updated individual business unit risk assessments through follow-up interviews with process owners conducted by the Director of Enterprise Risk Management.

- Risk Management and Compliance staff have been documenting the SBA's trading counterparty addition, deletion and annual evaluation processes through interviews and development of flowcharts and procedures. Numerous meetings have been conducted to finalize process flows, roles and responsibilities and associated documentation.

- Risk Management and Compliance staff participated in invitation to negotiate procurement process for a new internal trading order management system. Staff attended compliance module demos, and final vendor/system options are currently being evaluated by asset class trading personnel.

- Participated in interviews for the vacant Senior Investment Officer position in the Private Equity and Strategic Investments asset class.

- Participated in SBA orientation sessions with new Investment Advisory Council members Les Daniels, Gary Wendt, and Michael Price.

- Met with the SBA's newly appointed Inspector General (Ken Chambers) to discuss transfer of certain duties and responsibilities back to the Office of Inspector General from the Risk Management and Compliance unit, which had been performing the duties on an interim basis.

- Obtained Risk and Compliance Committee and Executive Director & CIO approval to close out (per management) ten outstanding audit recommendations identified as partially complete (and the rest will not be implemented) or not accepted by management. A proposed methodology was developed and presented to the Risk and Compliance Committee at January 19, 2012 meeting to annually assess potentially stale audit recommendations and document closure via management representation that the recommendation is either implemented to extent practical/feasible or, alternatively, not

accepted as circumstances around the original recommendation may have evolved. The committee approved the approach, which consists of written documentation submitted by business unit owner outlining rationale for closure, Risk Management and Compliance staff assessment of the proposal, and finally Risk and Compliance Committee evaluation of the proposed action with business unit owners in attendance to answer questions. Audit recommendations where the Risk and Compliance Committee deems the residual risk to be sufficiently low for non-implementation will be forwarded to the Executive Director & CIO for final approval. The results of the Risk and Compliance Committee's deliberations on the ten audit recommendations (with supporting documentation) were communicated in writing to the Office of Internal Audit on January 30, 2012.

- At the request of the Chair of the Audit Committee, prepared write-up regarding six outstanding Category B recommendations pertaining to the SBA's Continuity of Operations Program that the Office of Internal Audit has deemed as high risk. Three of the recommendations have now either been implemented or partially implemented (and rest will not be implemented), one recommendation is assigned to the building's property management company and is almost complete, and the remaining two recommendations pertaining to business interruption testing strategies are in progress.

- At the request of the Chair of the Audit Committee, prepared written management responses to eight recommendations that Crowe Horwath identified from the original (2009) Deloitte compliance program review as discrete "new" recommendations. Neither management nor the Office of Internal Audit had previously identified these eight as stand-alone recommendations to consider and/or resolve. The eight recommendations were all accepted by management and have been added to our project list.

- At the request of the Chair of the Audit Committee, prepared written rationale and process for a self-assessment approach to be utilized for periodic evaluation of the SBA's compliance program. Proposal set forth methodology for self-assessments to be utilized for two consecutive years with an external review commissioned every third year. This external review would be performed in conjunction with an Audit Committee charter requirement that mandates a holistic governance, risk and compliance (GRC) review, which would be designed to simultaneously evaluate the effectiveness of both internal and external audit functions. Responded to Audit Committee questions at February 13, 2012 meeting, and proposal was accepted and confirmed as reasonably cost effective approach going forward.

- Prepared and presented proposal to the Audit Committee at meeting of February 13, 2012 for the tracking and reporting on "Category B" recommendations. Category B recommendations are suggestions/recommendations received during the course of consulting engagements (not audits or other forms of attestation engagements) and, to date, have not been formally verified as implemented/completed by the Office of Internal Audit. There had been discussion over the last six months both internally within the Audit Committee and with management around the proper assignment of responsibility for both the monitoring and verification of Category B recommendations. The resolution reached at the Audit Committee meeting was that Risk Management and Compliance would receive written attestation from SBA management when a Category B recommendation has been implemented (or partially implemented and the rest not

accepted), along with a brief description on how the recommendation was implemented. Risk Management and Compliance will in turn regularly report progress to the Office of Internal Audit and the Audit Committee. The Office of Internal Audit will incorporate this information into their annual SBA risk assessment process and resulting work plan development to the extent deemed necessary.

- Made presentation and distributed materials to the Audit Committee at February 13, 2012 meeting regarding the SBA's risk management governance structure, including policy framework, organizational structure, committee structure (including function and participants), and current risk framework utilized by the SBA.

- Made numerous revisions to the "External Investment Manager Retention and Termination" policy effective 12/1/11 (primarily impacting Appendix A "Investment Manager Monitoring Guidelines") which codified a number of suggestions put forth by Mercer Investment Consulting in their capacity as the newly appointed public market asset class implementation consultant. Other policies revised during the period included:

  -FRS Pension Plan Investment Policy Statement (effective 2/9/12)
  -FRS Investment Plan Investment Policy Statement (effective 2/9/12
  -Lawton Chiles Endowment Fund Investment Policy Statement (effective 2/9/12)
  -Investment Management Acquisition (effective 12/1/11)
  -Internal Trading Policy (effective 2/1/12)
  -Confidential/Sensitive Data Handling (effective 12/20/11)
  -Passwords (effective 1/10/12)
  -General Performance Measurement Policies (effective 1/3/12)
  -Performance Measurement for FL PRIME (effective 1/4/12)

- Completed development of online program to administer fiduciary training to Investment Advisory Council members as statutorily required. The online course is a condensed version of the half-day program delivered to SBA staff, with a slide deck voice-over provided by members of Groom Law Group and ten fiduciary concept-reinforcing questions. A link to the training portal and instructions were sent to IAC members on February 28, 2012.

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# SBA Risk Management and Compliance

**Compliance Report for Quarter Ended December 31, 2011**

SBA FLORIDA
INVESTING FOR FLORIDA'S FUTURE

| A. | STATUTORY COMPLIANCE | STATUS |
|---|---|---|
| 1 | Chapter 215.47, F.S. - Investments | All investments statutorily permitted<br>All investments within statutory limits |
| 2 | Chapter 215.4755, F.S. - Certification and disclosure requirements for investment advisers and managers | Conflict of interest certifications received as of 12/31/11 for public market external investment managers |
| 3 | Quarterly Report to Joint Legislative Auditing Committee on Florida PRIME and Fund B | Monthly Florida PRIME reports for quarter ending 12/31/11 reviewed and approved by SBA Trustees and sent to JLAC on 2/9/12 |
| 4 | Protecting Florida's Investment Act Compliance (Iran/Sudan) | No violations reported - latest quarterly report approved by Trustees on 12/6/11 |
| 5 | Free Cuba Act of 1993 (Chapter 215.471, F.S.) | No restricted securities currently identified as of 12/31/11- no compliance violations |
| 6 | Northern Ireland (Chapter 121.153, F.S.) | No restricted securities currently identified as of 12/31/11 - no compliance violations |
| 7 | Form 13F- SEC Institutional investment managers that have discretion over $100 million in Section 13(f) securities | Report filed for SBA internally managed accounts |
| 8 | Form 13H - SEC Disclosure for large traders | Communicated large trader identification number to all registered Global Equity broker-dealers |
| 9 | Basket Clause Securities | No proposed plans for such investments were reported to the IAC |

| B. | INVESTMENT POLICY STATEMENTS - APPROVED BY TRUSTEES | STATUS |
|---|---|---|
| 1 | FRS Pension Plan | Asset allocation within specified ranges<br>Performance measured to approved benchmarks |
| 2 | FRS Investment Plan | Education requirements in compliance<br>Investment Plan Administrator and Bundled Provider requirements in compliance<br>Investment options and performance measurement against approved benchmarks in compliance |
| 3 | Lawton Chiles Endowment Fund | Asset allocation within specified ranges<br>Performance measured to approved benchmarks |
| 4 | Florida PRIME | Portfolio securities and transactions in compliance with Investment Policy Statement<br>Federated conducted monthly stress test and reported results to the Investment Oversight Group as of 12/30/11<br>Daily NAV and other high risk ranked parameters independently verified and in compliance |
| 5 | Fund B Surplus Fund | Securities and transactions independently reviewed and all principal and interest payments distributed to participants net of fees |

| C. | ETHICS / CONFLICTS OF INTEREST | STATUS |
|---|---|---|
| 1 | Ethics Policy | Annual certifications of compliance completed by all employees for FY 2011-12 |
| 2 | Internal Controls and Fraud Policy | No instances of fraud or employee misconduct reported or discovered<br>Fraud Hotline: No calls received as of 2/27/12 |
| 3 | Insider Trading Policy | No compliance violations reported |
| 4 | IAC Annual Conflict Disclosure Statement | Certifications received for three new IAC members (Wendt, Price, and Harrell) |
| 5 | Consultant Independence and Disclosure Principles (CIDP) | All eight CIDPs received for calendar year 2011 as of 2/15/12 |
| 6 | Personal Investment Activity Policy and Annual Certifications | All required employees completed training and annual compliance certifications for FY 2011-12<br>One minor personal trading violation was detected during the quarter<br>All personal investment holdings reports received for new employees |
| 7 | Conflict of Interest Certification - SBA Employees participating in selection process for external investment manager or private market investments | All certifications executed |
| 8 | Fiduciary Training | The online fiduciary training site for IAC members has been developed and link sent to IAC members on 2/28/12 |
| 9 | Mandatory Employee Training | All mandatory training requirements fulfilled for FY 2011-12 |
| 10 | Audit Committee Annual Independence Statements | Signed at 2/13/12 Audit Committee meeting for calendar year 2012 |
| 11 | Semi-Annual Statement of Compliance - External Investment Managers (Public) | All managers reported compliance with Investment Management Agreements as of 12/31/11 |

# SBA Risk Management and Compliance

**Compliance Report for Quarter Ended December 31, 2011**

| | D. GOVERNANCE AND POLICY OVERSIGHT | STATUS |
|---|---|---|
| 1 | Governance and Oversight Group Meetings | All internal governance oversight group meetings conducted as specified in policy except for Risk & Compliance Committee and the Performance Measurement Oversight Group |
| 2 | Investment Portfolio Guidelines Compliance (# of portfolios) | |
| | FRS: Global Equity and REIT Portfolios (69) | No material compliance violations through 12/31/11 |
| | Fixed Income & High Yield Portfolios (21) | No material compliance violations through 12/31/11 |
| | Private Market Asset Classes (10) | No material compliance violations as of 9/30/11 (one quarter lag) |
| | Other Non-FRS mandates / Trust Funds (29) | No material compliance violations through 12/31/11 |
| | Review of Investment Portfolio Guidelines | |
| 3 | External Investment Manager and Private Market Investment Acquisition | Acquisition checklists completed for all new managers/funds/real estate investments<br>Placement Agent disclosures received and reviewed on all new investments and amended contracts with economic impact<br>Due diligence received and reviewed (to include prudent person opinions for Private Equity and Strategic Investments) |
| 4 | External Investment Manager and Private and Public Market Investment Retention and Termination | Checklist completed for all terminated managers/funds/real estate investments which includes compliance with Investment Manager Monitoring Guidelines |
| 5 | Internal Trading Policy | Trading limits in compliance with policy |
| 6 | Derivative Instruments Usage | Verified usage permitted by policy<br>Reviewed counterparty risk exposures - within historically normal ranges |
| 7 | Leverage Usage | Reviewed direct-owned real estate loan-to-value exposures as of 9/30/11 - within investment portfolio guidelines |
| 8 | Trading Counterparty Management | Approved broker dealer lists updated and current for FY 2011-12<br>Bank of Nova Scotia and Barclays Capital Inc. were added to the Repo Dealers list on 02/15/12 |
| 9 | Rebalancing and Liquidity Assessments | All funds currently within policy operating ranges |
| 10 | Risk Budget | Aggregate active investment risks (sources, levels and trends) reviewed by Senior Investment Group |
| 11 | New Investment Vehicles and Programs | No new investment vehicles approved during period 11/17/11 - 02/22/12 |
| 12 | Securities Lending | No material compliance violations |
| 13 | Investment Valuation | All direct-owned real estate properties externally appraised within last 12 months (unless newly acquired or in the process of being sold)<br>Public Market Securities: 100.0% (valued as of 12/31/11)<br>Real Estate: 99.9% (valued as of 9/30/11 or later)<br>Private Equity: 99.6% (valued as of 9/30/11 or later)<br>Strategic Investments: 99.3% (valued as of 9/30/11 or later) |
| 14 | Private Market Allocation Policies | Real Estate: within intra-asset class allocation ranges<br>Private Equity: certain categories outside intra-asset class operating ranges, DED notified<br>Strategic Investments: certain categories outside intra-asset class operating ranges, DED notified |
| 15 | Performance Measurement | All calculations performed in compliance with policy |
| 16 | Procurement | 2 ITN's in progress, none completed during the quarter |

End of Section

# Florida Retirement System

Trustee Meeting
July 1, 2011 Actuarial Valuation Results & Considerations

Presented by:

Robert Dezube
Consulting Actuary

March 20, 2012

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# Valuation Results

**($ in Billions)**

| | July 1, 2010 Valuation | 2010 Valuation Reflecting SB 2100 | July 1, 2011 Valuation |
|---|---|---|---|
| 1. Present Value of Benefits (PVB) | $166.4 | $156.2 | $163.3 |
| 2. Present Value of Future Normal Cost (PVFNC) | $28.8 | $19.7 | $19.2 |
| 3. Actuarial Liability [(1) – (2)] | $137.6 | $136.5 | $144.1 |
| 4. Actuarial Value of Assets (AVA) | $120.9 | $120.9 | $126.1 |
| 5. Unfunded Actuarial Liability [(3) – (4)] | $16.7 | $15.6 | $18.0 |
| 6. Funded Percentage [(4) ÷ (3)] | 87.9% | 88.6% | 87.5% |

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# Employer Contribution Rates

| | July 1, 2010 Valuation | | 2010 Valuation Reflecting SB 2100 | | July 1, 2011 Valuation[1] | |
|---|---|---|---|---|---|---|
| | Regular Class | Special Risk | Regular Class | Special Risk | Regular Class | Special Risk |
| **Actuarially Determined Blended Rates** | | | | | | |
| Normal Cost | 9.76% | 22.20% | 3.93% | 11.78% | 3.97% | 12.00% |
| Amortization of the UAL[2] | 1.94% | 5.80% | 1.61% | 6.36% | 2.02% | 7.03% |
| Total "Uniform" Rate | 11.70% | 28.00% | 5.54% | 18.14% | 5.99% | 19.03% |
| **Legislated Blended Contribution Rates** | | | | | | |
| Normal Cost | N/A | N/A | 3.28% | 10.21% | TBD | TBD |
| Amortization of the UAL[2] | N/A | N/A | 0.49% | 2.75% | TBD | TBD |
| Sec 121.71 "Uniform" Rate | N/A | N/A | 3.77% | 12.96% | TBD | TBD |

1) Actuarially determined rates assume no change to Investment Plan contribution rates in current statutes.
2) The UAL is currently composed of 11 separate bases. Section 121.031(4) of Florida Statutes requires each new base to be amortized within 30 plan years. The July 1, 2011 valuation weighted average amortization period is 27 years.

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# Actuarial Assumption Conference

- Section 216.136(10), Florida Statutes

"The Florida Retirement System Actuarial Assumption Conference shall develop official information with respect to the economic and noneconomic assumptions and funding methods of the Florida Retirement System necessary to perform the system actuarial study undertaken pursuant to s. 121.031(3). Such information shall include:

- An analysis of the actuarial assumptions and actuarial methods used in the study, and
- A determination of whether changes to the assumptions or methods need to be made due to experience changes or revised future forecasts."

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End of Section

# 2012 Update of the Asset-Liability and Asset Allocation Study

Hewitt ennisknupp
An Aon Company

# Executive Summary



Hewitt ennisknupp
An Aon Company

# Overview

- Changes reflected in the 2012 update:
  - Actual results since the 2011 update, resulting in lower plan funded status
    - Investment return from 4/1/2011 through 12/31/2011 = -4.1%
    - Reduced employer contributions, from deferral of UAL funding
  - Full recognition of plan changes, based on the plan actuary's 7/1/2011 valuation
  - Updated capital market assumptions
    - Lower expected returns for fixed income
    - Relatively small changes in expected returns for other major asset classes
    - Net impact is a higher "equity risk premium"
- Key messages from the 2012 update:
  - Supports continuation of the current policy (with the expanded authority, just approved by the legislature), but also shows some areas where change could be considered.
  - On the target level for overall portfolio risk, there are some conflicting indicators – some supporting an increase in risk, and some supporting a decrease in risk.
  - More liquidity might be desired – and this could be accomplished with some restructuring of the fixed income portfolio.
  - The current expanded authority policy is now being implemented, over a multi-year period, with increased allocations to asset classes favored for diversification of risk under the capital market assumptions (real estate, private equity, and strategic assets). The update re-emphasizes the value of this diversification process.
  - The funding policy has a direct impact on some of the investment policy risk-reward analysis.



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An Aon Company

# Asset-Liability Update



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An Aon Company

# Summary

- The main purpose of the asset-liability update is to monitor the policy regarding the overall risk target (i.e. the split between fixed income assets and all other asset classes, where a return spread over fixed income is expected). The current policy is for 25% fixed income (including 1% cash) and 75% other asset classes (usually referred to as "risk assets" in the asset-liability analysis), shown on page 7.
- In the 2012 update, we see some conflicting indicators:
  - When we focus on the long-term economic cost (15 years), an argument could be made for an increase in the overall risk target
    - This is driven entirely by the higher equity risk premium from current capital market assumptions (now 4.4%, vs a 3.4% assumption used for the 2010 study)
    - If fixed income yields, and return expectations, return to more normal levels the equity risk premium would fall back to something closer to 3.0% – 3.5%, and with this assumption the current policy of 75%/25% remains in the optimal range
    - See chart on page 8
  - When we focus on short-term risk, an argument could be made for a decrease in the overall risk target
    - Projections show that recovering from a sharp drop in the plan funded status can be very difficult in a significant number of scenarios
    - This is largely a function of the way funding rates are determined under the actuarial cost method and amortization policy for the unfunded actuarial liability
    - See charts on pages 9 and 10



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An Aon Company

# Best Estimate Return – 75% Risk Assets + 25% Fixed Income

| | Current Policy Targets* | --- Expected Average Return --- Compounded | Single Year | Standard Deviation | |
|---|---|---|---|---|---|
| ***Global Equity*** | 52% | 8.5% | 10.6% | 20.8% | |
| ***Private Equity*** | 5% | 9.2% | 13.2% | 28.3% | |
| ***Real Estate*** | 7% | 7.1% | 8.4% | 16.3% | |
| ***Strategic*** | | | | | |
| ***Debt-oriented*** | 3% | 9.5% | 10.1% | 10.5% | ***Risk Assets*** |
| ***HF - Absolute Return*** | 2% | 5.8% | 6.3% | 9.3% | |
| ***HF - Equity Long/Short*** | 2% | 7.7% | 8.4% | 11.5% | |
| ***HF - Open Mandate*** | 2% | 7.3% | 7.8% | 10.6% | |
| ***Infrastructure*** | 2% | 8.5% | 10.2% | 18.3% | |
| ***US Bonds*** | 24% | 3.0% | 3.1% | 3.5% | ***Fixed Income*** |
| ***Cash*** | 1% | 2.2% | 2.2% | 1.3% | |
| ***Inflation*** | | 2.1% | | | |
| ***Total Portfolio*** | | | | | |
| ***Gross*** | | 7.5% | 8.4% | | |
| ***Expenses*** | | 0.14% | 0.14% | | |
| ***Net - Nominal Return*** | | **7.4%** | **8.3%** | 13.0% | |
| ***Net - Real Return*** | | **5.3%** | | | |

** Allocation targets based on "Expanded Authority" policy, with typical diversification within the "Strategic" class*



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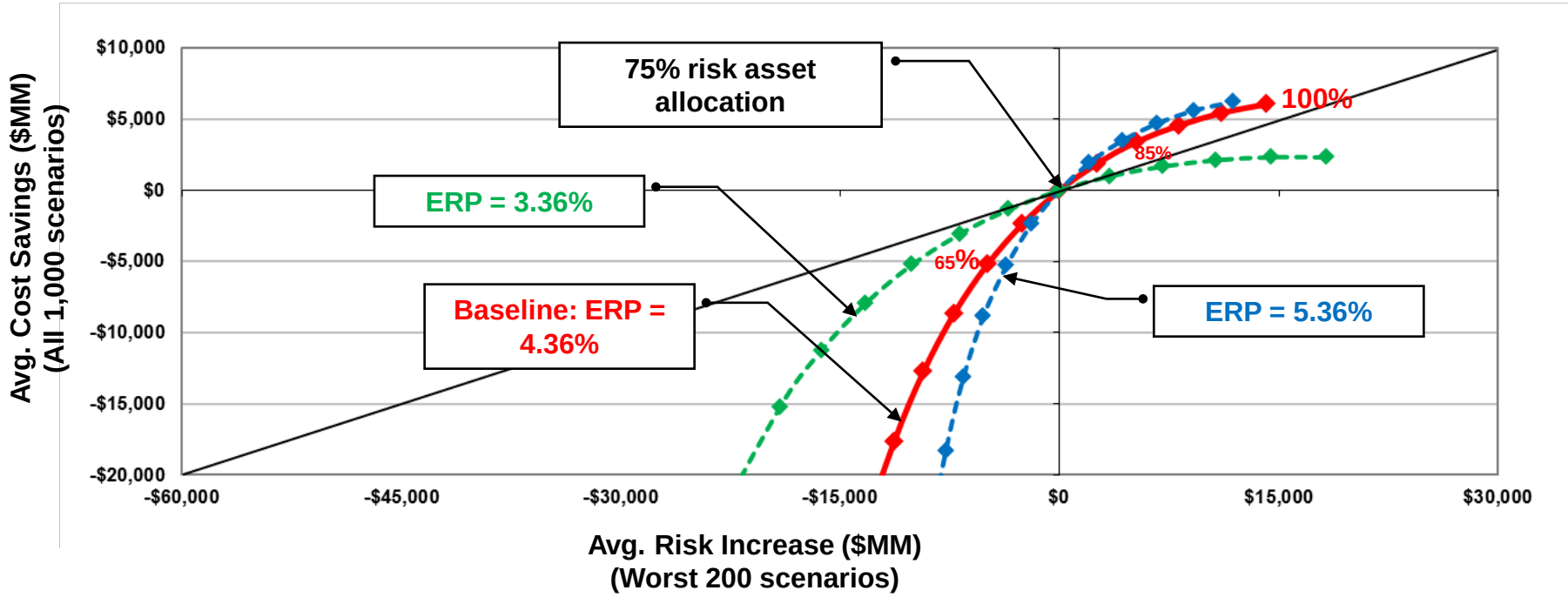
# 2012 Risk-Reward Analysis:
# Sensitivity to Equity Risk Premium Assumption




Observation: The shift in the risk-reward curve appears to be almost entirely due to the increased equity risk premium assumption now (4.36%), versus the assumption used in the 2010 study (3.36%). The green line above, based on a 3.36% equity risk premium assumption supports the current 75% allocation to risk assets.



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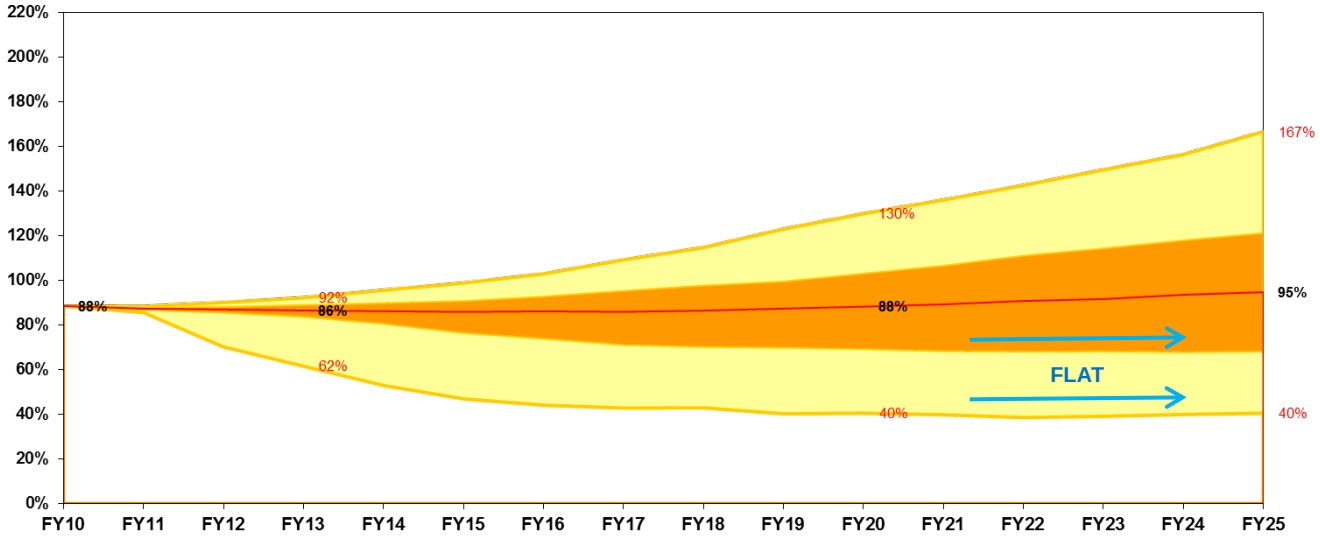
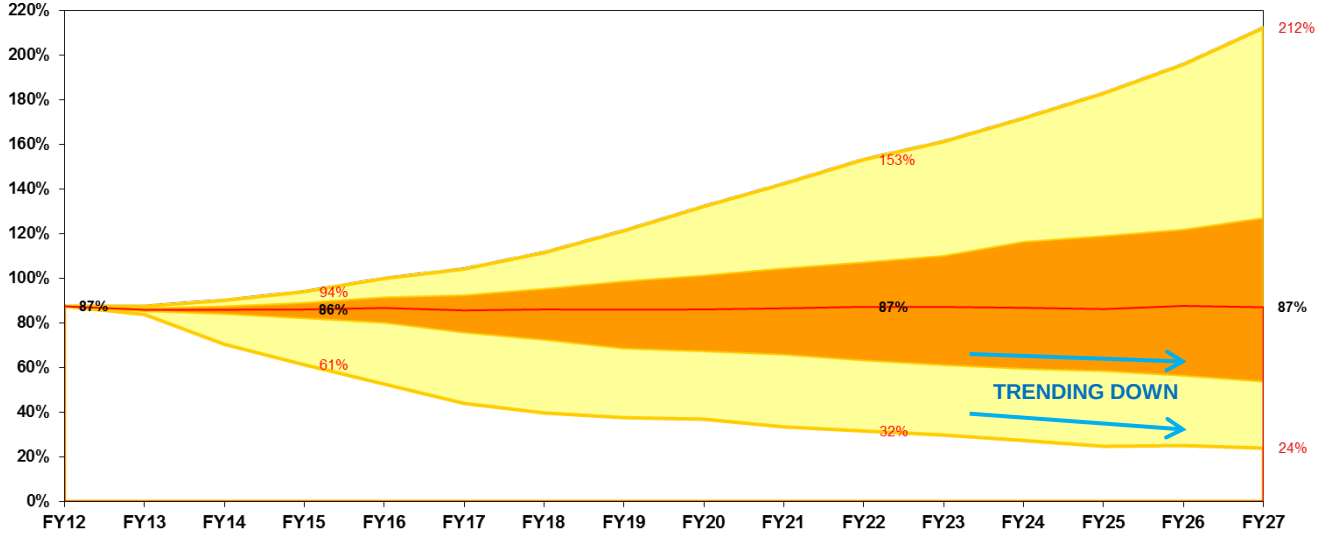
# Range of Funded Ratios – Compare 2010 With 2012

From 2010 AL study
Before plan changes




From 2012 AL study
After plan changes

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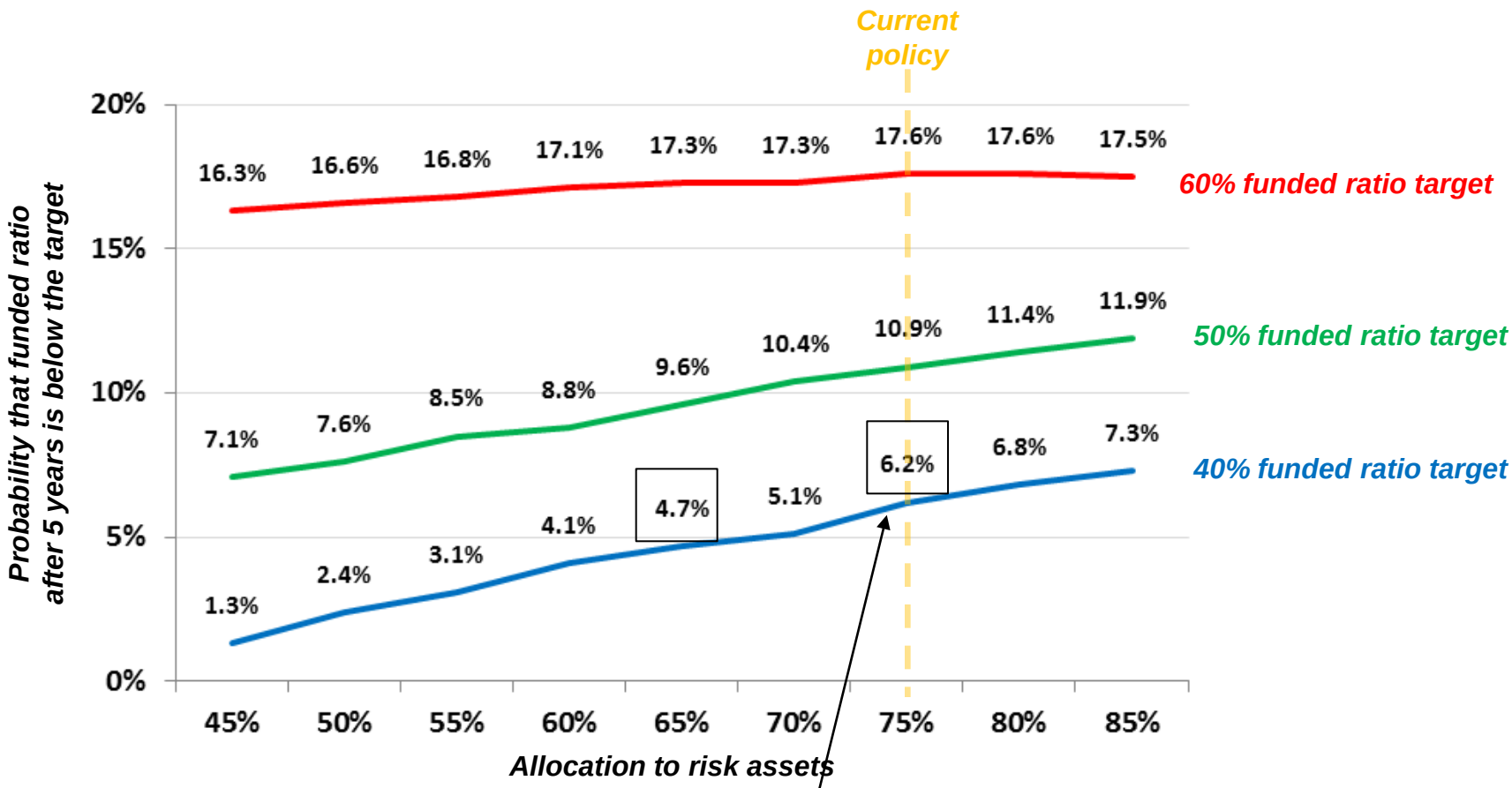
# Short-Term Funded Ratio Shortfall Analysis




**Under current policy there is a 6.2% chance that the funded ratio after 5 years will be below 40%. With a 65% risk asset allocation, this probability falls to 4.7%.**



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# Impact of Pension Funding and/or Benefit Policy Changes

- Immediate -- Continue to defer funding of UAL.
  - May amount to about $1 billion lower contribution for FY 2013-2014.
  - Equivalent to a one-time negative investment return “headwind” of about 0.8%.
  - Shortfall would be amortized over 30 years and added to future cost rate.
  - Would lower funded status slightly.
- Later? – Change in actuarial assumptions for cost calculations
  - For example, lower assumed return assumption from 7.75% to 7.25% and lower wage increase assumption from 4% to 3%.
  - Employer cost would increase (maybe about 2% of payroll).
  - Reported funded status would decrease (maybe about 7-8 percentage points).
  - After testing our model, we find that the risk-reward curve based on our long-term economic cost metric would remain almost unchanged.
  - To be considered by the FRS Actuarial Assumption Estimating Conference
- Later? – Revised funding cost methodology
  - Goal would be to provide more funding support if return targets are not met, and mitigate the risk of persistent low funded ratios if returns fall below target levels.
  - Could include changes in the amortization method (either shorter period and/or level dollar amounts, instead of level percent of payroll method).
  - Could include a change in the actuarial cost method (switch to “traditional” Entry Age, from the current “ultimate” Entry Age method).
  - Issues here would also be considered by the FRS Actuarial Assumption Estimating Conference.



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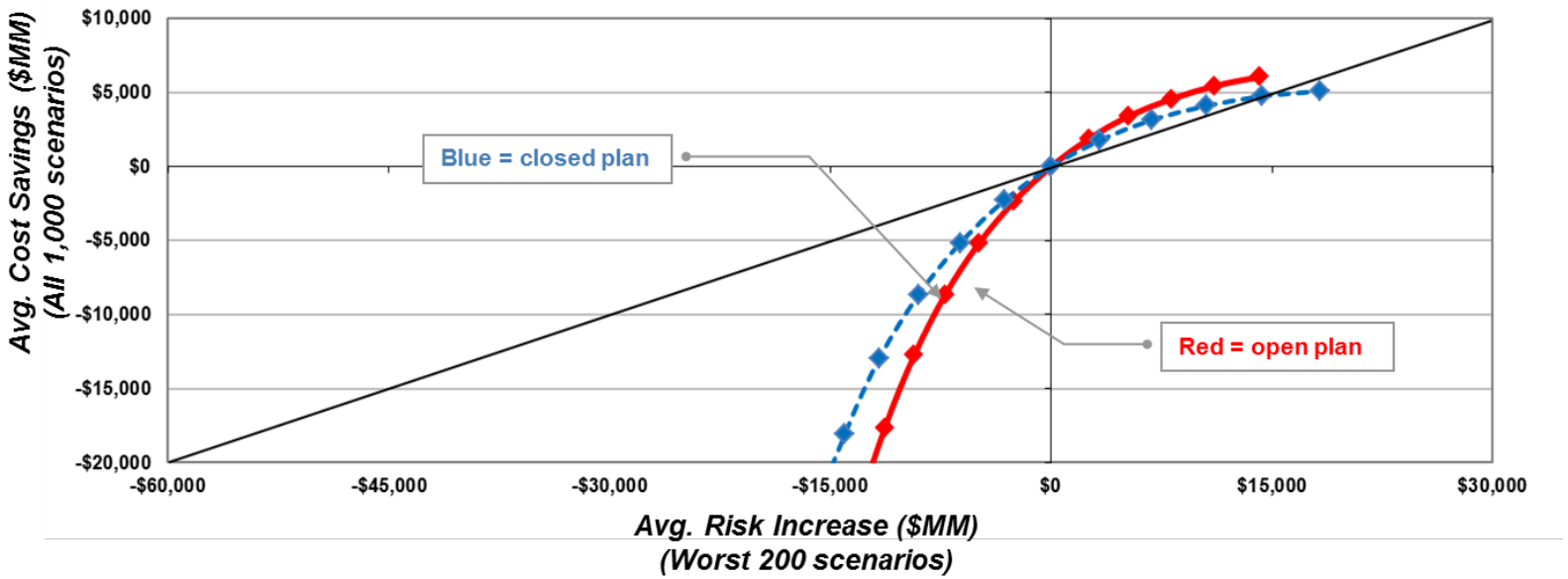
# Impact of Pension Funding and/or Benefit Policy Changes (cont'd.)

- Later? -- Switch the default election from DB pension (now) to Investment Plan.
  - Projected IP elections likely to move from 25% up to 50%+
  - We ran model with a 54% IP election rate – there was no significant change in the risk-reward curve.
- Later? -- Close the DB pension to new hires.
  - There is a shift in the risk-reward curve towards somewhat less risk. Initially, the shift will be fairly small, but the effect is likely to become more pronounced over time



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# Asset Allocation Update



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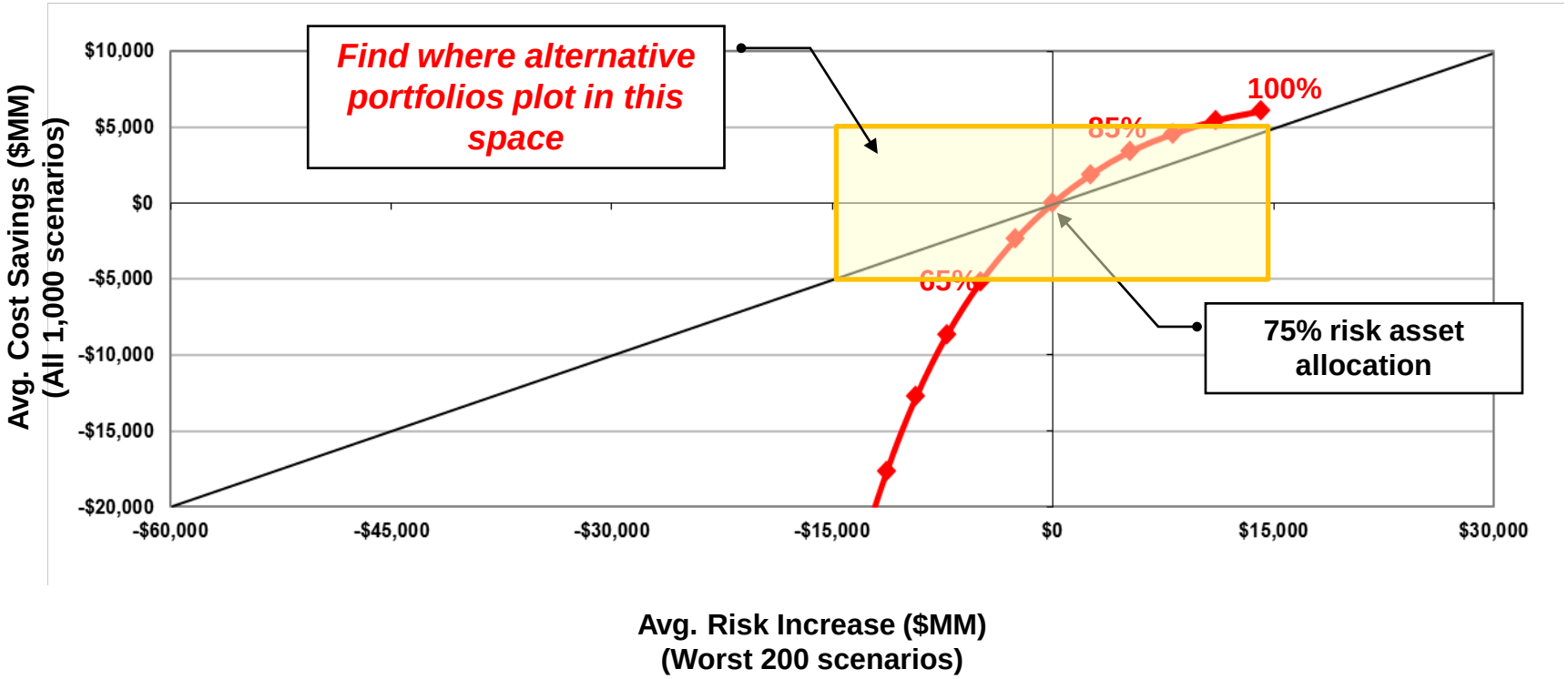
# Asset Allocation – Drilling Down




<u>Observation</u>: The risk-reward curve has shifted in the direction of suggesting a higher allocation to risk assets. However, there are no real marginal gains beyond an 85% allocation target.



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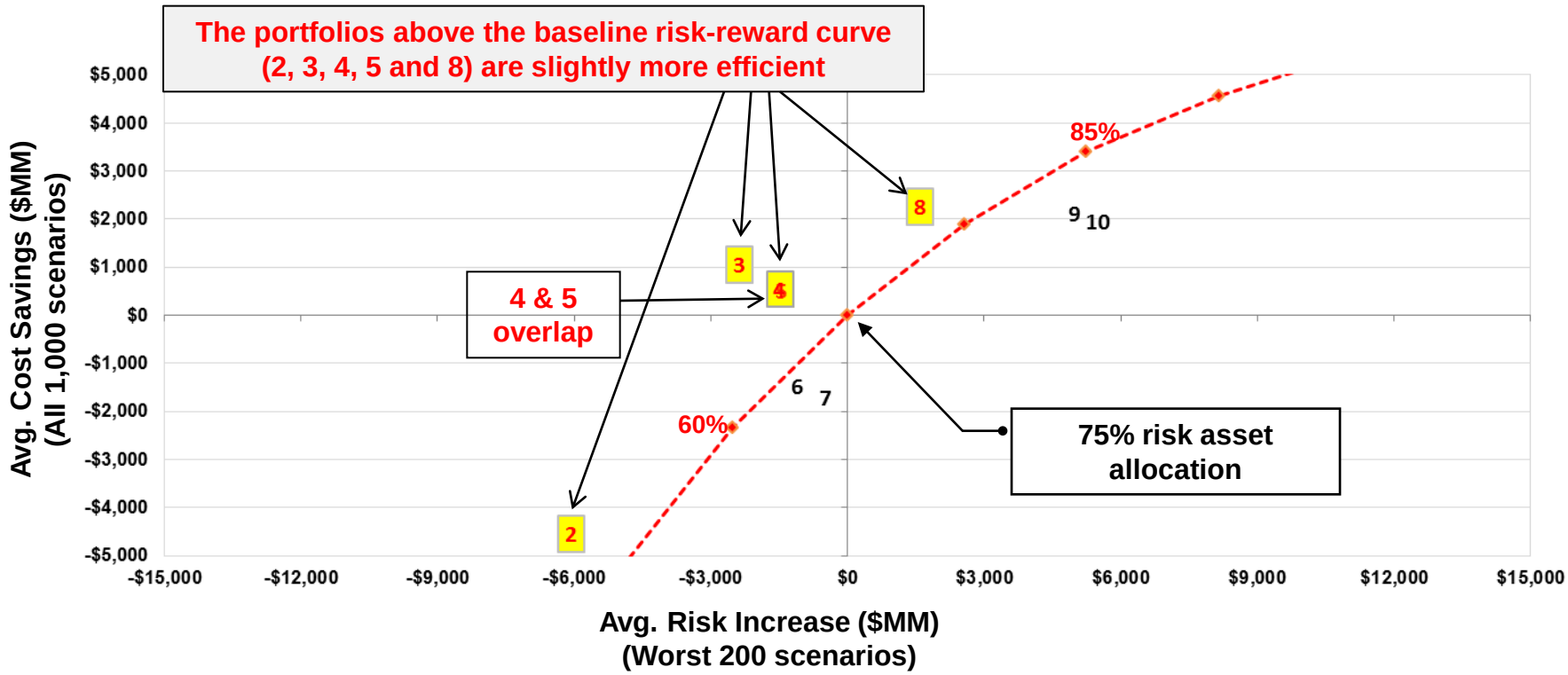
# Asset Allocation – Alternative Portfolios




NOTE: All results shown here are based on the current fixed income framework (1% cash + balance in core) – but any of the alternative portfolios could also include revised fixed income structures with increased liquidity. All of these portfolios are shown in the appendix.



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# Asset Allocation – Alternative Portfolios

| | ---------- Alternative Portfolios---------- | | | | | |
|---|---|---|---|---|---|---|
| | 2 | 3 | 4 | 5 | | 8 |
| | 10% to FI | EQ to SI (7%) | EQ to RE/SI (5%) | EQ to RE (5%) | Current policy: Expanded | FI to RE/SI (5%) |
| **Global Equity** | 42% | 45% | 47% | 47% | 52% | 52% |
| **Real Estate (Broad Market)** | 7% | 7% | 10% | 12% | 7% | 10% |
| **Private Equity** | 5% | 5% | 5% | 5% | 5% | 5% |
| **Debt-Oriented Funds** | 3% | 5% | 4% | 3% | 3% | 4% |
| **Commodities** | 0% | 0% | 0% | 0% | 0% | 0% |
| **Absolute Return HFs** | 2% | 4% | 3% | 2% | 2% | 3% |
| **Hedge Funds – Equity Long/Short (Universe)** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Open Mandate HFs** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Infrastructure** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Core Fixed Income (Market Duration)** | 34% | 24% | 24% | 24% | 24% | 19% |
| **Cash** | 1% | 1% | 1% | 1% | 1% | 1% |
| | | | | | | |
| **Expected Geometric Return** | | | | | | |
| **Nominal Gross** | **7.02%** | **7.51%** | **7.51%** | **7.51%** | **7.54%** | **7.76%** |
| **Expenses** | **0.14%** | **0.14%** | **0.14%** | **0.14%** | **0.14%** | **0.14%** |
| **Nominal Net** | **6.88%** | **7.37%** | **7.37%** | **7.37%** | **7.40%** | **7.62%** |
| | | | | | | |
| **Real Net** | **4.85%** | **5.35%** | **5.34%** | **5.34%** | **5.37%** | **5.60%** |
| | | | | | | |
| **Expected Risk (Annual Return S.D.)** | **10.97%** | **12.01%** | **12.29%** | **12.33%** | **12.95%** | **13.29%** |
| **Sharpe Ratio** | **0.442** | **0.444** | **0.434** | **0.433** | **0.414** | **0.420** |

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# Asset Allocation – Alternative Portfolios (cont'd.)

| | ---------- Alternative Portfolios---------- | | | | | |
|---|---|---|---|---|---|---|
| | 2 | 3 | 4 | 5 | | 8 |
| | 10% to FI | EQ to SI (7%) | EQ to RE/SI (5%) | EQ to RE (5%) | Current policy: Expanded | FI to RE/SI (5%) |
| **Global Equity** | 42% | 45% | 47% | 47% | 52% | 52% |
| **Real Estate (Broad Market)** | 7% | 7% | 10% | 12% | 7% | 10% |
| **Private Equity** | 5% | 5% | 5% | 5% | 5% | 5% |
| **Debt-Oriented Funds** | 3% | 5% | 4% | 3% | 3% | 4% |
| **Commodities** | 0% | 0% | 0% | 0% | 0% | 0% |
| **Absolute Return HFs** | 2% | 4% | 3% | 2% | 2% | 3% |
| **Hedge Funds – Equity Long/Short (Universe)** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Open Mandate HFs** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Infrastructure** | 2% | 3% | 2% | 2% | 2% | 2% |
| **Core Fixed Income (Market Duration)** | 34% | 24% | 24% | 24% | 24% | 19% |
| **Cash** | 1% | 1% | 1% | 1% | 1% | 1% |
| **Long-term economic cost:** | | | | | | |
| **Cost savings** | **$ (4,547)** | **$ 1,060** | **$ 544** | **$ 526** | **$ -** | **$ 2,259** |
| **Risk increase** | **$ (6,079)** | **$ (2,378)** | **$ (1,492)** | **$ (1,495)** | **$ -** | **$ 1,588** |
| **Funded ratio shortfall risk after 5 years:** | | | | | | |
| **<60%** | **16.7%** | **16.7%** | **17.0%** | **17.0%** | **17.6%** | **17.3%** |
| **Probabilities that 15-yr. returns:** | | | | | | |
| **Net nominal return > 7.75%** | **43.9%** | **51.5%** | **51.5%** | **51.5%** | **50.4%** | **53.3%** |
| **Net nominal return > 7.25%** | **49.9%** | **55.7%** | **55.4%** | **55.4%** | **55.6%** | **58.0%** |
| **Net real return > 5.00%** | **52.2%** | **56.9%** | **56.8%** | **56.7%** | **56.8%** | **58.2%** |

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# Appendix



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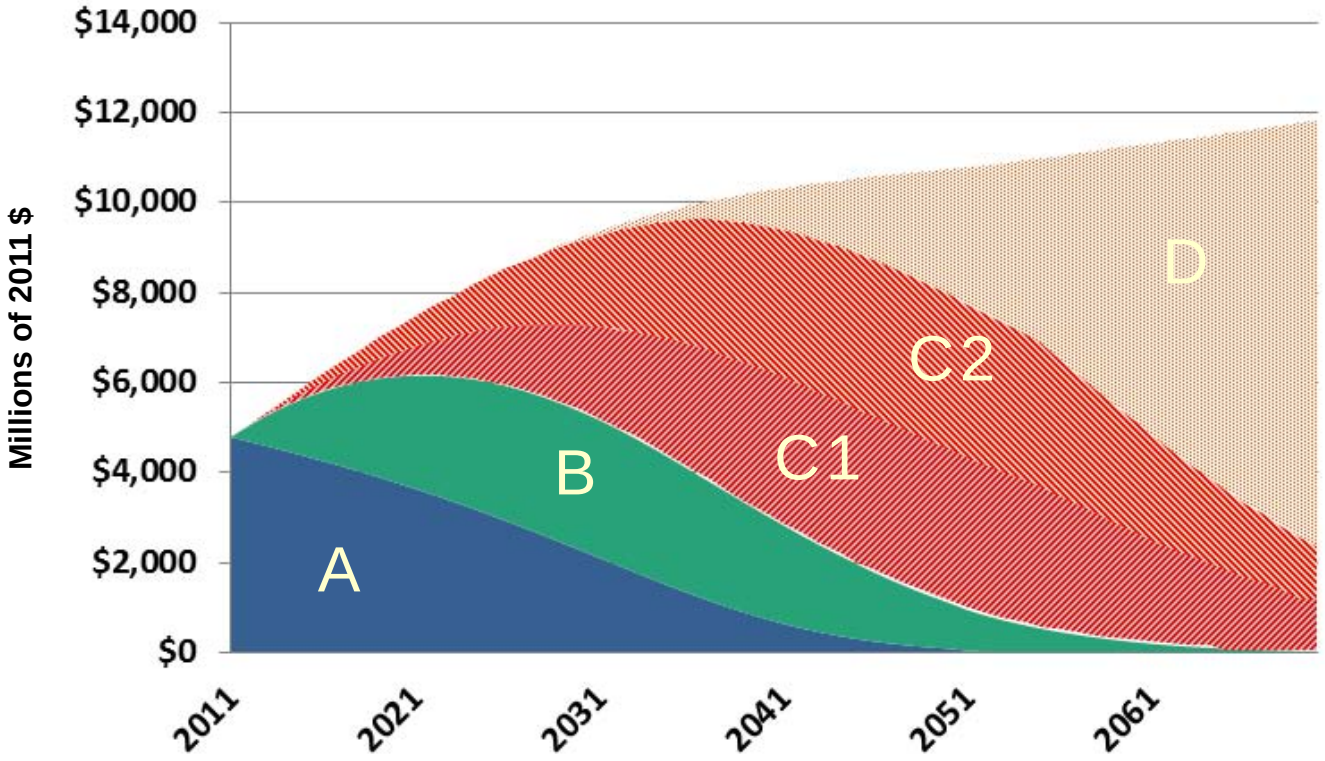
# Pension Obligations – Future Benefit Cash Flows




A = benefits for current retirees
B = benefits already accrued/earned for current employees
C1+C2 = benefits yet to be earned for current employees
(C1 = portion allocated by actuarial method for past service)
D = benefits for future employees



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# Pension Obligations – Liability Measures

- A liability measure is calculated by:
  - Taking future cash flow estimates
  - Discounting the value of each yearly amount by some rate of interest, or discount rate
  - Adding all these values into a single amount
- Different liability amounts result from:
  - Including different portions of the total future cash flow stream
  - Using different discount rates
    - A higher rate to reflect the expected future investment return (e.g. 7.75%)
    - A risk-free, or low risk, bond yield (e.g. 5.5% - 6.0%)
- Different calculations may be more appropriate for certain purposes:
  - Measuring current balance sheet exposure
    - Accumulated Benefit Obligation ("ABO") measure – includes cash flow segments A + B
    - Can be measured using either low risk bond yields, or expected portfolio return
  - Guiding long term funding rates
    - For corporate plans, the ABO measure based on current bond yields is used
    - For public plans, the funding target is
      - More comprehensive – it includes cash flow segment C1
      - Based on the actuary's estimate of expected portfolio return (currently 7.75% for FRS)



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# Pension Liability Measures

**Estimated FRS Pension Liability at 7/1/2011 (billions):**

| *Benefit payment layer:* | *----- Discount Rate -----* 7.75% Expected Return | 6.00% AA Corp. Bond Yields | *Discount* 7.75% Expected Return |
|---|---|---|---|
| *A* | $ 90 | $ 108 * | $ 90 |
| *B* | $ 28 | $ 38 * | $ 28 |
| *C1* | NA | NA | $ 26 |
| *Total* | $ 118 | $ 146 * | $ 144 |

** rough estimate*

| ABO measured at 7.75% -- disclosed in FRS annual report | ABO measured at 6.00% -- comparable to corporate plan measurement | Funding target used by actuary to determine funding rates |
|---|---|---|



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# U.S. Equity Return

- For the 2012 asset liability update we used an equity risk premium assumption equal to 4.36%, the average of the assumptions used by the four SBA investment consultants. The resulting expected average compounded return for U.S. equities is equal to 7.4% (the U.S. bond expected return of 3.0% plus the equity risk premium of 4.4%):

| | ***2010 AL Study*** | ***2011 AL Update*** | ***2012 AL Update*** |
|---|---|---|---|
| **Price inflation** | 2.40% | 2.15% | 2.10% |
| **US bond returns** | 4.60% | 4.20% | 3.00% |
| **Risk premium for US equities** | | | |
| **HEK** | 2.40% | 3.60% | 4.50% |
| **Callan** | 4.00% | 4.25% | 4.50% |
| **Wilshire** | 3.25% | 3.50% | 4.65% |
| **Mercer** | 3.80% | 3.80% | 3.80% |
| **Average** | 3.36% | 3.79% | 4.36% |
| **US equity returns** | 7.96% | 7.99% | 7.36% |

***All returns are 15-year geometric average expected returns.***



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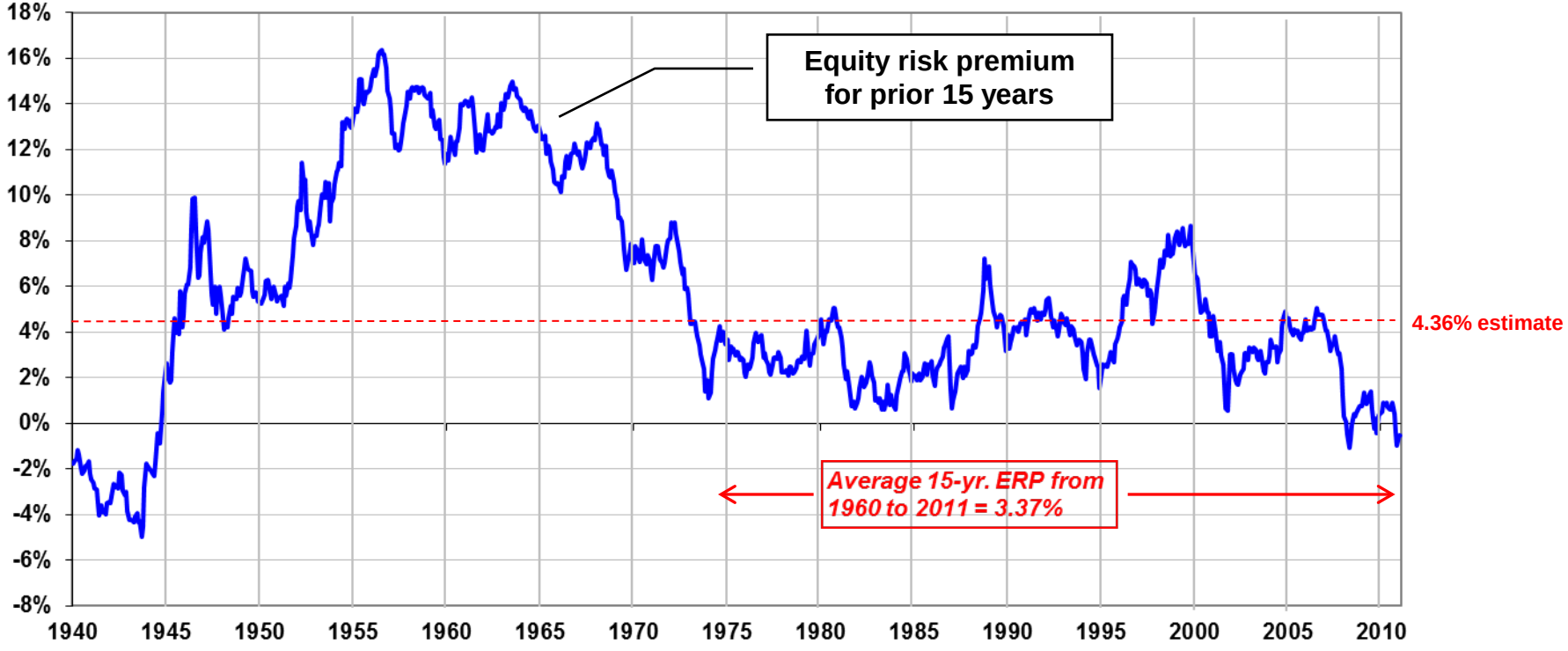
# Equity Risk Premium

- The equity risk premium is the difference between the expected return on US equities and the expected return on US bonds, using compounded returns.
- This is the single most important assumption for an asset-liability study, as it establishes the price of risk.
- Historical equity risk premiums over 15-year time periods are not very stable:



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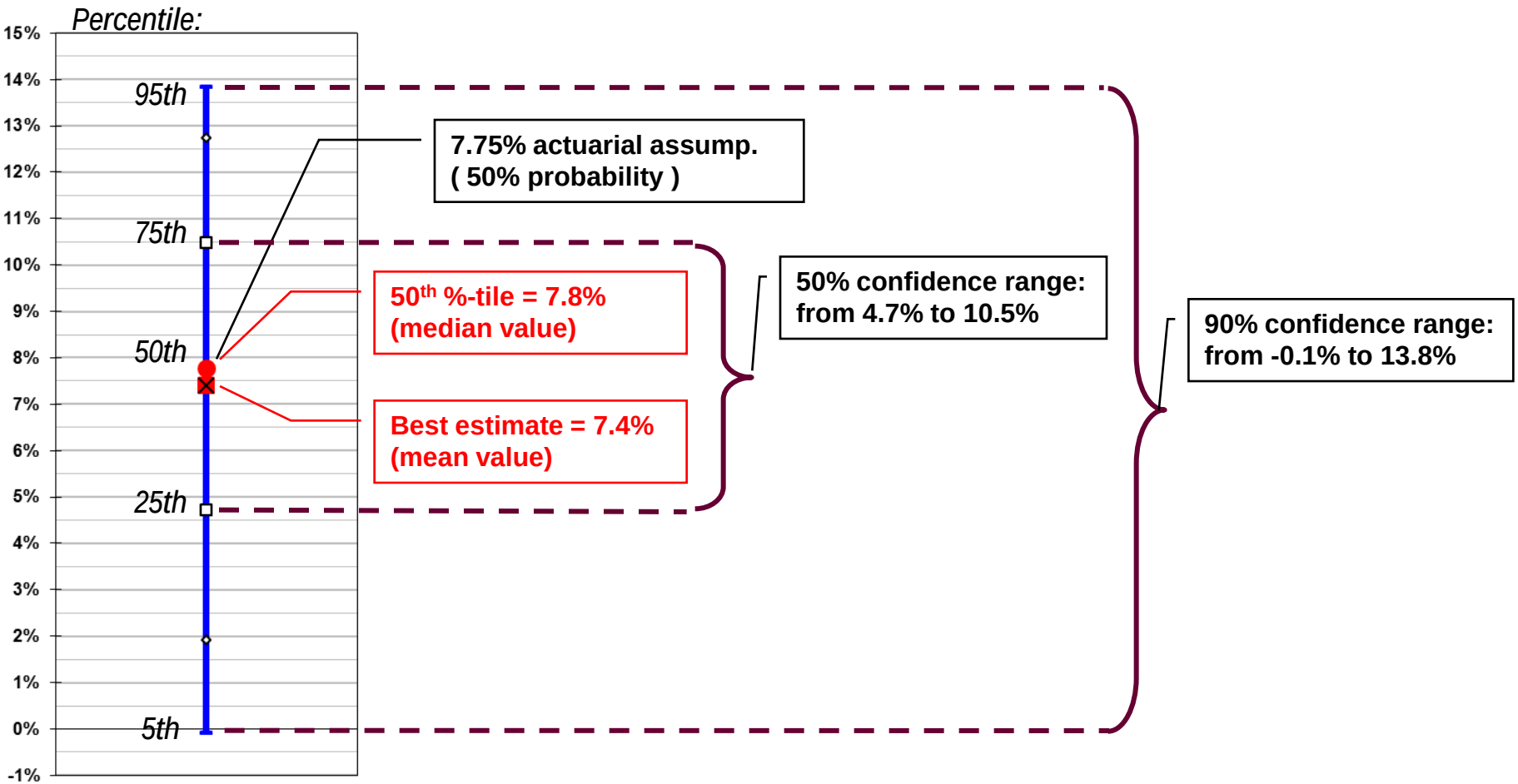
# Range of Possible 15-Year Compound Returns -- Nominal



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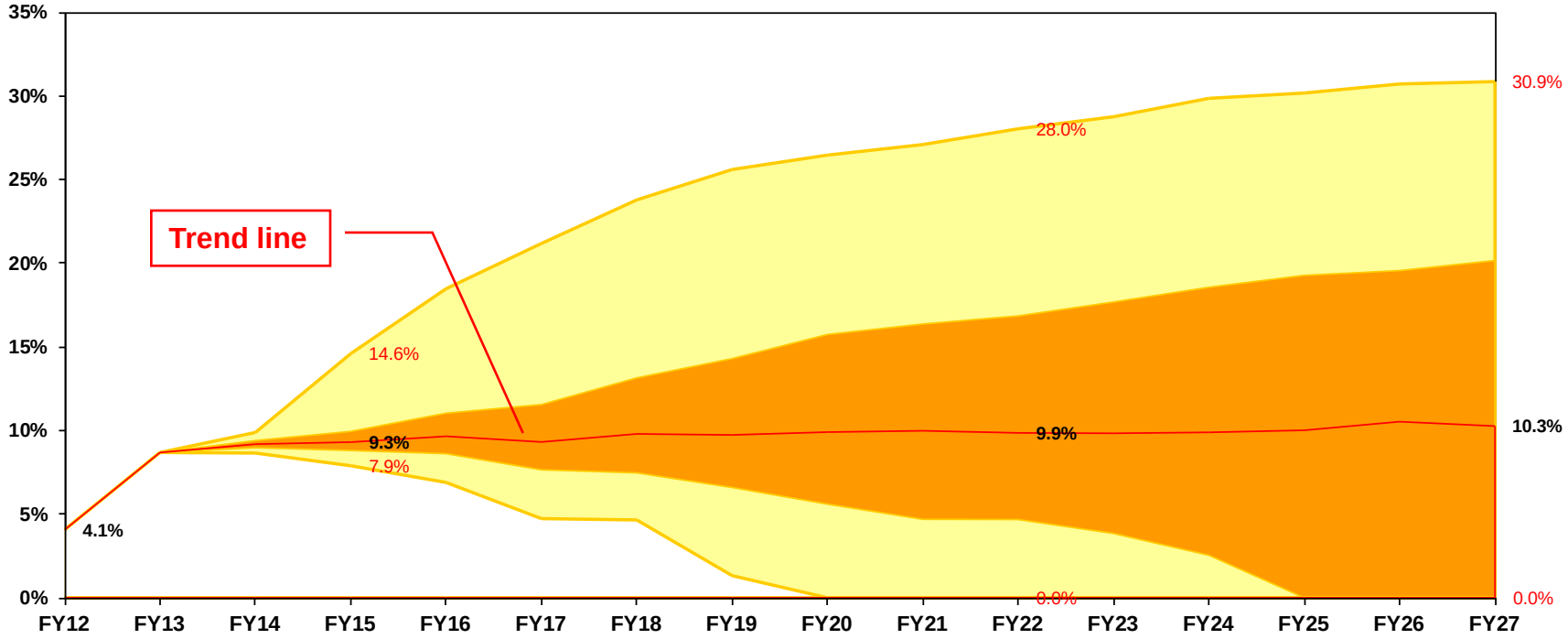
# Range of Employer Contribution Rates (DB Plan Only) – Current 75% Risk Asset Allocation




**%-tile values:**

| | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5% | 4.1% | 8.7% | 8.6% | 7.9% | 6.9% | 4.7% | 4.7% | 1.3% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| 25% | 4.1% | 8.7% | 9.0% | 8.8% | 8.6% | 7.6% | 7.5% | 6.6% | 5.6% | 4.7% | 4.7% | 3.8% | 2.5% | 0.0% | 0.0% | 0.0% |
| **50%** | **4.1%** | **8.7%** | **9.2%** | **9.3%** | **9.7%** | **9.3%** | **9.8%** | **9.7%** | **9.9%** | **10.0%** | **9.9%** | **9.8%** | **9.9%** | **10.0%** | **10.5%** | **10.3%** |
| 75% | 4.1% | 8.7% | 9.4% | 9.9% | 11.0% | 11.5% | 13.1% | 14.3% | 15.7% | 16.4% | 16.8% | 17.7% | 18.6% | 19.3% | 19.6% | 20.2% |
| 95% | 4.1% | 8.7% | 9.9% | 14.6% | 18.5% | 21.2% | 23.8% | 25.6% | 26.5% | 27.1% | 28.0% | 28.8% | 29.9% | 30.2% | 30.7% | 30.9% |

**Dark shaded area indicates the 50% probability zone, and light shaded area indicates the 90% probability zone.**



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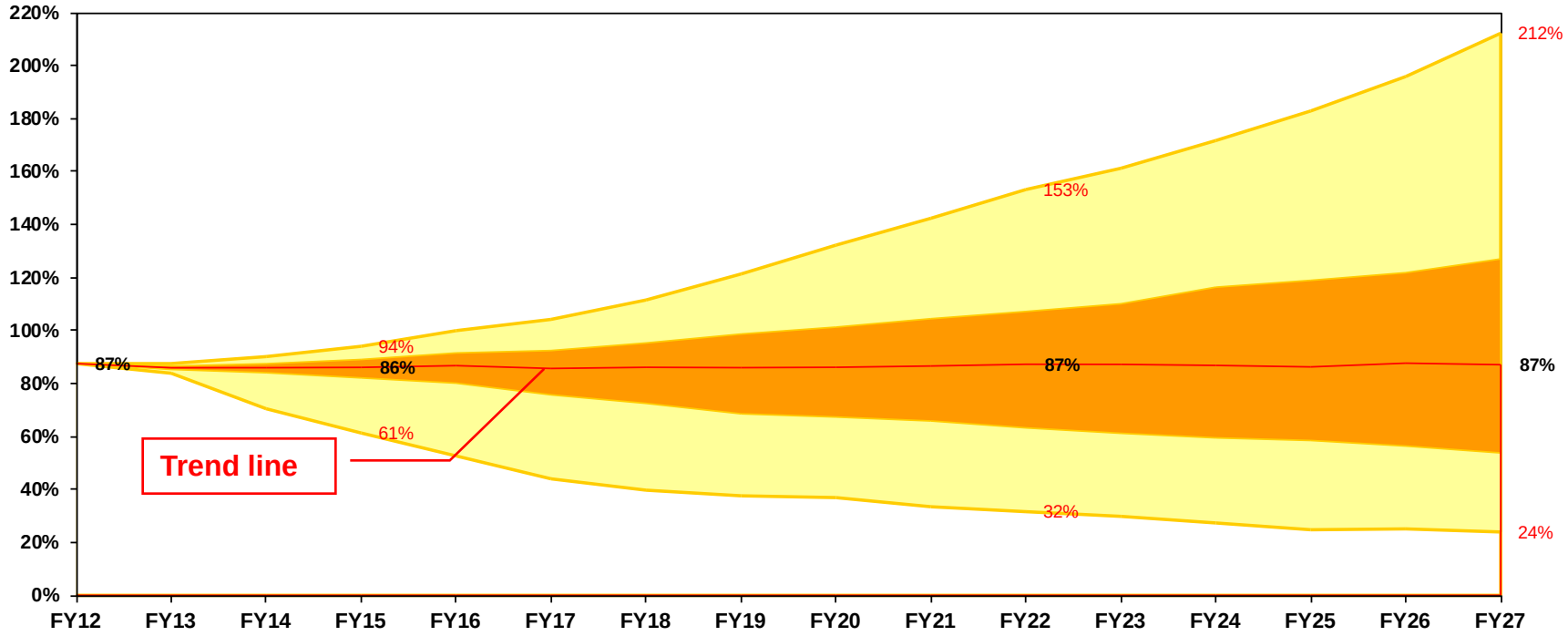
# Range of Funded Ratios – Current 75% Risk Asset Allocation




**%-tile values:**

| | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 5% | 87% | 84% | 70% | 61% | 53% | 44% | 40% | 38% | 37% | 33% | 32% | 30% | 27% | 25% | 25% | 24% |
| 25% | 87% | 85% | 84% | 82% | 80% | 76% | 72% | 69% | 67% | 66% | 63% | 61% | 59% | 58% | 56% | 54% |
| **50%** | **87%** | **86%** | **86%** | **86%** | **87%** | **86%** | **86%** | **86%** | **86%** | **87%** | **87%** | **87%** | **87%** | **86%** | **88%** | **87%** |
| 75% | 87% | 87% | 87% | 89% | 91% | 92% | 95% | 99% | 101% | 104% | 107% | 110% | 116% | 119% | 122% | 127% |
| 95% | 87% | 87% | 90% | 94% | 100% | 104% | 111% | 121% | 132% | 142% | 153% | 161% | 172% | 183% | 196% | 212% |

**Dark shaded area indicates the 50% probability zone, and light shaded area indicates the 90% probability zone.**



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# Appendix
# Liquidity Analysis



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# Sources and Uses of Liquidity

**Net Cash Outflow: Benefit Payments – Employer & Employee Contributions**

| Annual as % of Total Fund | | | | | |
|---|---|---|---|---|---|
| Percentile | FY 2013 | FY 2014 | FY 2015 | FY 2016 | FY 2017 |
| 95% | 5.0% | 6.8% | 7.6% | 10.2% | 7.2% |
| 75% | 4.5 | 5.3 | 5.8 | 7.6 | 5.7 |
| 50% | 4.3 | 4.9 | 5.2 | 6.7 | 5.0 |
| 25% | 4.2 | 4.5 | 4.8 | 5.9 | 4.5 |
| 5% | 4.0 | 4.1 | 4.2 | 5.0 | 3.9 |

# Internal Fund Cash Flow

**Recurring Cash Yield on Investments**

| | | Cash Return | |
|---|---|---|---|
| Asset Class | Policy Allocation | Long-Term | Stressed |
| U.S. Equities | 23% | 3.6% | 2.0% |
| Foreign Equities | 29% | 4.2 | 2.0 |
| Core Fixed Income | 24% | 2.7 | 2.7 |
| Cash | 1% | 1.0 | 1.0 |
| Real Estate | 7% | 4.3 | 3.0 |
| Private Equity | 5% | 0.0 | 0.0 |
| Strategic Investments | 11% | 0.0 | 0.0 |
| **Total Fund** | **100%** | **3.0%** | **1.9%** |

**Non-Recurring Cash Flow – Range for RE + PE + SI combined likely to be -0.5% to -1.5% of total fund value.**

# Alternatives to Enhance Liquidity

- Increase cash allocation
- Implement a duration-neutral barbell into the fixed income allocation
  - A short-duration fund (maturity 1-3 years, duration 2 years) for liquidity
  - A long-duration fund (duration 11-12 years) to maintain a market-based duration
  - Example
    - Target 3 years of liquidity, based on net cash outflow from previous slide
    - Requires a short-duration fund allocation of about 10%
    - The required long-duration fund allocation would be about 4-5%
    - The balance of the fixed income portfolio would remain in a core strategy
  - Issues
    - Laddered maturity structure for short-duration fund?
    - Utilize credit bonds?
    - Tactical implementation for long-duration fund?
    - Rebalancing protocol?
- Increase allocation to classes with higher cash returns (e.g. real estate)



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# Liquidity Options: Analysis of Cost Impact

| Economic Cost Metric ($ Billion) | Reward (All 1,000) | Risk (Worst 200) |
|---|---|---|
| Current (1% Cash) | $66,029 | $191,318 |
| 3% Cash | $66,615 | $191,973 |
| % Change from Current | 0.89% | 0.34% |
| Sample Barbell | $65,468 | $190,740 |
| % Change from Current | -0.85% | -0.30% |

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End of Section

# 2012 Corporate Governance Principles & Proxy Voting Guidelines

SBA FLORIDA

INVESTING FOR FLORIDA'S FUTURE

# SBA Perspectives on Corporate Governance

- Maximize economic value of investment
- Promote and protect shareowner rights
- Alignment of interests between investors and management
- Allow management appropriate discretion
- Avoid attempts to micromanage company's day-to-day operations or business strategies
- Elect competent directors who are knowledgeable regarding company issues and capable of making well-informed decisions

# What are Shareowner Proposals?

- Shareowners can submit resolutions on corporate issues
- SEC Rule 14(a)8 governs the submission process
- ~ 500 proposals are submitted annually
- Investors may withdraw proposals prior to AGM vote
- SBA periodically submits proposals

# Summary Voting Statistics (as of 12/31/11)

| | |
|---|---|
| **Votes in Favor of Directors**<br>**77.3%** (FY2011=76.7%) | **Votes with Management**<br>**78.6%** (FY2011=78.9%) |
| **Votes in Favor of Auditors**<br>**89.2%** (FY2011=90.0%) | **Total Ballot Items Voted**<br>**70,306** (FY2011=56,536) |
| **Votes in Favor of All Governance Proposals**<br>**71.7%** (FY2011=71%) | **Total Proxies Voted**<br>**7,630** (FY2011=6,138) |

# Proxy Voting Guidelines

- Comprehensive
- Empirical grounding
- Ensures consistent voting
- Modeled on best practice

# DOL Guidance

- Act solely in the best interest of beneficiaries
- Act as an owner in exercising proxy votes and electing board of directors, which appoints and monitors management
- Prudently manage proxy voting rights as an asset

# SBA Proxy Voting Guidelines

- Structure:
  - Principles
    - high level, global best practices
  - Policy narrative
    - mid level, individual topics, empirical support
  - Guidelines
    - lowest level, factors used to make voting decision
- Account coverage

# 2012 Updates

- General edits:
  - Empirical citations added
  - Additional policy narrative
- Amended Guideline: **Proxy Access**
- New Guideline: **Exclusive Judicial Forum Provisions**

**UPDATES TO SBA 2012 CORPORATE GOVERNANCE PRINCIPLES & PROXY VOTING GUIDELINES**

Amended Guideline: This updated guideline deals with the newly enacted process allowing investors the ability the submit shareowner proposals to implement procedures to nominate investor-selected candidates to the board of directors.

⇨ **Proxy Access: FOR**

In late 2009, the SEC proposed to allow shareowners the right to place director candidates within the company's proxy materials. "By making it easier for shareholders to replace directors, proxy access can contribute to making directors more accountable to shareholders and more attentive to their interests."[1] The SBA supported this proposal, which would have set an access default with the freedom to opt-out to a no-access regime. Additional reforms occurred in August 2009, dramatically changing Delaware Law governing the ability of shareowners to nominate directors and make other nomination oriented changes to a company's bylaws. Delaware General Corporation Law ("DGCL") Section 112 permits shareowners to adopt bylaws that require the corporation to include shareowner nominees for board election and permits the right to be conditioned on several factors. Section 113 of the DGCL permits shareowners to adopt bylaws that require the reimbursement of expenses incurred by a shareowner in connection with a proxy solicitation, again, with certain permitted conditions.[1] Some observers view proxy access without a corresponding solicitation reimbursement mechanism to be less than optimal and represent a shortcoming in the ability of shareowners to have meaningful input into selecting their own director representatives.

In July 2011, the SEC rule covering a mandatory proxy access default (Rule 14a-11) was legally overturned. The SEC's corresponding Rule 14a-8(i)(8) covering the adoption of proxy access mechanisms through individual shareowner resolutions, commonly referred to as "private ordering," was implemented in September 2011. Shareowners in the United States are now permitted to require companies to include shareowner proposals regarding proxy access procedures in company proxy materials beginning in 2012. Such proposals may be submitted either as precatory (advisory) proposals or binding proposals.

The SBA will generally vote FOR proposals that allow significant company shareowners access to management's proxy material in order to nominate their own candidates to the board of directors. The original 2009 proposal contained within SEC Rule 14a-11, requiring a three percent ownership and a three year holding period, is considered a reasonable benchmark against which individual shareowner proposals can be compared.

Factors to be assessed by the SBA include, but are not limited to:

- Ownership thresholds stipulated by the proposal;
- Maximum proportion of the full board that shareowners may nominate in a single year; and
- Other procedural matters, such as listing order within the proxy, ownership certification requirements, etc.

Proposals that require an investor (or group of investors) to own a meaningful percentage of the company's voting stock, generally defined as greater than one percent, are favored. Proposals that require ownership for meaningful periods of time, generally defined as greater than one year, are favored. The SBA may vote AGAINST proposals which contain burdensome or otherwise restrictive requirements, such as ownership or holding thresholds which are set at impractical levels.

1 Bebchuk, Lucian A. and Scott Hirst, "Private Ordering and the Proxy Debate." Harvard Law School. Discussion Paper No. 653. 11/2009 Available at SSRN: http://papers.ssrn.com/abstract=1513408.

New Guideline: this new guideline deals with changes to a corporate charter (or bylaws) that can restrict an investor's ability to pursue legal remedy.

⇨ **Exclusive Judicial Forum Provisions: CASE-BY-CASE**

In a March 2010 opinion, the Delaware Court of Chancery provided an opportunity for any Delaware corporation to establish the Court as the exclusive forum for "intra-entity" corporate disputes, such as claims of breach of fiduciary duty. Such claims have been used to overturn directors' business judgments on mergers, and other matters. Early adopters of the exclusive forum provision chose to enact bylaw provisions without seeking shareowner approval. However, the Galaviz v. Berg decision by the U.S. District Court for Northern California provided that Oracle's exclusive forum provision was unenforceable, in part due to Oracle's failure to bring the provision before shareowners. Subsequently, a number of U.S. companies have decided to bring the exclusive forum provision to a shareowner vote and others have amended their charter or by-law provisions.[1]

The SBA generally opposes restrictions on shareowner ability to pursue derivative claims and to participate in the selection of appropriate venue. Standard access to the court system is considered to be a fundamental shareowner right. Companies should not attempt to restrict the venue for shareowner claims by adopting charter or bylaw provisions that seek to establish an exclusive judicial forum without shareowner approval. Therefore, the SBA generally votes AGAINST management proposals to establish exclusive forum, and votes FOR shareowner proposals requesting that exclusive forum provisions be approved by shareowners. As with many other voting decisions, the SBA will critically examine the company's rationale for limiting shareowners' rights to legal remedy, including choice of venue, and any material harm that may have been caused by related litigation outside its jurisdiction of incorporation.

[1] Claudia H. Allen, "Deleware Corporations—Can Delaware Forum Selection Clauses in Charters or Bylaws Keep Litigation in the Court of Chancery?," April 18. 2011

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# *CORPORATE GOVERNANCE PRINCIPLES*
# & Proxy Voting Guidelines

March 2012

SBA FLORIDA

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**About the State Board of Administration**

The Florida State Board of Administration (SBA) is an agency of Florida state government that provides a variety of investment services to various governmental entities. FRS Trustees are dedicated to ensuring that the SBA invests assets and discharges its duties in accordance with Florida law, guided by strict policies and a code of ethics to ensure integrity, prudent risk management and top-tier performance. The SBA has three Trustees: the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary. All three of the Trustees of the Board are elected statewide to their respective positions as Governor, Chief Financial Officer, and Attorney General. The Board of Trustees appoints six members to serve on the Investment Advisory Council. The Investment Advisory Council provides independent oversight of SBA's funds and major investment responsibilities. The SBA is an investment fiduciary under law, and subject to the stringent fiduciary duties and standards of care defined by the Employee Retirement Income Security Act of 1974 (ERISA), as incorporated into Florida law.

As of December 31, 2011, the net asset value of total funds under SBA management was approximately $150 billion. The FRS Pension Plan provides defined pension benefits to over 1.1 million members. The strong long-term performance of the FRS Pension Plan, the fourth-largest public pension fund in the nation, reflects our commitment to responsible fiscal management. The SBA strives to meet the highest ethical, fiduciary and professional standards while performing its mission, with a continued emphasis on keeping operating and investment management costs as low as possible for the benefit of Florida taxpayers.

We encourage you to review additional information about the SBA and its corporate governance program, as well as the FRS, on our website at www.sbafla.com

**INTRODUCTION**

The Florida State Board of Administration (SBA) manages the fourth largest U.S. pension fund and other non-pension trust funds with assets spanning domestic and international capital markets. Our primary function is to represent the interests of our stakeholders so that they will see fair returns on their investment; therefore we have a clear interest in promoting the success of companies in which we invest. To ensure returns for our shareowners, we adopt internationally recognized governance practices for well-managed public companies. These include independent boards, performance-based executive compensation, accurate accounting and audit practices, transparent board procedures, and policies covering issues such as succession planning and meaningful shareowner participation. Essentially, we address and work with the companies in which we invest to ensure the maximization of long-term shareowner value.

The SBA takes an active role in strengthening corporate governance. Sound corporate governance practices enhance shareowner value and thereby play an important role in achieving our financial objectives as a long-term investor. To implement our corporate governance program, the SBA works with many different organizations, including the Asian Corporate Governance Association (ACGA), the Council of Institutional Investors (CII), the International Corporate Governance Network (ICGN), Institutional Shareholder Services, Inc. (ISS), Glass, Lewis & Co. (GLC), , GovernanceMetrics International (GMI), Manifest, Inc., the Investor Responsibility Research Center (IRRC), Equilar, Inc., , The Conference Board Corporate Governance Center, and the Harvard Law School Shareholder Rights Project.

Although we believe that it is essential to confront corporate boards with poor governance practices, we also recognize the necessity of allowing boards to direct the businesses that they have been entrusted to oversee without excessive interference; therefore, we do not attempt to mandate business strategies for the companies we own. However, to balance our position, we vote "against" any proposal that limits shareowner rights or makes it more difficult for shareowners to have a voice in company practices, as well as certain board structures, poison pills, super-majority requirements, and others.

**CORPORATE GOVERNANCE PRINCIPLES**

The SBA believes that, as a long-term investor, good corporate governance practices serve to protect and enhance our long-term portfolio values.[1] To this end, voting rights should be exercised for the exclusive benefit of Florida Retirement System (FRS) members and their beneficiaries (i.e. as members of the FRS Pension Plan or Investment Plan) as well as other non-pension clients.

The SBA is reliant on its Corporate Governance Principles to direct its activities related to corporate governance and proxy voting. These Principles, in conjunction with other relevant policies, set the parameters for the SBA's shareowner activism and provide a framework for SBA corporate governance initiatives. The SBA's Proxy Voting Guidelines are formulated and revised in accordance with these principles.

In accordance with the Department of Labor (DOL) Interpretive Bulletin §2509.08-2, stock ownership rights, which include proxy votes, participation in corporate bankruptcy proceedings, and shareowner litigation, are financial assets. They must be managed with the same care, skill, prudence, and diligence as any other financial asset. They must be exercised to protect and enhance long-term portfolio value and for the exclusive benefit of pension plan participants and beneficiaries as well as the clients and beneficiaries of other fiduciary accounts. Pursuant to the provisions set forth in the Employment Retirement Income Security Act of 1974, this is generally referred to as the "duty of loyalty" or the "exclusive purpose" rule. Under this rule, fiduciaries, defined as any person who, in part, "exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets" must act solely in the interest of plan participants and beneficiaries in making decisions concerning the management or disposition of plan assets.[2] While the SBA is exempt from most provisions of ERISA, we agree with this treatment of the value of proxy voting rights and follow the standard as a part of our fiduciary duty. Section 215.47(10) of the Florida Statutes encompass the prudent persons standards and fiduciary responsibilities of the SBA and its employees.

Managing stock ownership rights and the proxy vote includes the establishment of written proxy voting guidelines, which must include voting policies on issues likely to be presented, procedures for determining votes that are not covered or which present conflicts of interest for plan sponsor fiduciaries, procedures for ensuring that all shares held on record date are voted, and procedures for documentation of voting records. The following corporate governance principles and proxy voting guidelines are primarily designed to cover publicly traded equity securities. Other investment forms such as privately held equity, limited liability corporations, privately held REITs, etc. are not specifically covered by individual guidelines, although broad application of the principles and guidelines can be used for these more specialized forms of equity investments.

The primary role of shareowners within the corporate governance system is in some ways limited, although critical. Shareowners have the duty to communicate with management and encourage them to align their processes with corporate governance best practices. This means shareowners have two primary obligations: 1) to monitor the performance of the company and 2) to protect their right to act when it is necessary.

A study conducted by NYU's Pollack Center for Law & Business revealed that external and internal governance mechanisms

[1] CFA Centre for Financial Market Integrity, "The Corporate Governance of Listed Companies: A Manual for Investors," 2009.

[2] Lannof, Ian D., "DOL Advisory Opinion 2007-07A." Groom Law Group, February 2008.

are strong complements. The importance of internal governance crucially depends on the extent of external governance and vice versa. In addition, effective corporate governance design relies on a combination of high exposure to the market for corporate control and a high degree of monitoring by shareowners. [3]

In the 1930's, Benjamin Graham and David Dodd succinctly described the agenda for corporate governance activity by stating that shareowners should focus their attention on matters where the interest of the officer and the stockholders may be in conflict. This includes questions about preserving the full integrity and value of the characteristics of ownership appurtenant to shares of common stock. For example, the right to vote may be diluted by a classified board or by dual class capitalization, and the right to transfer the stock to a willing buyer at a mutually agreeable price may be abrogated by the adoption of a poison pill.

Since management and board composition change over time, while shareowners continue their investment, shareowners must ensure that the corporate governance structure of companies will allow them to exercise their ownership rights permanently. Good corporate management is not an excuse or rationale upon which institutional investors may relinquish their ownership rights and responsibilities.

The proxy voting system must be an even playing field. Neither management nor shareowners should be able to dominate or influence voting dynamics. A 2006 article analyzed the corporate governance implications of the decoupling of voting power and economic ownership through methods such as vote trading and equity swaps, methods largely hidden from public view and not captured by current regulation or disclosure rules. This method has been used by finance-savvy activist hedge funds, for example, who have borrowed shares just before the record date in order to better support proposals they favor, reversing the transactions after the record date. The SBA believes that enhanced disclosure rules are critical to reveal hidden control of voting power. [4, 5]

Management needs protection from the market's frequent focus on the short-term in order to concentrate on long-term returns, productivity, and competitiveness. Shareowners need protection from coercive takeover tactics and directors with personal agendas. Ideal governance provisions should provide both sides with adequate protection. They should be designed to give management the flexibility and continuity it needs to make long-term plans, to permit takeover bids in cases where management performance is depressing long-term value, to ensure that management is accountable to shareowners, and to prevent coercive offers that force shareowners to take limited short-term gains.

A study on shareowner activism and corporate governance in the United States found that shareowner opposition has slowed the spread of takeover defenses, such as staggered boards, that require shareowner approval. However, shareowners have failed in their efforts to get companies to roll back takeover defenses and, perhaps more importantly, managers frequently ignore even a majority shareowner vote in favor of a proposal. [6]

**GLOBAL STANDARDS OF CORPORATE GOVERNANCE**

The SBA believes strongly that good corporate governance practices are important to encourage investments in countries and companies in a globalized economy where gaining access to capital markets is increasingly viewed as critical. A comparative analysis of corporate governance in US and international firms shows that the ability of controlling shareowners to extract private benefits is strongly determined by a country's investor protection. Thus, if investor protection is weaker, improvements in firm-level governance will be costlier for the controlling shareowner. [7]

Over the last several years, many countries, international organizations, and prominent institutional investors have developed and implemented international policies on corporate governance and proxy voting issues (e.g., the Organization for Economic Cooperation and Development (OECD), and the International Corporate Governance Network (ICGN)). Many of these promulgated guidelines recognize that each country need not adopt a "one-size-fits-all" code of practice. However, the SBA expects all capital markets to exhibit basic and fundamental structures that include the following:

1. **Corporate Objective**
   The overriding objective of the corporation should be to optimize the returns to its shareowners over time. Where other considerations affect this objective, they should be clearly stated and disclosed. To achieve this objective, the corporation should endeavor to ensure the long-term viability of its business, and to manage effectively its relationship with stakeholders.

2. **Communications & Reporting**
   Corporations should disclose accurate, adequate and timely information, in particular meeting market guidelines where they exist, so as to allow investors to make informed decisions about the acquisition, ownership obligations and rights, and sale of shares. Material developments and foreseeable risk factors, and matters related to corporate governance should be routinely disseminated to shareowners. Shareowners, the board, and management should discuss corporate

[3] Martijn Cremers, K.J., Nair, V., 2003. "Governance Mechanisms and Equity Practices."
[4] Hu, Henry T.C. and Black, Bernard S., "Empty Voting and Hidden (Morphable) Ownership: Taxonomy, Implications, and Reforms". As published in Business Lawyer, Vol. 61, pp. 1011-1070, 2006 Available at SSRN: http://ssrn.com/abstract=887183.
[5] Christoffersen, S.E.K., Geczy, C.C., Musto, D.K., and Reed, A.V. (2006). Vote Trading and Information Aggregation.
[6] Black, B., 1998. "Shareowner Activism and Corporate Governance in the United States."
[7] Aggraval, Reena et al, 2007, "Differences in Governance Practices between US and Foreign Firms: Measurement, Causes, and Consequences", Charles A. Dice Center for Research in Financial Economics, Working Paper 2007-14.

governance issues among them. Where appropriate, these parties should converse with government and regulatory representatives, as well as other concerned bodies, so as to resolve disputes, if possible, through negotiation, mediation, or arbitration. For example, investors should have the right to sponsor resolutions and convene extraordinary meetings. Formal procedures outlining how shareowners can communicate with board members should be implemented at all companies and be clearly disclosed.

3. **Voting Rights**
Corporations' ordinary shares should feature one vote for each share. Corporations should act to ensure the owners' rights to vote and apply this principle to all shareowners regardless of their size.

4. **Corporate Boards**
The Board of Directors, or Supervisory Board, as an entity, and each of its members, as individuals, is a fiduciary for all shareowners, and they should be accountable to the shareowner body as a whole. Each member should stand for election on a regular basis, preferably with annual election cycles. Corporations should disclose upon appointment to the board, and thereafter in each annual report or proxy statement, information on the identities, core competencies, professional or other backgrounds, factors affecting independence, other commitments, and overall qualifications of board members and nominees so as to enable investors to weigh the value that they add to the company. Information on the appointment procedure should also be disclosed annually. Boards should include a sufficient number of independent, non-executive members with appropriate qualifications. Responsibilities should include monitoring and contributing effectively to the strategy and performance of management, staffing key committees of the board, and influencing the conduct of the board as a whole. Accordingly, independent non-executives should comprise no fewer than three (3) members and as much as a substantial majority. Audit, Compensation and Nomination committees should be composed entirely of independent non-executives.

5. **Executive & Director Compensation**
Remuneration of corporate directors or supervisory board members and key executives should be aligned with the interests of shareowners. Corporations should disclose in each annual report or proxy statement the board's policies on remuneration and, preferably, the remuneration of individual board members and top executives; so that shareowners can judge whether corporate pay policies and practices meet this standard. Broad-based employee share ownership plans or other profit-sharing programs are effective market mechanisms that promote employee participation.

6. **Strategic Planning**
Major strategic modifications to the core business of a corporation should not be made without prior shareowner approval of the proposed modification. Equally, major corporate changes that, in substance or effect, materially dilute the equity or erode the economic interests or share ownership rights of existing shareowners should not be made without prior shareowner approval of the proposed change. Shareowners should be given sufficient information about any such proposal early enough to allow them to make an informed judgment and exercise their voting rights.

**ACTIVE STRATEGIES & COMPANY ENGAGEMENT**

The objective of SBA corporate governance engagement is to improve the governance structures at companies in which the SBA owns significant shares in order to enhance the value of SBA equity holdings.

A study on the evolution of shareowner activism in the United States affirms that activism by investors has increased considerably since the mid-1980s due to the involvement of public pension funds and institutional shareowners. The study identifies the potential to enhance value of investments as the main motive for active participation in the monitoring of corporations. However, as shareowner activism entails concentrated costs and widely disbursed benefits, only investors with large positions are likely to obtain a large enough return on their investment to justify the costs.[8]

The two primary obligations of shareowners are to monitor the performance of the companies and to protect their right to act when necessary. The SBA has neither the time nor resources to micromanage companies in which it holds publicly traded stock. Furthermore, the legal duties of care and loyalty rest with the corporate Board of Directors, not with the shareowners. For these reasons, the SBA views its role as one of fostering improved management and accountability within the companies in which we own shares. Other recent SBA corporate governance activities have included dealing with conflicts of interest within organizations with which we do business.

Department of Labor (DOL) Interpretive Bulletin §2509.08 states that voting proxies is a fiduciary responsibility and that proxies should be treated like any other financial asset, executed in the best interest of beneficiaries in accordance with written guidelines.

Additionally, Florida Law may prohibit investment in companies or mandate reporting on certain investments due to geopolitical, ethnic, religious, or other factors. Compliance with these laws and any related reporting requirements have

[8] Gillan, Stuart L. and Laura T. Starks, 2007, "The Evolution of Shareowner Activism in the United States", *Journal of Applied Corporate Finance*, Volume 19, Number 1, Winter 2007, Published by Morgan Stanley.

similarities to corporate governance issues and are consolidated organizationally.

Consistent with prudent and responsible investment policy, all or some of the following measures may be instituted when a corporation is found by the SBA to be under-performing market indices or in need of corporate governance reform:

- The SBA will discuss the corporate governance deficiencies with a representative and/or the Board of Directors. Deficiencies may occur in the form of policies or actions, and often result from the failure to adopt policies that sufficiently protect shareowner assets or rights. The SBA may request to be informed of the progress in ameliorating such deficiencies.

- Under SEC Rule 14(a) 8 [9], shareowner proposals may be submitted to companies with identified performance deficiencies. Shareowners proposals will be used to place significant issues on a company's meeting ballot in order to allow all shareowners to approve or disapprove of significant issues and voice the collective displeasure of company owners.

- Any other strategies to achieve desired corporate governance improvements as necessary.

In addition to overseeing the corporate governance of companies in which we invest, the SBA must also govern the accessibility of our own records by these companies. As a beneficial owner of over 10,000 publicly traded companies, the SBA has elected to be an objecting beneficial owner, or an "OBO." By being an OBO, the SBA does not give permission to a financial intermediary to release our name and address to public companies that we are invested in. This keeps our holdings or trading strategies confidential, and allows us to avoid unwanted solicitations.

Recent developments have led many to believe that the distinction between OBO and non-objecting beneficial owners or "NOBO's" should be eliminated. However, the SEC is likely to be cautious in seeking to change the current framework in significant ways. [10] Strong opponents to an elimination of OBO and NOBO distinction are brokers and banks, who have a large incentive to ward off this change due to fee income derived from forwarding proxy materials.

While we feel that shareowner communication can be important, a number of steps must be taken to address the distinction between OBO and NOBO companies and to respect the privacy of beneficial owners involved. Proposals that eliminate the possibility of anonymity completely are not feasible. It is necessary for any changes made to the current system to accommodate the strong privacy interests of current OBO firms, such as the SBA.

[9] Rule 14a-8 is an SEC rulemaking promulgated under the Securities Exchange Act of 1934 and offers a set of procedural requirements governing how and when shareowners may submit resolutions for inclusion in a corporation s proxy statement.

[10] Beller, Alan L. and Janet L. Fisher. "The OBO/NOBO Distinction in Beneficial Ownership: Implications for Shareowner Communications and Voting." Council of Institutional Investors. February 2010.

## II. PROXY VOTING GUIDELINES

**Empirical Basis for Proxy Voting Guidelines**
The SBA's voting guidelines are based on rigorous empirical research, industry studies, investment surveys, and other general corporate finance literature. We believe that sound proxy voting policies should be based on both market experience and balanced academic and industry studies, which aid in the application of specific policy criteria, quantitative thresholds, and other qualitative metrics. Empirical citations should provide evaluation of specific items over long time frames, in excess of 3 years. Studies should also be extensive in scope and analyze companies of various market capitalizations across U.S. and foreign markets.

**Disclosure of Proxy Voting Decisions**
The SBA discloses all proxy voting decisions once they have been made, approximately seven to 10 calendar days prior to the date of the shareowner meeting. Disclosing proxy votes prior to the meeting date improves the transparency of our voting decisions and supports widespread public disclosure of SBA investment decisions. Disclosing proxy votes in advance of their effective dates will fully emphasize the SBA's position on proper corporate governance practices. Historical proxy votes are also archived for a period of five years and available electronically on the SBA's website.[11]

**Proxy Voting and Securities Lending**
The SBA participates in securities lending in order to enhance the return on its investment portfolios. In the process of lending securities, the legal rights attached to those shares are transferred to the borrower of the securities during the period that the securities are on loan. As a result, the SBA's right to exercise proxy voting on loaned securities is forfeited unless those affected shares have been recalled from the borrower in a timely manner (i.e. on, or prior to, the share's record date). The SBA has a fiduciary duty to exercise its right to vote proxies and to recall shares on loan when it is in the best interest of our beneficiaries. The ability to vote in corporate meetings is an asset of the fund which needs to be weighed against the incremental returns of the securities lending program.

Although the SBA shall reserve the right to recall the shares on a timely basis prior to the record date for the purpose of exercising voting rights for domestic as well as international securities, the circumstances required to recall loaned securities are expected to be atypical. Circumstances that lead the SBA to recall shares include, but are not limited to, occasions when there are significant voting items on the ballot such as mergers or proxy contests or instances when the SBA has actively pursued coordinated efforts to reform the company's governance practices, such as submission of shareholder proposals or conducting a detailed engagement. In each case, the direct monetary impact of recalled shares will be considered and weighed against the discernible benefits of recalling shares to exercise voting rights. The SBA recognizes that it may not be possible to determine, prior to a record date, whether or not shares warrant recall. Further, the potential operational and investment consequences of recall upon the securities lending program's collateral investment pool will be taken into consideration. In order to determine if securities will be recalled, individual circumstances shall be evaluated on a case-by-case basis. One situation in which securities lending could conflict with maximization of shareowner value may occur in the case of special meetings with the right to convert shares at a premium. This can occur in the case of a Special Purpose Acquisition Company (SPAC), with investors being allowed the alternative of a conversion of shares to cash. If shares are on loan at the time of the special meeting, the ability to exercise conversion rights for those shares is lost.

The SBA is a long-term investor. Certain external investment managers are authorized to use strategies that include shorting in portfolios managed on our behalf. In the potential event that a combination of securities lending and short selling activity led to voting rights at a company meeting despite a net negative economic exposure, the SBA would view such conditions as temporary and cast any votes in the economic well being of the firm for the long term. Under no circumstance would the SBA cast votes contrary to shareholder value due to the use of short selling or securities lending within its portfolios.

The SBA opposes the practice of borrowing shares for the primary purpose of exerting influence or gaining control of a company without sharing the risks of ownership. The SBA views an attempt by any entity to deliberately distort the voting outcome at a shareholders' meeting to be detrimental to the proper functioning of equity capital markets.

The SBA supports enhanced disclosure in voting reports in the form of votes cast, number of shares voted, and number of shares on loan over the record date. This enhanced transparency allows beneficiaries and recipients of voting reports to have a more complete understanding of the stewardship of their assets. The number of shares voted or on loan for corporate meetings is relevant information for plan participants, mutual fund investors and retail clients seeking to determine how well the governance of invested companies is monitored.

In the rare event that the SBA received a proxy ballot to vote shares that were on loan as of the record date, we would vote such shares in the best interest of the long-term firm value and our beneficiaries. Shares on loan are only out of the SBA's legal possession on a temporary basis, and we will act as a long-term investor in any voting action.

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[11] Registered investment advisors are required pursuant to Rule 30(b)1-4 of the Investment Company Act of 1940, known as the SEC s rule "N-PX," to report their proxy votes by August 31st of each year, covering voting decisions made over the prior year ending in June. Although the SBA is not legally required to file N-PX reports with the SEC, it does make identical reporting publicly available at www.sbafla.com, including real time voting decisions prior to shareowner meetings.

**BOARD OF DIRECTORS**

Director elections are considered to be one of the most important voting decisions that shareowners make, especially because shareowners are only given the opportunity to review their companies' operations once a year at the AGM. Thus, if detailed information on boards or nominees is available, shareowners should scrutinize it closely. Directors function as the representatives of shareowners throughout the year and are therefore a crucial avenue of ongoing influence on management.

Levels of disclosure regarding directors vary widely. In some countries, such as the United States, United Kingdom, Canada, and Australia, companies publish detailed information such as director biographies, share ownership, and related information that aids shareowners in determining the level of director independence. In many other countries, the only information available on directors is their names, while still other countries disclose no information at all. In cases where detailed information about directors is not available, it would be counterproductive to vote against directors on the basis of a lack of information. Opposition to specific nominees or boards should be supported by specific problems or concerns.

The effectiveness of the board is a direct function of its composition and structure. In developed markets including the United States, Canada, United Kingdom and Australia, the stringent board independence standards mandated by relevant market listing rules have enabled shareowners to raise the bar of "best practices" for board independence. Many institutions and even members of the corporate community, such as the Business Roundtable, National Association of Corporate Directors (NACD), and a blue ribbon panel of the Conference Board, now advocate that a substantial majority of directors be independent. As a result, a two-thirds threshold has become commonplace in shareowner proposals.

While numerous studies have been conducted on the benefits of board independence, much evidence reveals that board independence is desirable and has a positive impact on institutional investors' perception of a corporation. A survey for Russell Reynolds Associates found that institutional investors are more closely examining the composition of boards. Over a majority of the survey participants stated that family ties on the board and boards with dismissed CEOs or other dismissed executives are significant concerns in addition to director interlocks[12] and board members serving on multiple boards.

Fortunately, corporate boards of publicly-listed companies in developed markets generally provide for a high level of independence. By contrast, many of their counterparts in emerging markets in Asia, Latin America, the Middle East, etc. exhibit very low independence structure coupled with poor board transparency. Boards in emerging markets, have traditionally been, and in some cases, continue to be dominated by families. Specifically in Asia, these family-owned companies have a relatively low concentration of independent non-executive directors. Problems arise due to the controlling shareowners' power to nominate friends, former colleagues, or relatives to the board regardless of their experience or qualifications.[13] These boards find themselves at a significant disadvantage when it comes to attracting foreign institutional investors. Family-dominated boards need reform as it would help improve a company's credit status, which would enable it secure cheaper borrowing rates on debt financing. A greater level of institutional participation would also foster longer-term perspective to the market, prompt improvements in corporate governance and even help entice more international private equity investment into the country. It is believed that many international constituents have been reluctant to pursue activity in the Middle East because many companies do not provide for a reasonable level of due diligence during investment, partnership, or exit opportunities.[14]

Boards without adequate independence from management may suffer from conflicts of interest and impaired judgment in their decision-making. In addition to poor transparency, directors with ties to management may be perceived to be less willing and able to effectively evaluate and scrutinize company strategy and performance. Another factor investors may examine when evaluating a director's performance is their relationship to a company's competitors within the same industry or across similar business segments.

***Election of Directors: CASE-BY-CASE***

The SBA generally votes FOR directors up for election. However, after taking into consideration unique country-specific practices and disclosure standards[15], the SBA may vote AGAINST (i.e., "withhold" support for) director nominees for one or more of the following reasons:

- Lack of stock ownership.
- Poor attendance at meetings (e.g., if less than 75 percent attendance rate).
- Whether they are inside or outside of the company (i.e., director independence). The SBA strongly disfavors board representation that does not meet a minimum two-thirds independence threshold, and will routinely withhold support from individual director nominees who are not independent (excluding the CEO) in those circumstances where the full

[12] Board "interlocks" are created when two directors who are considered inside directors on their primary company s board, also serve as an outside, or independent, director on the other s board of directors. A typical example includes two CEOs serving as directors on each other s board. Also see Devos, Erik, Prevost, Andrew, and Puthenpurackal, John, "Are Interlocked Directors Effective Monitors?"

[13] Asia Pacific Office of the CFA Institute Centre for Financial Market Integrity. "Independent Non-Executive Directors, A Search for True Independence in Asia." 2010.

[14] Saigol, Lina, "Family-owned Businesses Need to Reform." FT Report – Corporate Finance 2008, May 2008.

[15] For instance, Italy amended its "Consolidated Financial Act" to mandate that Italian issuers reserve a certain number of board seats for candidates presented by minority shareowners. This mandate affects Board of Director elections, Supervisory Board elections, and Board of Statutory Auditor elections. *See,* "Italian Issuers- Guidelines for the election of the Board of Directors (or Supervisory Board) or Board of Statutory Auditors," Trevisan & Associati February 19, 2009 *available at* http://www.trevisanlaw.it/en_mask.html?5 (last visited March 2, 2009).

board comprises less than 50 percent independence levels.

- Negligence in board committee performance.
- Ignored a material shareowner proposal that was either approved by a majority of votes cast or approved by a majority of the shares outstanding.
- Over boarding – the SBA will likely withhold support from a director who serves on more than 3 outside boards, which the SBA considers as over boarded, and who is employed in a full-time position. Directors with significant outside responsibilities (e.g. is CEO of a separate company) sitting on more than one external board may also have support withheld. [16]
- Poor performance across all company boards upon which the individual serves as a director.

According to a study on corporate governance performance of U.S. industrial firms between 1989 and 1995, empirical evidence suggests that busy outsider directors are associated with weak corporate governance. When a majority of outside directors serve on three or more boards, firms exhibit lower market-to-book ratios, as well as weaker operating profitability. When a majority of outside directors are over boarded, the sensitivity of CEO turnover to performance is significantly lower than when a majority of outside directors are not busy. Investors react positively to the departure of over boarded directors, while firms, whose directors acquire an additional board seat and become over boarded, end up experiencing negative abnormal returns. [17] In light of such findings, the SBA generally limits directorships to 3 boards if a director is employed in a full-time position and one board for directors who serve as CEO of a separate company.

The SBA believes that director performance is paramount to sound corporate governance. It is important that directors, as shareowner representatives in the boardroom, not only be independent of management but also effectively exercise their fiduciary duty through good performance. A paper by the Global Corporate Governance Forum recommends using board evaluations as open communication to focus on inadequacies, identify strategic priorities and become more efficient through the review of policies and procedures [GCGF, Board Performance Evaluation]. Evaluations can help uncover breakdowns in committee functioning and responsibility. The SBA takes into account the performance of a director across all boards on which the director serves. Underperformance, or exceptional performance, on any given board provides a more complete depiction of an individual's capabilities as director.

As an example, evaluations can be particularly helpful in assessing audit committee performance as the audit committee is responsible for independent[18] oversight of the company's financial statements and, in the absence of a separate risk committee, is also often responsible for risk oversight. Regular self-assessments are critical to a productive audit committee. The SBA will consider the audit committee's performance, especially as it relates to oversight and risk management, when voting on individual committee members. Evidence of poor audit committee performance are financial restatements, including as a result of option backdating, unremediated material weaknesses, and attempts to limit auditor liability through auditor engagement contracts.

Shareowners can take issue with under-performing directors through "vote no" campaigns. An empirical study found that "vote no" campaigns are an effective tool to voice concerns with a particular director, and ultimately pressure the company to take action. The study specifically finds a forced CEO turnover rate of 25 percent in firms targeted with "vote no" campaigns.[19] This underscores that performance is an essential component of governance and should be considered when evaluating election of director proposals. Where a clear pattern of underperformance exists, even external to the company in question, the SBA will review that director's qualification to serve on the board on a case-by-case basis.

The SBA generally will not consider age as a rationale for withholding votes. Length of service on a board is sometimes a factor in determining independence for a director, but is not used to justify a withhold vote except in rare instances with unusual circumstances.

***Election of Directors (Japan): CASE-BY-CASE***

Japanese boards are dominated by insiders, and the few outside directors are generally affiliated outsiders from a main bank, parent company or business partner. While independent directors are still very rare in Japan, the SBA believes a shift to independent directors (even on an incremental basis) would increase the degree of company oversight and shareowner representation. The SBA may vote against the chairman and additional nominees unless a substantial portion of the board is independent. Additionally, attention should be focused on the independence of the statutory auditors, who should fulfill the oversight function at Japanese companies. The SBA will vote against directors in cases of scandal or other malfeasance, or egregiously poor performance.

However, since 2003, Japanese companies have been given the option of switching to a U.S.-style "board-with-committees" structure. Such companies abolish their board of statutory auditors, and must create audit, compensation, and nomination

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[16] Neil Roland, "Directors at troubled companies overbooked, research firm claims" *Financial Week* (February 25, 2009) *available at* http://www.financialweek.com/apps/pbcs.dll/article?AID=/20090223/REG/902239979/1038/EXCLUSIVES (last visited February 25, 2008) (this article gives examples of overbaording problems at struggling U.S. financial institutions).

[17] Fich, Eliezer M. and Anil Shivdasani, 2006, "Are Busy Boards Effective Monitors?," *The Journal of Finance*, Vol. 61, No. 2, pp. 689-724 (36), Blackwell Publishing.

[18] SEC Rule 10A-3 under the Exchange Act mandates that stock exchanges adopt listing standards that require that each member of the audit committee of a listed company has (1) not received compensation from the issuer other than for board services and (2) is not an "affiliated person" of the issuer that either controls, is controlled by, or is under common control with the issuer."

[19] Diane Del Guercio, Laura Seery, and Tracie Woidtke, "Do Boards Pay Attention when Institutional Investor Activists Just Vote No, "*available at* http://ssrn.com/abstract=575242.

committees of at least three directors each. A majority of committee members must be outside directors. In order to separate responsibility for management execution and oversight, these companies must also create a board of executive officers, whose members are appointed by the board of directors. In these cases, the role of the outside directors becomes much more important, and the SBA believes that the independence of the outsiders is critical to effective corporate governance under the new system. Therefore, the SBA will vote against outside director nominees at such companies where we believe that the nominees cannot fulfill the role of independent monitor of the company's activities.

Additionally, the SBA may vote against the reelection of representative directors (including President and Chairman) in cases where a company implements a poison pill or similar antitakeover measure pursuant to a board resolution, giving shareowners no opportunity to vote on the matter. The SBA may vote against the chairman of the board or President regardless of their individual representative roles. Such decisions will be made on a case-by-case basis, where the SBA will oppose nominees to indicate a vote of "no-confidence".

With changes mandated by the Corporate Law in 2006, Japanese companies must disclose the participation of outside directors and statutory auditors at meetings of the board of directors (and in the case of statutory auditors, meetings of the board of statutory auditors as well). Most companies interpret this as a call to disclose the number of meetings attended. Meanwhile, as the number of outsiders in Japan continues to increase, we are seeing some cases of low attendance rates, apparently caused by scheduling conflicts.

Pursuant to the greater disclosure, the SBA has adopted the same policy used at U.S. companies: namely, generally opposing the reelection of directors who fail to attend at least 75 percent of board meetings, unless the company discloses a legitimate reason for the poor attendance. The SBA views attendance at board meetings as one of the fundamental responsibilities of a board member, and that all directors and statutory auditors should attend meetings regularly to review the company's performance and to ensure the protection of shareowner interests. Japanese laws and regulations require public companies to disclose only outside director and external statutory auditor attendance at board meetings, whereas the attendance record of insiders is not required by law to be disclosed. Japanese companies typically hold board meetings on a monthly basis, if not more frequently, and outside board members comprise a small minority on Japanese boards.

The SBA applies the same approach to statutory auditors because they will not be able to properly fulfill their oversight function if they fail to attend meetings of the board of directors and board of statutory auditors. Attendance via webcast or teleconference will be deemed equivalent to attendance in person.

Increasing demand for independence on Japanese boards from sources including the Japan Pension Fund Association, the Japan Association of Corporate Directors, the Asian Corporate Governance Association, and the Financial Services Agency, have requested that exchanges in Japan revisit their independence policies. Until now there has been no definition of 'independence' for directors or statutory auditors and affiliates often serve as so-called 'external' directors and statutory auditors. This traditional lack of true independence has led critics and investors to question whether there are sufficient systems in place in Japan to serve as a check on management. Amidst this pressure, the Tokyo Stock Exchange, by amending its listing rules, has implemented a policy requiring all listed companies to appoint at least one independent director or statutory auditor to either board.

Most two-tier Japanese boards are dominated by executives of the company or of a major subsidiary and, though largely responsible for day-to-day management, have few or no independent representatives able to represent shareholders through more supervisory roles. The SBA votes against the election of insiders or affiliates in order to satisfy the independence threshold we believe is appropriate. For companies having adopted a two-tier board structure, at least two members of the board should be independent outside directors. However, we will always review the board structure on a case-by-case basis, and may vote differently based on whether the company has a unitary board with subcommittees, a statutory audit board, or two-tiered board structure.

***Elect a Corporation as a Director (France): CASE-BY-CASE***
The SBA considers whether the corporation, which is proposed to act as a director, will represent the interests of all shareowners.

***Limit Director Tenure: AGAINST***
The SBA votes AGAINST proposals to limit the tenure of outside directors. While we agree, in principles that new outside directors often bring in fresh ideas that benefit shareowners we do not believe this requirement is an appropriate way to achieve that goal. It is an artificial and arbitrary imposition on the board, and it could conceivably harm shareowners' interests by forcing some experienced and knowledgeable directors from serving on the board.

***Age Limits: AGAINST***
The SBA votes AGAINST shareowner or management proposals to limit the tenure of outside directors through mandatory retirement ages. Similar to tenure limits, rather than imposing a narrow rule on director age limits, shareowners gain much more by retaining the ability to evaluate and cast their vote on all director nominees once a year and by encouraging companies to perform periodic director evaluations.

***Change or Approve Size of Board: CASE-BY-CASE***
There have been a growing number of management proposals that intend to limit a shareowner's ability to alter the size of the board, while at the same time, allowing management to increase or decrease the size of the board at its discretion. Corporate

management argues that the purpose of such proposals is to prevent a dominant shareowner from taking control of the board by drastically increasing the number of directors and electing its own nominees to fill the newly created vacancies. Other scenarios may include a board's downsizing in response to business changes or acquisitions. The SBA generally supports such proposals if we feel management is not coercive.

***Classified Board: AGAINST***
A classified, or staggered, board is one in which directors are divided into three "classes" with each director serving three-year terms. All directors on a non-classified board serve one-year terms and the entire board is re-elected each year.
Studies performed by SEC economists and by academics support the view that classified boards are contrary to shareowner interests, showing negative effects on share value for companies that adopt classified boards. For example, the SEC studied the impact of 649 antitakeover proposals submitted between 1979 and 1985. The proposals consisted of fair price provisions, institution of supermajority vote requirements, classified board proposals, and authorization of blank check preferred stock. Stocks within the group showed an average loss in value of 1.31 percent. The study also found that the proposals were most harmful when implemented at firms that have higher insider and lower institutional shareholdings. While classified board proponents cite stability, independence, and long-term strategic risk taking as justification for staggered boards, recent research has shown little evidence of such benefits.[20]

A 2002 academic study covering hostile bids between 1996 and 2000 showed that classified boards nearly doubled the odds of a target remaining independent. However, the findings revealed that a staggered board structure did not provide any countervailing benefits in terms of higher acquisition premiums. In fact, for the period covered, it resulted in the loss of $8.3 billion for target shareowners by impeding value-creating transactions without any offsetting increases in alternative transaction or stand-alone target returns.[21] Additional studies reveal that staggered boards bring about, and not merely reflect, reduction in firm value, especially for companies that establish classified boards in the corporate charter, which shareowners cannot amend, as opposed to such boards established in the company's bylaws, which shareowners can amend.[22] Finally, a 2001 study found that between 1990 and 1999, firms with weak shareowner rights, including classified board structures, exhibited lower net profit margins and sales growth and made more capital expenditures and acquisitions than firms with a high degree of shareowner rights.[23]

A study on the relationship between board classification, takeover activity, and transaction outcomes for a panel of firms between 1990 and 2002 finds that board classification does not have an impact on the likelihood that a firm, once targeted, is ultimately acquired. However, the study reveals that bidding shareowner returns are 2.7 percent lower when bids involve classified targets.[24]

Furthermore, empirical evidence supports the belief that staggered boards, by entrenching inefficient managers, may motivate managers to adopt a lower level of debt, thereby avoiding disciplinary mechanisms associated with leverage. According to a study, results show that staggered boards are likely to bring about, and not to merely reflect, lower leverage. At the same time, the study finds that there appears to be no significant impact on firm value as a result of excess leverage.[25]

The SBA opposes classified boards and their provisions because we believe that annual accountability will ultimately lead to increased corporate performance. Classified boards also decrease corporate accountability by protecting directors from election on an annual basis. Alternatively, the SBA supports changing from a staggered board structure to annual elections for all directors.

***Adopt Cumulative Voting: FOR***
Cumulative voting guarantees that shareowners of a certain size will be able to elect at least one of their candidates to the board of directors, even if the candidate does not win a majority vote. In contrast, only majority shareowners are guaranteed board representation at companies without cumulative voting. The opposite is also true when cumulative voting is in effect. A majority position, either alone or as a bloc of votes, may not always be sufficient to control the board, while a majority position is always guaranteed board control at companies without cumulative voting. The difference has to do with the way votes are counted and distributed in director elections.

At companies with cumulative voting, the total number of votes each shareowner may cast is determined by multiplying the number of shares owned by the number of board slots up for election. Shareowners may cast all their votes for one nominee, for a combination of nominees or may spread their votes across the entire board. This means that shareowners of a certain size will always be assured of having at least one of their choices for a director elected to the board. For example, consider a company with a 10-member board and 500 shares outstanding. The total number of votes that may be cast is 10 x 500, or 5,000. In this case, a shareowner with 51 shares (10.2 percent of the shares outstanding) would be guaranteed one board seat.

The SBA will make certain exceptions on proposals to adopt cumulative voting in light of the introduction of proxy access and majority voting reforms that directly address the voting process.

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20 Faleye, Olubunmi, "Classified Boards, Stability, and Strategic Risk Taking." Financial Analysts Journal, Volume 65, No. 1, 2009.
[21] Bebchuk, Lucian Arye, John C. Coates IV, and Guhan Subramanian, "The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, & Policy." National Bureau of Economic Research Working Paper No. W8974, May 2002.
[22] Bebchuk, Lucian Arye and Cohen, Alma, "The Costs of Entrenched Boards." Journal of Financial Economics, Vol. 78, pp. 409-433, 2005.
[23] Gompers, Paul A., Joy L. Ishii, and Andrew Metrick, "Corporate Governance and Equity Prices." National Bureau of Economic Research Working Paper No. W8449, August 2001.
[24] Bates, Thomas W., David A. Becher and Michael L. Lemmon, 2007, "Board Classification and Managerial Entrenchment from the Market for Corporate Control", electronic copy available at: http://ssrn.com/abstract=923408.
[25] Jiraporn, Pornsit and Yixin Liu, 2008, "Capital Structure, Staggered Boards, and Firm Value," Financial Analyst Journal, Volume 64, Number 1.

As an alternative for cumulative voting, a majority vote standard ensures board accountability in uncontested elections. Boards elected under such a majority vote structure are sufficiently accountable to shareowners, as this standard has emerged in the last few years as a catalyst to make director elections meaningful rather than merely symbolic. Although majority voting is meaningful in uncontested elections, it can potentially serve as an anti-takeover mechanism in contested elections. Cumulative voting, on the other hand, is meaningful primarily in contested elections.

The SBA may also vote against proposals to adopt cumulative voting if the company has adopted true majority voting (not a resignation policy), as well as proxy access or a similar structure that proactively encourages shareowners to nominate directors to the company's ballot.

***Director Indemnification: CASE-BY-CASE and in accordance with State Laws***
Indemnification literally means "to make whole." When a corporation indemnifies its directors and officers it means the corporation promises to reimburse them for certain legal expenses, damages and judgments incurred as a result of lawsuits relating to their corporate actions. In effect, the corporation becomes the insurer for its officers and directors. The corporation then purchases insurance to cover its own risk. The vote will be in favor if the damage was caused by violations of the duty of care provided that a "good faith" standard was satisfied. In addition, votes will be cast for increased indemnification proposals where a director's defense was unsuccessful, unless there is a final adjudication that the director acted in bad faith and not for a purpose that he or she reasonably believed to be in the best interest of the company.

Conversely, the SBA votes AGAINST such proposals if coverage expands beyond mere legal expenses and to acts, such as negligence, that are more serious violations of fiduciary obligation than carelessness is, or for violating the duty of care.

State corporation statutes govern whether a corporation may indemnify a corporate director or corporate officer in a particular instance. For instance, Section 607.0850 of the Florida Statues regulates indemnification of corporate directors by Florida corporations. Many states model their indemnification statutes on the Model Business Corporation Act or the Revised Model Business Corporation Act.

***Director Liability: CASE-BY-CASE***
Liability means a director's or officer's personal financial assets are at risk if the individual loses a lawsuit that results in a financial reward or damages to the plaintiffs. Most corporations that indemnify their officers and directors also limit or eliminate the personal liability of the individuals.

The SBA votes AGAINST proposals to limit or eliminate liability for monetary damages of directors and officers for violating the duty of care. The SBA votes FOR liability proposals provided such expanded coverage is for cases where a director's or officer's legal defenses were unsuccessful because either the director was found to have acted in good faith and in a manner that he/she reasonably believed was in the best interests of the company or if the director's legal expenses would be covered.

***Establish/Amend Nominee Qualifications: CASE-BY-CASE***
The SBA evaluates proposals that establish or amend director qualifications on a case-by-case basis. Votes should be based on how reasonable the criteria are and to what degree that they may preclude dissident nominees from joining the board.

***Require Two or More Nominees per Board Seat: AGAINST***
The SBA opposes shareowner proposals requiring two candidates per board seat.

***Separate Chairman & Chief Executive Officer (CEO): CASE-BY-CASE***
The SBA believes that separating the positions of Chairman of the Board and CEO may improve the decision-making process at firms with records of significant underperformance when compared to market and peer group benchmarks. While there are many instances where executives and boards perform well while simultaneously serving as Chairman and CEO, recent studies find that the increase in separation of chairman and CEO positions at US companies from 2000-2004 were driven significantly by monitoring needs, and not only advisory needs. The same study indicates that financial restatements are received more favorably in firms that have a separation of leadership than in firms that do not, suggesting potential value effects of the decision to separate the chairman and CEO positions.[26]

Separating the duties of Chairman and Chief Executive Officer is a necessity when dealing with the issue of CEO succession planning. Research released in August, 2009 by The Conference Board shows that responsibility for a succession plan should be passed to a standing committee within the Board of Directors. However, The Conference Board reports that "an alarming 51 percent of corporate secretaries surveyed in 2008 reported their organizations do not rely on a detailed succession plan for C-suite executives."[27] This is particularly disturbing when taking into account the costs of these increased executive turnovers. Faulty integration of a new senior manager can cost an organization 10 to 20 times the executive's salary in opportunity cost. In order for succession plans to be effective, they should be headed by an independent board chair or lead director; otherwise, the succession

[26] Grinstein, Yaniv and Valles Arellano, Yearim, "Separating the CEO from the Chairman Position: Determinants and Changes after the New Corporate Governance Regulation." March 2008.
[27] Tonello, Matteo, John C. Wilcox, and June Eichbaum, "The Role of the Board in Turbulent Times… CEO Succession Planning." The Corporate Board, August 2009.

planning process may become politicized and possibly cause harm to the organization's cohesiveness and strategic focus. The use of an independent leader will allow the succession committee to implement internal and external transparency, while simultaneously decreasing the risk of instability when the company inevitably faces turnover.

Further evidence supporting the separation of Chairman and CEO was provided by Booz Allen's annual CEO succession study.[28] The study concluded that "Nonchairman [sic] CEOs are now the best performers," with non-chairmen in North America producing shareowner returns three times as high as those of individuals serving as CEO/chairman. In addition, a 2006 Moody's study cited the increased effectiveness of an independent chair or lead director, stating that "the arguments against independent board leadership are outweighed by advantages offered by clarity of accountability and the strengthened ability of independent directors to respond quickly in a crisis." [29] Moreover, investors benefit when the role of chairman is not held by the former CEO. The presence of the former CEO as chairman can have the effect of insulating the current CEO from performance concerns. One study found that in 2006, all of the long-serving underperforming CEOs in North America who departed their companies either held the combined title of CEO/Chairman or served under a chairman who was a former CEO.[30]

In 2012, an influential group of current and former non-executive chairman of boards of directors developed a model policy statement, advocating for the separation of CEO and Chair positions, and recommending all boards adopt the statement's language into their corporate governance policies.[31] The policy statement, by default, supports the creation of an independent chair whenever there is CEO succession and a leadership change at the firm. The policy statement reads, "The Board believes that having a separate, independent director to serve as Chair of the Board assists the Board by providing clear, independent Board leadership. Therefore, it is expected that the Board will be chaired by an independent director. This principle will guide the Board's approach to succession planning and succession decisions. If the Board determines that special circumstances require the roles of Chair and Chief Executive Officer to be combined, the independent directors of the Board shall designate a Lead Independent Director who shall serve in such capacity until such time as a new independent Chair is appointed. In this event, the Board shall provide an explanation of its decision to shareholders."

As a medium between an Independent Chair and the CEO serving as Chair, the presence of an Executive Chair has risen. As defined in Annalisa Barrett's article in the Corporate Library, "an Executive Chair leads the Board of Directors as an employee of the company, but does not simultaneously hold the title of CEO."[32] The main advantage of having an Executive Chair is that due to their current employment in another area of the company, this person may be able to contribute additional institutional knowledge and is likely to display a strong commitment to the company's success. However, when dealing with an internal Executive Chair one must beware of the Chair allowing their personal interests to reign supreme over those of other shareholders. Additionally concerning is the excessive level of total pay that these Executive Chairs receive, with some of these employees receiving in excess of $10 million.

The SBA generally votes FOR shareowner proposals asking that the Chairman and CEO positions be separated, i.e., an independent Chairman who is not employed by the company. Unless the company has a strong countervailing governance structure, including a designated lead director who is appointed from the ranks of the independent board members and who has the authority to develop and set the agenda for meetings and to lead sessions outside the presence of an insider Chair, resolutions to separate the Chairman and CEO positions are in the best interest of shareowners.

***Require Independent Board Chairman: CASE-BY-CASE***

For several years, there has been ongoing discussion over the merits of a separate and independent board chair versus a combined or non-independent chairman/CEO structure. While the latter has been a prevalent practice among US companies for many years, some investors argue that the combined role limits accountability and is indicative of a poor governance structure.

This lack of a consensus opinion on the matter has led to myriad different structures, including:

Separate and independent chair/CEO
Combined chair/CEO
Combined chair/CEO with an independent lead director
Combined chair/CEO with a presiding director
Executive chair/CEO with an independent lead director

Each structure has its advocates and opponents; however, from a governance perspective, it appears that the majority of investors prefer an independent chair or an independent lead director with a well-defined role in managing the board. Similar to our approach on proposals to separate chairman and CEO positions, the SBA generally supports proposals requiring the position of chairman to be filled by an independent director unless there are compelling reasons to oppose the proposal, such as a strong countervailing governance structure. This should include:

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[28] Lucier, Chuck, Paul Kocourek, and Rolf Habbel, "CEO Succession 2005: The Crest of the Wave." Strategy+Business, May 2006.
[29] Taub, Stephen, "CEO as Chairman Still the Rule in US." CFO.com, August 3, 2006.
[30] Lucier, Chuck, Steven Wheeler, and Rolf Habbel, "The Era of the Inclusive Leader." The Corporate Board, September/October 2007.
[31] Chairmen s Forum, founded in 2008 by the Yale School of Management, Millstein Center for Corporate Governance and Performance. Also see, "Chairing the Board: The Case for Independent Leadership in Corporate North America," Policy Briefing No. 4, Millstein Center for Corporate Governance & Performance, Yale School of Management, 2009
[32] Barrett, Annalisa, "Executive Chairs." The Corporate Library, December 2009.

1. Designated lead director, elected by and from the independent board members with clearly delineated duties. Alternatively, the role may reside with a presiding director, vice chairman, or rotating lead director. At a minimum the duties should include:

    - Presides at all meetings of the board at which the chairman is not present, including executive sessions of the independent directors
    - Serves as liaison between the chairman and the independent directors
    - Approves information sent to the board
    - Has formal control of the agenda setting process—developing and approving meeting agendas for all board meetings
    - Approves meetings schedules to assure that there is sufficient time for discussion of all agenda items
    - Has the authority to call meetings of the independent directors
    - If requested by major shareowners, ensures that he is available for consultation and direct communication;

2. The company publicly discloses a comparison of the duties of its independent lead director and that of its chairman;

3. The company publicly discloses a sufficient explanation as to why it chose not to give the position of chairman to the independent lead director;

4. 2/3 independent board;

5. All independent key committees;

6. Established governance guidelines;

7. The company should not have underperformed both its peers and index on both a one-year and three-year total shareowner returns basis, unless there has been a change in the Chairman/CEO position within that time; and

8. The company does not have any problematic governance issues.

***Require Majority of Independent Directors: FOR***
Shareowners are best served when their board includes a significant number, preferably a supermajority, of independent outside directors. They can bring the most objectivity and a fresh perspective to the issues facing the company since they are not employed at the company and thus are not susceptible to the problems insiders often face. The conflicts of interest problems boards face when designing executive compensation policies, as well as responding to takeover offers, are much less severe for outsiders than executive officers. Perhaps the most important role of outside directors is to objectively evaluate the performance of top management.

A 2006 study on options backdating, identifying a link between manipulation of stock options and corporate governance, examines the occurrence of grants given at the lowest price of the month ("lucky grants") for the period of 1996-2005. The authors of the paper find that 1,150 lucky grants took place during the observed period while 12 percent of companies provided such grants due to manipulation. According to the study, lucky grants are more likely to occur when the firm lacks a majority of independent directors and when the CEO has longer tenure—both factors associated with greater CEO influence on the company's pay-setting and governance processes. The paper also finds that grant manipulation is not concentrated in any one sector, rather, it was found to be widespread across all industries. Grants from manipulation do not appear to have served as substitutes to other forms of compensation, and the gains to CEOs from such grants are estimated to exceed 20 percent of the value of the grant, increasing the CEO's total compensation by more than 10 percent.[33]

[33] Bebchuck, Lucian, Yaniv Grinstein and Urs Peyer, 2006, "Lucky CEOs", available at http://papers.ssrn.com/abstract_id=945392.

As a general rule, we consider a two-to-one ratio of independent outsiders to insiders and affiliated outsiders to be a reasonable standard. We strongly disfavor board representation that does not meet this minimum two-thirds independence threshold, and routinely withhold support from individual director nominee who are not independent (excluding the CEO) in those circumstances where the full board comprises less than 50 percent independence levels. Furthermore, the SBA believes strongly in restricting membership on compensation, audit, and nominating committees to independent outside directors only.

***Limit the Number of Non-Independent Directors: CASE-BY-CASE***
Proposals that seek to limit the number of non-independent board members often define who would be considered non-independent and describe a time period during which the criteria may be met. Since shareowners are well served by a majority of independent directors, the SBA is likely to support proposals that seek to limit the service of non-independent directors provided that the terms of the limits, including number of directorships and independence criteria, are reasonable and not overly restrictive. Limiting the number of company executives, relatives, and prior employees that serve on the board is expected to result in a better system of monitoring on behalf of shareowners.

***Independent Committees: FOR***
As stated above, the SBA votes FOR proposals asking that the audit, compensation, and nominating committees be compromised exclusively of independent directors. We believe that independent directors face fewer conflicts of interests and are better prepared to protect shareowner interests under most corporate scenarios.

Our opinion is further supported by the conclusion drawn upon by academic studies that have examined whether audit committees and board characteristics are related to earnings management by the firm. Empirical studies have revealed a non-linear negative relationship between audit committee independence and earnings manipulation. Additionally, significant relation is found only when the audit committee has less than a majority of independent directors. Furthermore, earnings management is positively related to whether the CEO sits on the board's compensation committee. The results suggested that committees structured to be more independent of the CEO may be more effective in monitoring the corporate financial accounting process.[34] Finally, an academic comparative study on governance also finds that audit committee independence is associated with higher value of firms both in the United States and worldwide.[35]

***Establish a Nominating Committee: CASE-BY-CASE***
It is a fundamental tenet of corporate governance that the board should be an independent body capable of providing objective oversight of management and company's overall direction. The SBA believes that this goal can best be achieved when those entrusted with the responsibility of proposing nominees for election to the board are independent of the CEO and have no personal interest in the company arising from a salary, a retainer (other than fees received for service as a director), a consulting agreement, or any other significant business agreement.

If the company's performance has been below average and the nominating committee is to be composed of independent directors, a vote may be cast FOR the proposal.

***Establish an Enterprise Risk Management Committee: CASE-BY-CASE***
The SBA generally encourages companies, especially financial companies, to have a standing enterprise risk management committee of the board with formal risk management oversight responsibilities.[36] Traditionally, risk management has been the purview of the audit committee at most companies. However, with the increased responsibilities and resultant time commitment for audit committees as a result of rule making under Sarbanes-Oxley, we believe the formation of a committee dedicated to identifying and managing risk may be warranted. Poor or nonexistent risk management controls exacerbated catastrophic losses for companies and shareowners during the 2008 credit crisis when many boards did not fully appreciate the level of risk to which the company was exposed. We believe all companies should have in place robust, effective risk mitigation policies.

In the Institute of International Finance's Final Report of the IIF Committee on Market Best Practices: Principles of Conduct and Best Practice Recommendations, the IIF established recommendations advocating corporate adoption and implementation of the Chief Risk Officer position and the development of either a risk committee as part of the corporate board of directors, or at the very least, adding the role of risk management to the audit committee's duties.[37] However, the SBA believes that a separate risk management committee would be the best option in most circumstances because many audit committees are overworked and the complexity of risk management may surpass the skills and knowledge of many audit committee members. A recent National Association of Corporate Directors (NACD) white paper recommended boards consider assigning risk management responsibilities to certain committees to help ensure adequate coverage, potentially assigning the board governance committee with allocating such responsibilities. The NACD report noted that risk oversight is a full board responsibility, with maintenance of an appropriate risk management infrastructure encompassing risk identification, monitoring, and mitigation as a key duty.[38] While the trend is leading

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[34] Klein 2006.
[35] Aggraval, Reena et al, 2007, "Differences in Governance Practices between US and Foreign Firms: Measurement, Causes, and Consequences", Charles A. Dice Center for Research in Financial Economics, Working Paper 2007-14.
[36] In 2004, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) defined Enterprise Risk Management (ERM) as, "a process, effected by an entity s board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives".
[37] Final Report of the IIF Committee on Market Best Practices: Principles of Conduct and Best Practice Recommendations, Institute of International Finance, July 2008, *available at* http://www.iif.com/regulatory/ (last visited March 11, 2009) [hereinafter IIF].
[38] "White Papers: Series I – Risk Oversight/Transparency/Strategy/Executive Compensation," National Association of Corporate Directors, March 2009.

toward more banks developing these risk management committees, "the presence of a dedicated risk committee is still not common practice across large banks."[39] Additionally, many banks that do have committees do not hold meetings on a regular basis and their committees are not made up of qualified members.

As part of the director election process, we may withhold support for individual directors if there are indications that a director failed to understand company risk exposures and/or failed to take reasonable steps to mitigate the effects of the risk, leading to large losses (e.g. in the form of write-downs for mortgage-related losses). In those instances where the board or committee is responsible for risk management and risk oversight, under the terms of its charter, we believe shareowners need to enforce accountability on those directors responsible for failing to properly execute that oversight.

***Advisory Committee: CASE-BY-CASE***
The main purpose of a shareowner advisory committee is to advise the board on shareowner concerns and to create a formal means of communication between company stockholders and company management. Such committees do not have any decision-making authority and they remain advisory in nature. Their scope does not stray into matters concerning the day-to-day management of company operations but is limited to only those subjects involving corporate governance instead. The SBA generally votes FOR advisory committee proposals that are intended to improve poor corporate governance.

***Use of Majority Voting For Election of Directors: FOR***
The board of directors is elected to represent the company's shareowners, and its primary responsibility is to monitor management. Shareowners need an appropriate and effective method for expressing their satisfaction or lack thereof with the board's performance of its duties. The SBA supports any proposal that provides shareowners the ability to better monitor the board and make its members more accountable to shareowners. Most corporations use plurality voting under existing state laws, whereby management can nominate an individual director and, if the election is uncontested, approve its own nominee to the board with just a single vote. The SBA favors the majority voting method for the election of unopposed candidates and favors the plurality method only in rare cases where multiple candidates seek the same directorship, to ensure an election winner.

In October 2006, the Majority Vote Work Group, a joint effort between a number of institutional investors and corporations, issued a report on the findings of the group's examination into issues associated with the majority vote standard. The report's findings include the assertion that failure of a director to be elected by a majority of votes cast may indicate loss of shareowner confidence in the director or the board, and that election of directors by less than a majority vote may lead shareowners to question the value of the election process. The report also supports the application of the plurality standard to any contested director election, where there are more nominees than board seats available, even if a majority vote standard were applied to uncontested election of directors. The investor members of the group note an increase in shareowner support for proposals to adopt the majority vote standard, reaching an average support of 48 percent in the 2006 proxy season.[40]

In November of 2007, Neal, Gerber & Eisenberg LLP published a survey of 534 companies that have adopted provisions regarding majority voting in director elections. The study found that two-thirds of the companies in the S&P 500 have adopted some type of majority voting. In February 2006, only sixteen percent of the companies in the S&P 500 had adopted majority voting. Forty-two percent of companies surveyed adopted policies on majority voting while thirty percent of companies adopted bylaws addressing the issue. Twenty-eight percent of companies adopted both policies and bylaws. Just over half of the companies surveyed have a true majority voting requirement while the rest retained the plurality vote standard with a discretionary policy addressing the status of nominees who receive a majority withhold vote.[41]

In July 2011, Ertimur and Ferri examined the effects of a change in the director election system from a plurality voting standard to majority voting. They documented abnormal returns of 1.43-1.60 percent around annual meeting dates where shareowner proposals to adopt a majority vote standard are voted upon. The results suggest that shareowners perceive the adoption of a majority vote standard as a value enhancing change in governance and is consistent with the notion that the majority vote system makes boards more responsive to shareowner pressure.[42]

The SBA strongly endorses majority voting for the meaningful accountability it affords shareowners and because it provides another element to the system of checks and balances of power within the corporate structure. The SBA will therefore support shareowner proposals at companies with a discretionary policy towards majority voting seeking for the company to adopt true majority voting, through a formal bylaw amendment.

***Office of the Board: FOR***
The SBA generally supports shareowners proposals requesting that the board establish an Office of the Board of Directors in order to facilitate direct communications between shareowners and non-management directors, unless the company has all of the following:

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[39] "Risk Governance at Large Banks: Current Status and Credit Implications." Moody s Global Banking, July 2009.
[40] Majority Vote Work Group Report, October 2006.
[41] Allen, Claudia H., November 2007. "Study of Majority Voting in Director Elections", Neal, Gerber & Eisenberg LLP.
[42] Ertimure, Yonca and Fabrizio Ferri, 2011. "Does the Director Election System Matter? Evidence from Majority Voting." Social Science Research Network. http://ssrn.com/abstract=1880974.

- Established a communication structure that goes beyond the exchange requirements to facilitate the exchange of information between shareowners and members of the board
- Disclosed information with respect to this structure to its shareowners
- Heeded majority-supported shareowner proposals or a majority withhold vote on a director nominee
- Established an independent chairman or a lead/presiding director. This individual must be made available for periodic consultation and direct communication with major shareowners.

***Proxy Access: FOR***
In late 2009, the SEC proposed to allow shareowners the right to place director candidates within the company's proxy materials. "By making it easier for shareholders to replace directors, proxy access can contribute to making directors more accountable to shareholders and more attentive to their interests."[43] The SBA supported this proposal, which would have set an access default with the freedom to opt-out to a no-access regime. Additional reforms occurred in August 2009, dramatically changing Delaware Law governing the ability of shareowners to nominate directors and make other nomination oriented changes to a company's bylaws. Delaware General Corporation Law ("DGCL") Section 112 permits shareowners to adopt bylaws that require the corporation to include shareowner nominees for board election and permits the right to be conditioned on several factors. Section 113 of the DGCL permits shareowners to adopt bylaws that require the reimbursement of expenses incurred by a shareowner in connection with a proxy solicitation, again, with certain permitted conditions.[44] Some observers view proxy access without a corresponding solicitation reimbursement mechanism to be less than optimal and represent a shortcoming in the ability of shareowners to have meaningful input into selecting their own director representatives.

In July 2011, the SEC rule covering a mandatory proxy access default (Rule 14a-11) was legally overturned. The SEC's corresponding Rule 14a-8(i)(8) covering the adoption of proxy access mechanisms through individual shareowner resolutions, commonly referred to as "private ordering," was implemented in September 2011. Shareowners in the United States are now permitted to require companies to include shareowner proposals regarding proxy access procedures in company proxy materials beginning in 2012. Such proposals may be submitted either as precatory (advisory) proposals or binding proposals.

The SBA will generally vote FOR proposals that allow significant company shareowners access to management's proxy material in order to nominate their own candidates to the board of directors. The original 2009 proposal contained within SEC Rule 14a-11, requiring a three percent ownership and a three year holding period, is considered a reasonable benchmark against which individual shareowner proposals can be compared.

Factors to be assessed by the SBA include, but are not limited to:
- Ownership thresholds stipulated by the proposal;
- Maximum proportion of the full board that shareowners may nominate in a single year; and
- Other procedural matters, such as listing order within the proxy, ownership certification requirements, etc.

Proposals that require an investor (or group of investors) to own a meaningful percentage of the company's voting stock, generally defined as greater than one percent, are favored. Proposals that require ownership for meaningful periods of time, generally defined as greater than one year, are favored. The SBA may vote AGAINST proposals which contain burdensome or otherwise restrictive requirements, such as ownership or holding thresholds which are set at impractical levels.

***Minimum Stock Ownership: FOR***
The SBA supports proposals that require directors to own a minimum amount of company stock. The SBA will consider voting against directors who own no company stock and have served on the board for more than one year. One of the best ways for directors to align their interests with those of the shareowners is to own stock in the corporation.

A prototype of a set of Share Ownership and Retention Guidelines should link a significant portion of an executive's compensation to the company's stock performance. In this manner, the interests of management are better aligned with the interests of shareowners.

The guidelines should annually review and identify the positions covered by directors and executives. The annual review should also provide information on whether guidelines are met, and should describe what action is taken for non-compliance. Furthermore, the guidelines should identify what compensation types may be considered as ownership and what compensation types are not taken into account. Ownership levels should be linked to an individual's corporate position, with the greatest ownership target assigned to the CEO. Significant targets should be set for non-employee directors in the form of multiples of their annual salary. Finally, the guidelines should identify the time allowed to participants to meet the guidelines, and provide for penalties for non-compliance in the signified timeframe.

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[43] Bebchuk, Lucian A. and Scott Hirst, "Private Ordering and the Proxy Debate." Harvard Law School. Discussion Paper No. 653. 11/2009 Available at SSRN: http://papers.ssrn.com/abstract=1513408.
[44] HealthSouth Corporation, in October of 2009, became the first large U.S. public company to adopt a bylaw implementing sections 112 and 113 ofthe DGCL.

Per the SBA's model ownership guidelines, non-employee directors need to maintain ownership of a number of shares having a market value equal to five times their annual retainer. Senior executives are required to achieve and maintain an ownership position expressed as a multiple of salary as follows:

| | |
|---|---|
| Chief Executive Officer | 15X Salary |
| Chief Operating Officer | 10X Salary |
| Chief Administrative Officer | 8X Salary |
| President | 7X Salary |
| Other Senior Executives | 5X Salary |

***Require Director(s) be Non-Executives: CASE-BY-CASE***
In general, non-executive directors are best suited to provide the oversight role expected of them by shareowners. Proposals to increase or set a minimum number of independent directors, therefore, generally promote shareowner interests. However, the boards of many growth companies are comprised of management/owners, often including the founder. Since the interests of these management directors are already aligned with the shareowners, a requirement that would entail a significant change in the board may not always be appropriate in these cases.

***Adopt Two-Tiered (Supervisory/Management) Board Structure: CASE-BY-CASE***
Companies in many foreign countries have a two-tiered board structure, comprising a supervisory board of non-executive directors and a management board with executive directors. The supervisory board oversees the actions of the management board, while the management board is responsible for the company's daily operations. At companies with two-tiered boards, shareowners elect members to the supervisory board only; the supervisory board appoints management board members. In Austria, Brazil, the Czech Republic, Germany, Peru, Poland, Portugal, and Russia, two-tiered boards are the norm. They are also permitted by Company law in France and Spain.

The merits of the new structure will be weighed against the merits of the old structure in terms of its ability to represent shareowners' interests adequately, provide for optimal governance structure, and also to generate higher shareowner value.

***Ratify actions taken by Board during past year provided that local law does not exempt directors from liability for wrongful misconduct or suits arising from falsification of accounts: CASE-BY-CASE***
Many countries require that shareowners discharge the board or management for actions taken in the previous year. In most cases, discharge is a routine item and does not preclude future shareowner action in the event that wrongdoing is discovered. Unless there is clear evidence of negligence or action counter to shareowners' interests, the SBA will support the proposals . However, in the United States, given the unusual nature of discharge proposals, the SBA will pay close attention and consider voting against proposals that would limit the board or management from any future legal options.

In June 2008, Manifest and Morley Fund Management analyzed governance practices in continental Europe and issued a report that emphasized the country-specific implications of discharging directors. "Directors' Liability Discharge Proposals: The Implications for Shareowners" stressed that the nature and scope of directors' liabilities vary by jurisdiction. "Each market has its own rules, regulations and best practice guidelines against which informed decisions should be measured and carefully weighed." One similarity noted in the report was that "in all the markets covered by the study, a failure to grant a discharge from liability does not have an immediate effect on the liability of directors, but merely leaves the possibility open for the company to initiate an action for liability."

***Approve proposed/completed transactions between directors and company: CASE-BY-CASE***
A transaction between a parent company and its subsidiary, or a company's dealings with entities that employ the company's directors, are usually classified as related-party transactions and are subject to company law or stock exchange listing requirements that mandate shareowner approval. Shareowner approval of these transactions is critical as they are meant to protect shareowners against insider trading abuses.

The SBA will consider whether the proposed transaction unduly favors the director(s) at the expense of the company or was completed at arm's length. We vote FOR reviews of director transactions by independent committees.

***Designate directors to represent company in judicial proceedings: FOR***
By the time a company has reached the point of having to restructure, it may be in desperate straits, and attempts to forestall a lifesaving financial operation by voting against this item is counterproductive to shareowners' best interest.

**AUDITORS**

Most major companies around the world use one of the major international auditing firms to conduct their audits. As such, concerns about the quality and objectivity of the audit are minimal, and the reappointment of the auditor is usually a routine matter. In the United States, companies are not legally required to allow shareowners to ratify the selection of auditors; however, a growing number are doing so. Typically, proxy statements disclose the name of the company auditor and that the board is responsible for selection of that firm.

The auditor's role in safeguarding investor interests is critical. Independent auditors have an important public trust, for it is the auditor's impartial and professional opinion that assures investors that a company's financial statements are accurate.[45] Therefore, the practice of auditors providing non-audit services to companies must be closely scrutinized. While large auditors may have internal barriers to ensure that there are no conflicts of interest, an auditor's ability to remain objective becomes questionable when fees paid to the auditor for non-audit services such as management consulting, general bookkeeping, and special situation audits exceed the standard annual audit fees. While some compensation for non-audit services is customary, the importance of maintaining the independence of the auditor is paramount. Auditor independence from the firm being audited is essential to promote objectivity and reduce the potential for abuse. "The Audit Firm Governance Code supports the appointment of independent non-executives directors by the audit firms as it relates to the establishment of an independent board of directors."[46] An independent board increases the quality of informed influence on the governance structures of the auditing firm.

In addition to ensuring that the auditor is free from conflicts of interest with the company, it is also important to ensure the quality of the work that is being performed. A recent study found that when an audit partner's name is included within the audit report, the quality of the audit increases,[47] along with auditor fees. As such, a Glass Lewis trend report noted that the number of restatements is on the decline, down 17 percent from 2006, with one out of ten companies filing restatements in 2007 versus one out of nine companies filing restatements in 2006. [48] Despite the decline, restatements persist and can have a negative impact on the perception of the auditor's ability to perform an independent, accurate audit. The integrity of the audit comes into question especially in instances where a company has a significant restatement.

***Ratification of Auditors: CASE-BY-CASE***
The SBA votes FOR proposals to ratify auditors unless there is reason to believe that the auditing firm has become complacent in its duties or its independence has been compromised. For example, non-audit fees, primarily tax and other consulting fees, can exceed audit fee revenue by a large margin, impairing an audit firm's objectivity. A 2011 study indicated a strong relationship between changes in audit fee levels in year one and subsequent changes in operating performance in years two through five. The study examined about 5,000 small sized companies over a seven year period, concluding that rising audit fees were a leading indicator for future deterioration in financial performance as measured by firms' return on assets, determined by both earnings and cash flows.[49] The SBA believes all publicly held corporations should rotate their choice of auditor's periodically. Shareowners should be given the opportunity to review the performance of the auditors annually and ratify the board's selection of an auditor for the coming year.[50] Although, mutual funds have been allowed to trade off annual auditor ratification in exchange for independent directors on the audit committee, the SBA believes funds should maintain auditor ratifications as well.

Independent public audit firms should not be the auditors of any company for which they simultaneously provide other services, including other non-audit or information services; audits should be carried out by an independent external auditor. Moreover, the Audit Committee should oversee the firm's interaction with the external auditor and disclose any non-audit fees completed by the auditor. In the event of serial or significant restatements, the SBA will take a closer look at the auditor's performance when considering whether or not to support the re-appointment of the auditor.

***Appoint External Auditors and Authorize Directors to Set Auditors' Remuneration: FOR***
Shareowners are typically asked to approve the appointment of the independent auditors and to fix their remuneration at every annual shareowner convening. Because most major companies in international markets employ one of the major international auditing firms to conduct their audits, concerns about the quality and objectivity of the audit are generally minimal. As such, the reappointment of the auditor is usually a routine matter and the SBA generally votes in favor of the appointment, unless there are reasons to question their independence.

***Appoint Internal Statutory Auditors (Japan, Hong Kong, South Korea): FOR***
Most votes for auditors in Japan are to approve internal statutory auditors (also known as corporate auditors) rather than external auditors. Statutory auditors have the right to attend board meetings, although not to vote, and the obligation to cooperate with the

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[45] Hollis Ashbaugh-Skaife, et al, *The Effect of SOX Internal Control Deficiencies on Firm Risk and Cost of Equity* June 10, 2008.
[46] Wood, Christy. Chair of the ICGN Board of Governors. "Reply to: Audit Firm Governance, Second Consultation Paper, A Project for the Financial Reproting Council." October 10, 2009.
[47] Joseph Carcello & Chan Li, "Costs and Benefits of Requiring an Engagement Partner Signature: Recent Experience in the United Kingdom," Corporate Governance Center at the University of Tennessee, Working Paper, 2012
[48] Glass, Lewis & Co., "Restatement Trend Alert: Out of Sight, Out of Mind", 2006.
[49] Jonath Stanley, Auburn University, "Is the Audit Fee Disclosure a Leading Indicator of Clients Business Risk?," American Association of Accountants Quarterly Journal, 2011
[50] Under Rule 10A-3(b)(2) of the Securities Exchange Act of 1934, as amended, the audit committee, "must be directly responsible for the appointment, compensation, retention and oversight," of the independent auditor. Section 303A.06 of the New York Stock Exchange Listed Company Manual requires that the audit committees of its listed companies satisfy the requirements of Rule 10A-3. As a result of these requirements, audit committee charters normally include the responsibility for and total discretion to select, evaluate, compensate and oversee the work of any registered public accounting firm engaged in preparing or issuing audit report(s).

external auditor and to approve its audit. They are required by law to keep board members informed of the company's activities, but this has become a largely symbolic function. They do not have the ability to remove directors from office. Internal auditors serve for terms of four years, and may be renominated an indefinite number of times. While many investors view statutory auditors in a positive light, they are not substitutes for independent directors.

Companies must designate at least half of their internal auditors as independent. While companies have complied with the technical requirements of the law, many have ignored its spirit. It is in shareowners' interests to improve the audit and oversight functions in Japan and to increase the accountability of companies to shareowners. Therefore, the SBA will not support internal auditors specified as independent but with a past affiliation with the company.

Companies are also allowed to nominate alternate statutory auditors, who would serve only if an auditor becomes unable to complete his or her term. By designating an alternate in advance, companies are spared the need to convene an EGM to fill a vacancy on the board of statutory auditors. Alternate statutory auditors who are designated as independent should be held to the same standards as other nominees for independent auditor. As with directors, the Corporate Law requires companies to discuss the role played by the outside (independent) statutory auditors, including their attendance at meetings of the board of directors and board of statutory auditors. Where a statutory auditor attends fewer than 75 percent of such meetings, without a reasonable excuse, the SBA will generally vote against the auditor's reelection.

In other capital markets, such as South Korea, proposals seeking shareowner approval for statutory auditors' fees are not controversial. Generally, management should disclose details of all fees paid to statutory auditors well in advance of the meeting date so that shareowners can make informed decisions about statutory auditor remuneration requests.

***Remove/Accept Resignation of Auditors - CASE-BY-CASE***
The SBA seeks to ensure auditors have not been pressured to resign because of their zeal in providing full disclosure.

***Auditor Indemnification and Limitation of Liability: CASE-BY-CASE***
Auditor indemnification and limitation of liability are evaluated on a CASE-BY-CASE basis. Factors to be assessed by the SBA include, but are not limited to:

- The terms of the auditor agreement- the degree to which these agreements impact shareowners' rights;
- Motivation and rationale for establishing the agreements;
- Quality of disclosure; and
- Historical practices in the audit area.

The SBA will consider voting against auditor ratification if the auditor engagement contract includes provisions for alternative dispute resolution, liability caps, and caps on punitive damages (or the exclusion of punitive damages). Such limitations on liability and indemnification shift the risk from the auditor to the company, and therefore, the shareowners. The staff of the Securities and Exchange Commission ("SEC") has stated that it believes caps on punitive damages in audit contracts are not in the public interest and makes the auditor no longer independent.[51] The SBA will also consider voting against audit committee members when a company has entered into an agreement with its auditor requiring alternative dispute resolution and punitive liability caps.

***Approve Accounting Transactions (other than dividend): CASE-BY-CASE***
In many international markets, proposals to approve accounting transfers are common and are often required to maintain specified balances in accounts as required by relevant market law. Companies are required to keep specific amounts in each of their reserves. Additionally companies may, in some instances, be required by law to present shareowners with a special auditors' report confirming the presence or absence of any non-tax-deductible expenses, as well as the transfer of these to the company's taxable income if applicable.

In the absence of any contentious matters, the SBA is generally in favor.

***Audit Firm Rotation, Term Restrictions, and Scope of Engagement Proposals: CASE-BY-CASE***
Shareowner proposals normally ask companies to prohibit their auditors from engaging in non-audit services (or cap the level of non-audit services) or recommend rotation of the audit firm. In 1992, the American Institute of Certified Public Accountants' (AICPA) SEC Practice Section released its position regarding mandatory rotation of audit firms of publicly held companies. AICPA concluded that there was no credible evidence that rotating audit firms would improve the quality of audits. AICPA explained that a mandatory rotation "would dramatically increase costs for firms, clients and the public. In addition, it would increase the likelihood of poor audits, by depriving auditors of the most valuable tool: experience with a client and the resulting comprehensive knowledge of its business and operations."[52]

The concept of term limits for audit firms was encouraged in a 2002 study by the Conference Board's Commission on Public Trust and Private Enterprise. The Commission advocated rotation if the audit firm has been employed for a substantial amount of time

[51] U.S. Securities and Exchange Commission, Office of the Chief Accountant: Application of the Commission s Rules on Auditor Independence – Frequently Asked Questions, December 13, 2004.
[52] SEC Practice Section and AICPA Division for CPA Firms, Position Regarding Mandatory Rotation of Audit Firms of Publicly Held Companies, April 16, 1992.

(over ten years); when one or more former partners or managers of the firm are employed by the company; or when significant non-audit services are provided to the company. Apart from building shareowner confidence, the study cited other advantages of rotation:

- The incoming audit firm would be able to take a fresh look at the company's finances, accounting practices and the former firm's audit;
- It would reduce the financial incentives for an auditor to compromise its judgment on borderline accounting issues;
- The audit firm would not be risking a lengthy stream of revenues by disagreeing with management; and
- Knowing its work will be reviewed by another firm would deter questionable judgments by the current audit firm.

While there are costs to companies in changing auditors periodically, the Commission contended that such costs would be significantly less than the market costs resulting from the loss of investor confidence arising from inaccurate financial information.[53] In August 2011, the Public Company Accounting Oversight Board issued a concept release seeking comment on the possibility of mandatory audit firm rotation every ten years, in order to reduce management pressure and influence on auditing firms.[54] In late 2011, European regulators proposed sweeping changes to the audit industry, including mandatory audit rotation and other engagement limitations and service restrictions on certain audit firms within the industry.

A 2002 Harvard Business Review study observed that auditors are inclined to have a bias toward the companies that hire them. The authors argue that real independence would require automatic rotation of the audit firm, the prohibition of non-audit services, and a ban on auditors from going to work for their former clients.[55] A number of institutional investors advocate a term limit for audit firms of five to seven years, though some shareowner initiatives have suggested four-year cycles.[56] Other empirical studies examining the effects of mandatory auditor rotation on audit quality have shown mixed results.[57] As of 2012, only five global markets require some form of mandatory auditor rotation.[58]

The SBA votes CASE-BY-CASE on shareowner proposals related to audit firm fees, rotation requirements and related issues based upon the following:

- The tenure of the audit firm
- The company's establishment and disclosure of a renewal process whereby the auditor is regularly evaluated for both audit quality and competitive price
- The length of the rotation period advocated by the proposal
- Significant audit-related issues

**PROXY CONTESTS**

***Proxy Contests: CASE-BY-CASE***
Votes on proxy contests should be determined on a CASE-BY-CASE basis, considering the following factors:

- Past performance relative to its peers
- Market in which the fund invests
- Measures taken by the board to address the issues
- Past shareowner activism, board activity, and votes on related proposals
- Strategy of the incumbents versus the dissidents
- Independence of directors
- Experience and skills of director candidates
- Governance profile of the company
- Evidence of management entrenchment

When analyzing proxy contests, the policy focuses on two central questions: (1) Have the dissidents demonstrated that change is warranted at the company, and if so, (2) will the dissidents be better able to affect such change versus the incumbent board?

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[53] The Conference Board Commission on Public Trust and Private Enterprise, "Corporate Governance: Principles, Recommendations and Specific Best Practice Suggestions." Parts 2 and 3, Jan. 9, 2003.
[54] PCAOB Concept Release No. 2011-006. August 16, 2011. http://pcaobus.org/Rules/Rulesmaking/Docket037/Release_2011-006.pdf.
[55] Max H. Bazerman, George Loewenstein, and Don A. Moore, "Why Good Accountants Do Bad Audits." Harvard Business Review, Vol. 80, Issue 11, Nov. 1, 2002.
[56] Individual investor Chris Rossi proposed four-year audit firm rotations at Winn-Dixie Stores Inc. and the Great Atlantic & Pacific Tea Co. in 2002.
[57] See Jackson, Modrich, and Roebuck, "Mandatory Audit Firm Rotation and Audit Quality," 2007; Chung, H., "Selective Mandatory Rotation and Audit Quality: An Empirical Investigation of Auditor Designation Policy in Korea," 2004; and Martinez and Reis, "Audit Firm Rotation and Earnings Management in Brazil," 2010.
[58] Brazil (every five years), Germany (auditor cannot be same firm for more than six years out of any ten year time frame), Greece (every six years), Italy (every nine years), and South Korea (every six years).

When dissidents seek board control, the dissidents must provide a well-reasoned and detailed business plan, including the dissidents' strategic initiatives, a transition plan that describes how the dissidents will effect change in control, and the identification of a qualified and credible new management team. The SBA compares the detailed dissident plan against the incumbents' plan, and the SBA compares the dissidents' proposed board and management team against the incumbent team.

When dissidents seek minority board representation, the SBA places a lower burden of proof on the dissidents. In such cases, the SBA's policy does not require the dissidents to provide a detailed plan of action or proof that its plan is preferable to the incumbent plan. Instead, the dissidents must prove that change is preferable to the status quo and that the dissident slate will add value to board deliberations, including by considering the issues from a viewpoint different than current management, among other factors.

***Shareowner Proposals to Reimburse Shareowners for Expenses Incurred: CASE-BY-CASE***
Most expenditure incurred on behalf of incumbents in a proxy contest is paid directly by the company. Reimbursement is generally limited to those expenses deemed reasonable and necessary to inform shareowners. Practically speaking, reimbursement is almost never denied by these limitations; thus, incumbent directors are free to authorize the company to pay the entire cost of their proxy campaign.

By contrast, in most cases dissidents are reimbursed only for proxy solicitation expenses if they gain control of the company. In successful proxy contests, new management will often seek shareowner approval for the use of company funds to reimburse themselves for the costs of solicitation. The courts have supported such actions in ruling that successful dissident groups benefited the company by removing incompetent or dishonest management.

Empirical evidence suggests that the most advantageous solution for shareowners is an intermediate level of compensation, for both incumbents and dissidents.[59] Of course, when a proposal for reimbursement is submitted by the dissidents in either a successful or unsuccessful proxy contest, shareowners are usually asked to vote for or against repaying the entire cost of the solicitation.

Voting to reimburse proxy solicitation expenses should be analyzed on a CASE-BY-CASE basis. In cases where the dissident position is supported, believing it to be in the best interests of shareowners, the SBA generally votes FOR reimbursing such proxy solicitation expenses.

***Confidential Voting: FOR***
The SBA votes FOR resolutions requesting that corporations adopt a policy comprising both confidential voting and the use of independent vote tabulators and inspectors of elections because it is the best way to guarantee confidentially. However, the SBA does not withhold support for a resolution calling for confidential voting if it lacks an independent inspector requirement.

**ANTI-TAKEOVER DEFENSES AND VOTING-RELATED ISSUES**

The rise in unfriendly corporate takeover activity in the 1980s spawned various anti-takeover devices designed to make takeovers prohibitively expensive for the bidder, usually called "poison pills." To further entrench management, corporations sought to limit shareowners' ability to vote. In many earlier cases, boards unilaterally enacted such measures without providing shareowners a voice in the process. States also assumed a role by adopting takeover defense laws or statutes, competing with each other to become the most attractive corporate haven. Today, most companies have an array of defenses in place and, in response shareowners are increasingly filing proposals to remove these defenses.

The debate concerning these defenses focuses on whether they enhance or detract from shareowner value. Proponents argue that a company's board, when armed with these takeover protections, may use them to negotiate and obtain higher takeover premiums from bidders. According to this position, these devices protect the target company and provide it with negotiating flexibility, which benefits shareowners through financially fair tender offers.

Conversely, the opposing viewpoint claims that management afforded such protection are more likely to become insulated than to actively pursue the best interests of shareowners. Such takeover defenses serve as obstacles to the normal functioning of the marketplace, which, when operating efficiently, should replace poorly performing managers.

***Advance Notice Requirements for Shareowner Proposals/Nominations: CASE-BY-CASE***
The SBA considers shareowner proposals to provide for advanced notice proposals on a CASE-BY-CASE basis, supporting those proposals which allow shareowners to submit proposals as close to the meeting date as reasonably possible and within the broadest window possible. Requests to move advance notice deadlines as early as 150 days or 180 days prior to meetings have been presented by a number of companies in recent years. Such early deadlines may be intended more to protect incumbent directors than to provide early notice to the board.

In addition, many companies now request shareowner approval of "second generation advance notice bylaws", which require shareowner nominees to submit company-prepared director questionnaires.[60] While the SBA appreciates increased disclosure of

[59] Bebchuk, Lucian Arye and Kahan, Marcel, "A Framework for Analyzing Legal Policy Towards Proxy Contests," California Law Review. Vol. 78, October 1990, pp. 1073-1135.
[60] Weingarten, Marc and Erin Magnor, "Second Generation Advance Notification Bylaws" Harvard Law School Corporate Governance Forum, March 17, 2009.

the qualifications of nominees (and incumbents), we reserve the right to disapprove of such requirements if they served to frustrate shareowner-proposed nominees.

***Amend Bylaws without Shareowner Consent: AGAINST***
The SBA does not support proposals giving the board exclusive authority to amend the bylaws. Conversely, proposals giving the board, in addition to shareowner, the ability to amend the bylaws are supported by the SBA.

***Poison Pills: AGAINST***
Stock purchase rights plans or shareowner rights plans, otherwise known as poison pills, have enjoyed widespread adoption since their inception in 1983. Poison pills are the most prevalent takeover defense among S&P 500 companies. They also enjoy support among other large companies. According to publicly available data, over 3,000 plans are now in place at major companies, including over two-thirds of all S&P 500 companies and over one-half of all Business Week 1000 companies.[61] The vast majority of pills were instituted after November 1985, when the Delaware Supreme Court upheld a company's right to adopt a poison pill without shareowner approval in *Moran v. Household International, Inc.*

Poison pills are corporate-sponsored financial devices that, when triggered by potential acquirers, do one or more of the following: (1) dilute the acquirer's equity holdings in the target company; (2) dilute the acquirer's voting interests in the target company; or (3) dilute the acquirer's equity holdings in the post-merger company. Generally, poison pills accomplish these tasks by issuing rights or warrants to shareowners that are essentially worthless unless triggered by a hostile acquisition attempt.

Empirical studies reveal that firms that adopt poison pills show higher asymmetry between reported earnings and stock returns after the adoption and greater association between reported current earnings and lagged returns. Furthermore, they show that these firms undertake more R&D expenses and long-term investments after poison pill adoptions. While this evidence supports management's claims that poison pills increase their propensity to make long-term investments, researchers find that these long-term investments result in a decrease in firm value.[62]

Academic research indicates that firms that have removed poison pills have done so due to shareowner activism. In a study of 126 firms that removed their poison pills during the 1990-2004, Akyol and Carroll (2006) found that the removals took place following shareowner proposals to remove the takeover defenses, despite management's objection. In cases where companies voluntarily removed their pills, the authors found that such action was taken following active negotiations by institutional investors. Poison pill removals have become more frequent in the post-Enron period. The authors also found that board independence and insider shareholdings are positively related to a board's responsiveness to shareowner activism to remove pills.[63]

Legal arguments have been made to suggest the illegitimacy of poison pill adoptions. Velasco (2002) argues that at the time the poison pill was first considered, corporate law did not authorize corporations to employ poison pills. According to the same legal academic study, even now, Delaware corporate law, fairly interpreted, does not authorize the use of the poison pill against typical contemporary hostile offers.[64]

According to an academic study, poison pills have an impact on earnings management. Poison pills increase the degree of abnormal accruals by 1.9 percent on average, controlling for factors such as firm size, profitability, financial distress, growth opportunities, and information asymmetry.[65]

Companies are reacting to hostile takeover attempts by adjusting the rules of their antitakeover mechanisms. Louisiana Pacific Corp. and Micrel, Inc. have changed their shareowner rights plans, redefining the calculation of ownership to include derivatives. Typically, a poison pill is triggered when a shareowner exceeds a certain percentage of ownership of voting shares. The new emerging types of poison pills would trigger a defense mechanism when shareowners' economic interests, including derivatives, which do not confer voting rights to the owner, exceed a set threshold.

Poison pill adoptions that include derivatives arose in response to the proxy contest that The Children's Investment Fund (TCI) and 3G Capital Partners (3G) waged against CSX Corporation. TCI and 3G were involved in a proxy contest with CSX, requesting the replacement of 5 members of the total 12 members of CSX's board of directors. In June 2008, a court ruling against TCI and 3G declared that the two investors evaded disclosure of their total interest in railroad operator CSX, as the funds did not disclose their holdings of total return swaps. The ruling in relation to the CSX case and the new types of pills, as those introduced by Louisiana Pacific and Micrel hint to a movement towards new disclosure rules, which would strengthen companies' defenses against activist investors.[66]

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[61] Thomson Securities Data Co.
[62] Srinidhi, Bin and Sen, Kaustav, "Effect of Poison Pills on Value Relevance of Earnings."
[63] Akyol, Ali C. and Carroll, Carolyn A., "Removing Poison Pills: A Case of Shareowner Activism" (September 2006). Available at SSRN: http://ssrn.com/abstract=935950
[64] Velasco, Julian, "The Enduring Illegitimacy of the Poison Pill" . The Journal of Corporation Law, Vol. 27, No. 3, pp. 381-423, Spring 2002
[65] Jiraporn, Pornsit, "An Empirical Analysis of Corporate Takeover Defenses and Earnings Management: Evidence from the U.S.", Applied Financial Economics, Vol. 15, No. 5, pp. 293-303, 2005
[66] Lemos-Stein, Mara, "Poison Pills Target Derivatives", Wall Street Journal, June 18, 2008.

A Moody's study finds evidence supporting the view that more takeover defenses are associated with higher levels of credit risk. The report warns that the correlation is weak, and that the impact of takeover defenses on credit risk should be evaluated on a case-by-case basis.

According to a research report by RMG, the percentage of US companies with poison pills has dropped considerably in the post-Enron era. The number of S&P 500 companies with poison pills decreased from approximately 60 percent in 2002 to below 40 percent in 2006. A smaller, but still considerable, decrease was observed in the S&P 1500 companies, from slightly above 60 percent to approximately 45 percent of companies. In contrast to the decrease of poison pills in the US market, takeover defenses are on the rise in Japan and France.

In Japan, the introduction of the defenses comes as a reaction to foreign and domestic shareowners' demands for improved returns. Poison pills have been on the rise in Japan since 2005 when only 21 companies had a poison pill in place. That number rose to 165 in 2006, 266 in 2007, and reached more than 400 in 2008. The increase in poison pills is due to a convergence of factors including: a movement toward investors willing to tender their shares to a hostile acquirer, an emergence of investment funds, and the realization by Japanese managers that their companies are vulnerable to an acquirer. The most common poison pill used in Japan is the advance-warning type. Occasionally shareowners call for such pills to be abolished. A recent White Paper by the Asian Corporate Governance Association cited poison pills and the entrenchment of management as the core issues affecting the development of a robust investment community in Japan [ACGA White Paper, p. 28]. While the White Paper notes that the adoption of poison pills had a negative impact on share price, it also notes that those companies that adopted poison pills also had weak financial performance before adopting the poison pills. With more than half of Japanese companies trading below book value, and chronic overcapacity in many industries, it's hard to see how investors gain by helping underperforming managers resist buyouts. [67]

In France, poison pill adoptions appear as expressions of economic nationalism and protectionism. In contrast to France and Japan, Canada has taken steps to emphasize the rights of shareowners to consider and make final decisions on takeover offers with new generations rights plans, which seek to eliminate board discretion in controlling the bid process.[68]

The SBA supports proposals asking a company to submit its poison pill for shareowner ratification, and votes AGAINST proposals approving or creating a poison pill. "Pills," or shareowner rights plans, have the potential to act as doomsday machines in the event of an unwanted control contest, providing a target board with power (all it has to do is refuse to redeem the pill) over the takeover bid, even if the bid is in the best interest of target shareowners. The power of redemption is the crucial issue for shareowners, because the courts have allowed target company boards great leeway in deciding when a pill must be redeemed, even in the event of bona fide offers. The best defense against hostile takeovers is not necessarily a poison pill, but an effective board making prudent financial and strategic decisions for the company. Since shareowners are rarely afforded the opportunity to vote on the adoption or renewal of poison pills, the SBA will consider voting against boards that adopt or renew a poison pill unless the pill is subject to shareowner ratification within a year of adoption or renewal.

***Anti-Takeover Provisions (France): AGAINST***
All forms of public offers, whether hostile or not, have been more common in recent years, with one research piece citing an average of approximately 90 takeover offers being made each year.[69] Since France's implementation of the European Union Directive on takeover bids in March 2006, there has been a proliferation of proposals specifically related to approving anti-takeover provisions. French law requires companies to disclose whether any proposed capital devices, debt instruments, or other transactions will be used for the purposes of an anti-takeover mechanism. Generally, these proposals are presented as either (i) authority to repurchase shares and trade in company stock during a takeover period; (ii) authority to issue warrants as a takeover defense; (iii) authority to increase capital as a takeover defense; or (iv) authority to prevent a takeover of the company.

The SBA votes AGAINST these authorities as they are not conducive to good corporate governance and can reduce investment returns by substantially limiting opportunities for corporate takeovers.

***Limit Written Consent: CASE-BY-CASE***
The SBA votes AGAINST proposals to restrict or prohibit shareowners' ability to take action by written consent and vote FOR shareowner proposals to allow or make easier shareowner action by written consent. Most states allow shareowners to take direct action such as adopting a shareowner resolution or electing directors through a consent solicitation, which does not involve a physical meeting. Alternatively, consent solicitations can be used to call special meetings and vote on substantive items taking place at the meeting itself.

***Limit Special Meetings: CASE-BY-CASE***
The SBA votes AGAINST proposals that restrict or prohibit a shareowner's ability to call special meetings. We vote FOR shareowner proposals that make it easier for shareowners to call special meetings. Most state corporate statutes allow shareowners to call a special meeting when they want to present certain matters before the next annual meeting. The percentage of shareowner votes required to force the corporation to call the meeting depends on particular state statutes, as does the corporation's ability to limit or deny altogether a shareowner's right to call a special meeting.

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[67] "Poison Pills in Japan, What You Need to Know" RiskMetrics Group, April 25, 2008.
[68] "Poison Pills in France, Japan, the U.S. and Canada: Takeover Barriers Rise in Europe and Japan, But Fall in North America." RiskMetrics Group, May 2007.
[69] "Takeover in France" Freshfields Bruckhaus Deringer

***Supermajority Vote Requirements: AGAINST***
The SBA does not support shareowner proposals that require supermajority voting thresholds, except where required by law. Supermajority requirements can be particularly significant with resolutions to approve mergers and other significant business combinations. Conversely, we vote FOR shareowner proposals that lower such super-majority vote requirements. As a matter of principle, we think shareowner desires should be carried out with a majority vote of the disinterested shares. Furthermore, we much prefer fair price provisions. Fair price provisions, an alternative to the supermajority vote requirement for mergers, combine a standard super-majority vote requirement with the additional protection of requiring that all shareowners left in the back end of a two stage merger be compensated as well as those in the front end.

A study by three academics from 1999 concludes that supermajority requirements discourage a potential acquirer from launching a takeover process, but only when a rival bidder might contest the offer, which is precisely the situation that could generate the greatest economic gain for shareowners. On the other hand, fair price provisions ensure that rival bidders who place a higher value on the target than the initial bidder will enter the contest, resulting in the prospect of more value being delivered to investors. Hence, the study demonstrates that supermajority clauses are unambiguously poor policy while fair price provisions may not be. [70]

***Adopt Supervoting Rights ("Phased Voting") attached to shares held for longer than some specified period: AGAINST***
Under SEC Rule 19c-4, firms are generally prohibited from utilizing several forms of stock that deviate from a one-share, one-vote standard. Such instances include tracking stocks, different stock classes with asymmetric voting rights (e.g. dual class shares), shares with time-phased voting rights as well as shares of stock with capped voting or even no rights whatsoever. However, under an amendment to the Rule made in 1994, most U.S. companies are exempted from such restrictions under particular circumstances. Time phased voting involves the granting of super voting rights to shareowner who have held their stock for some specified period of time, commonly for a period of 5 years, and if so, has the ability upon certification to exercise a disproportionate voting decision. When the SBA has owned equity securities for the required time period, ownership certification will be provided in order to maximize the proxy voting rights offered by time-phased shares.

Additionally, the easiest way for companies to thwart a hostile takeover is to concentrate its voting power in the hands of management or other insiders through the issuance of shares with supervoting rights to members of management. The SBA votes AGAINST the adoption of supervoting rights due to its potential to be used as an anti-takeover instrument.

## MERGERS & CORPORATE RESTRUCTURINGS

***Mergers/Acquisitions: CASE-BY-CASE***
Merging with another company may take place for numerous reasons ranging from vertical integration to capital acquisition. In general, the SBA favors most mergers and acquisitions proposals while considering such factors as business combination or acquisition, the merger's or acquisition's economic merits (synergy), opinion of financial advisor(s), potential conflicts between management's interests and those of shareowners, and impact on corporate governance and shareowner rights.

For any merger proposal, the following items are evaluated:

- Independence of board, or special committee, recommending the transaction
- Process for identifying, selecting, and negotiating with merger partners
- Independence of financial advisor and financial opinion for the transaction
- Aggregate valuation of merger proposal and price of the deal

The SBA may vote AGAINST the merger or acquisition if there is a significant lack of information in order to make an informed voting decision. As well, the SBA may take into consideration investment exposures indirectly affected by the merger or acquisition proposal. For example, when evaluating a merger proposal among two simultaneously owned companies, the SBA may review the likely financial impact of the merger across both investments. This consideration will take into account both the investment objective as well as the individual security ownership rights.

***Appraisal Rights: FOR***
In many states, mergers and other corporate restructuring transactions are subject to appraisal rights. Rights of appraisal provide shareowners, who are not satisfied with the terms of certain corporate transactions, the right to demand a judicial review to determine a fair value for their shares. Such rights also serve another important interest. If a majority of shareowners approve a given transaction, the exercise of appraisal rights by a minority of shareowners will not necessarily prevent the transaction from taking place. Therefore, assuming that a small minority of shareowners succeed in obtaining what they believe is a fair value, appraisal rights may benefit all shareowners. The downside of appraisal rights is that if enough shareowners dissented and if the courts found a transaction's terms were unfair, such rights could prevent a transaction that other shareowners had already approved.

The SBA votes FOR proposals to restore or provide shareowners with rights of appraisal.

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[70] Ravid, S. Abraham and Matthew I. Spiegel, "Toehold Strategies, Takeover Laws and Rival Bidders." Journal of Banking and Finance, Vol. 23, No. 8, 1999, pp. 1219-1242.

***Asset Purchases: CASE-BY-CASE***
The SBA evaluates asset purchase proposals on a CASE-BY-CASE basis, considering the following factors:

- Purchase price
- Fairness opinion
- Financial and strategic benefits
- How the deal was negotiated
- Conflicts of interest
- Other alternatives for the business
- Non-completion risk

***Asset Sales: CASE-BY-CASE***
The SBA examines asset sales on a CASE-BY-CASE basis, considering the following factors:

- Impact on the balance sheet and working capital
- Potential elimination of diseconomies
- Anticipated financial and operating benefits
- Anticipated use of funds
- Value received for the asset
- Fairness opinion
- How the deal was negotiated
- Conflicts of interest

***Approve Reorganization of Division or Department/Arrangement Scheme, Liquidation - CASE-BY-CASE***
Resolutions approving corporate reorganizations or restructurings range from the routine shuffling of subsidiaries within a group to major rescue programs for ailing companies. Such resolutions are usually standard unless there are clear conflicts of interest among the various parties, shareowners' rights are being negatively affected, or certain groups or shareowners appear to be getting a better deal at the expense of general shareowners. In the case of routine reorganizations of assets or subsidiaries within a group, the primary focus with the proposed changes is to ensure that shareowner value is being preserved, including the effect of the reorganization on the control of group assets, final ownership structure, relative voting power of existing shareowners if the share capital is being adjusted, and the expected benefits arising from the changes. Options are far more limited in the case of a distress restructuring of a company or group as shareowners often have no choice but to approve the restructuring or lose everything. In such cases, the SBA first determines the company's degree of distress by examining whether the company still has a positive net asset value, that is, if realizable assets are greater than liabilities.

In most cases, however, the company has a negative asset value, meaning that shareowners would have nothing left after a liquidation. The SBA seeks to ensure that the degree of dilution proposed is consistent with the claims of outside parties and is commensurate with the relative commitments of other company shareowners. Because ownership of a small percentage of something is worth more than majority ownership of nothing, existing shareowners usually must accept the transfer of majority control over the company to outside secured creditors.

***Approve Special Purpose Acquisition Company (SPAC) Transaction: CASE-BY-CASE***
A SPAC is a pooled investment vehicle designed to invest in private equity type transactions, particularly leveraged buyouts. Although SPACs have been around since the 1990s, they have experienced a recent resurgence since 2003. SPACs are shell companies that have no operations at the time of their initial public offering, but are intended to merge with or acquire other companies. Normally, most if not all of a SPAC's IPO proceeds are held in trust to use to fund future acquisitions. Most SPACs grant shareowners voting rights, in order to approve proposed business combinations. When an acquisition deal is proposed, a shareowner has three options—the shareowner can approve the transaction by voting in favor of it, elect to sell their shares in the open market, or vote against the transaction and redeem their shares for a pro-rata share of the trust account. The assets of the trust are only released if a business combination is approved by the voting shareowners, or a business combination is not consummated within 24 months of the initial offering. This guarantees a minimum liquidation value per share in the event that a business combination is not affected.

Business transactions by SPAC entities have distinct differences when compared to standard M&A transactions:

| **Standard M&A** | **SPAC Merger** |
|---|---|
| **<u>Valuation analysis</u>**<br>· Premium paid for target shares<br>· Fairness opinion – performed by third party<br>· Financials available for both target and the acquirer<br>· Post merger ownership | **<u>Valuation analysis</u>**<br>· Premium is very difficult to calculate as generally the target is a private company<br>· Generally no independent fairness opinion. Most SPACs provide comparable analysis/valuation performed by sponsors.<br>· Financials may be limited as target in a private company<br>· Conversion value – compare conversion price vs. underlying value of the target company/acquirer's current market price |

| | |
|---|---|
| | · Post merger ownership – Usually target shareowners become majority owners of the combined entity. Analysts should evaluate the proportionate value of the combined entity attributable to the SPAC IPO shareowners versus the pre-merger value of SPAC.<br>· Apply private company discount to the target, if it is a private entity |
| **Market reaction**<br>· 1-day reaction and announcement-to date (acquirer)<br>· Stock price – review if trades above offer from announcement to date (public target) | **Market reaction**<br>· 1-day reaction and announcement-to date (SPAC as acquirer)<br>· Stock price – not applicable since target is private |
| **Strategic rationale**<br>· Synergies (cost/revenues) | **Strategic rationale**<br>· Generally no synergies, as SPAC is a shell company with no operations<br>· Charter requirement – mandate is to complete deal in 18-24 months |
| **Negotiations and process**<br>· Strategic process – full auction, partial auction, no auction, or go-shop period<br>· Management track record | **Negotiations and process**<br>· Strategic process – process undertaken to identify potential target companies within specified industry or location specified in charter<br>· Management track record – usually none for the SPAC. Mostly, the management of the target is retained to manage the combined entity<br>· Sponsors' background |
| **Conflicts of interest**<br>· CIC Payments<br>· Post-transaction management positions/ board seats | **Conflicts of interest**<br>· Founding sponsors usually retain 20 percent of the SPAC equity to find a deal. This causes immediate dilution upon consummation of the transaction.<br>· Time frame - deal must get done in an 18-24 month time frame unless an extension is approved by IPO shareowners. Urgency to close deal would increase as it gets closer to the expiration date.<br>· Fairness opinion – usually performed by insiders which could pose a conflict<br>· 80 percent rule – may cause management to pay higher price for the target. |
| **Governance**<br>· Governance structure – better or worse (target) | **Governance**<br>· Usually not applicable |

SPACs may also pursue conversion rights, with distinct differences relative to standard M&A transactions:

| Standard M&A | SPAC Merger |
|---|---|
| **Conversion/Voting Rights**<br>· Appraisal rights – depends on state law<br>· Voting rights – majority, 67 percent, etc. | **Conversion/Voting rights**<br>· Conversion rights – IPO shareowners can request money back if they vote against the transaction or if the SPAC is liquidated<br>· Two-tiered voting thresholds – majority + not more than 20 percent (or another specified number) exercise conversion rights<br>· Some SPAC sponsors enter into voting agreement/tender offer with shareowners that are likely to vote AGAINST the proposed merger. |

The SBA evaluates proposals for SPAC transaction and SPAC conversion rights on a CASE-BY-CASE basis.

***Formation of Holding Company – CASE-BY-CASE***
The SBA evaluates proposals to create a parent holding company on a CASE-BY-CASE basis, considering the following factors:

- The reasons for the change
- Any financial or tax benefits
- Regulatory benefits
- Increases in capital structure
- Changes to the articles of incorporation or bylaws of the company

The SBA will vote AGAINST a proposal to form a holding company should the formation of a holding company result in increases in common or preferred stock in excess of the allowable maximum or result in adverse changes in shareowner rights.

***Approve a "Going Dark" Transaction: CASE-BY-CASE***

Deregistration, or "going-dark,"' transactions occur whereby companies cease SEC reporting but continue to trade publicly. Such transactions are intended to reduce the number of shareowners below 300 and are typically achieved either by a reverse stock split (at a very high ratio with fractional shares resulting from the reverse split being cashed out), by a reverse/forward stock split (with fractional shares resulting from the reverse split being cashed out), or through a cash buyout of shares from shareowners owning less than a designated number of shares (tender offer or odd-lot stock repurchase). Such transactions allow listed companies to de-list from their particular stock exchange and to terminate the registration of their common stock under the Securities & Exchange Act of 1934, so that, among other things, they do not have to comply with the requirements of the Sarbanes-Oxley Act of 2002. Some empirical study indicates that following the enactment of the SOX there was a significant increase in the number of companies going dark, especially among smaller capitalization firms and those with lower quality financial accounting. Furthermore, on average, firms going dark experience significant declines in market value. There is also some evidence that firms may pursue a de-registration in order to protect private control benefits and decrease outside scrutiny and oversight. [71]

Reasons for "going dark" include:

- A company derives no material benefit from its status as a public reporting company;
- The low trading volume in its common stock has not provided significant liquidity to shareowners;
- A company does not expect that it will use its common shares as consideration for acquisitions or other transactions in the foreseeable future and has no present intention of raising capital through a public offering;
- The low trading volume in the common stock results in an inefficient trading market causing substantial spikes in the trading price when actual trades are made;
- The direct and indirect costs of remaining a public company (principally compliance with section 404 of Sarbanes-Oxley) will be unduly burdensome and costly in relation to a company's size;
- The common stock has attracted only limited market research attention and the company has not enjoyed the appreciable enhancement in image that usually results from having listed company status.

The benefits of de-listing and de-registering include:

- Eliminating the costs associated with filing documents under the Exchange Act with the SEC;
- Eliminating the costs of compliance with Sarbanes-Oxley and related regulations;
- Reducing the direct and indirect costs of administering shareowner accounts responding to shareowner requests;
- Affording shareowners who hold fewer than a designated number of shares the opportunity to receive cash for their shares without having to pay brokerage commissions and other transaction costs; and
- Permitting management to focus its time and resources on the company's long-term business goals and objectives.

Some of the disadvantages of de-listing and de-registration include:

- Shareowners owning less than a designated number of shares immediately before the transaction would not have an opportunity to liquidate their shares after the transaction at a time and for a price of their own choosing. Instead, they would be cashed out and would no longer be shareowners and would not have the opportunity to participate in or benefit from any future potential appreciation in the company's value.
- Continuing shareowners would no longer have available all of the information regarding a company's operations and results that is currently available in filings with the SEC.
- Following the transaction, shareowners would no longer be able to trade their securities, except in the pink sheets (if at all) or in privately negotiated transactions; the effect of this may be a significant reduction in liquidity.
- A company may have less flexibility in attracting and retaining executives and other employees because equity-based incentives (such as stock options) tend not to be viewed as having the same value in a non-listed company.
- A company will be less likely to be able to use its common shares to acquire other companies.

***Leveraged Buyout (LBO): CASE-BY-CASE***

A leveraged buyout is a takeover of a company using borrowed funds, normally by management or a group of investors. Most often, the target company's assets serve as security for the loan taken out by the acquiring firm, which repays the loan out of cash flow of the acquired company. The SBA is in favor of LBO's whenever public shareowners receive the customary premium over the current market value of their shares without decimating the target firm's balance sheet.

[71] "Why Do Firms Go Dark? Causes and Economic Consequences of Voluntary SEC Deregistrations," Christian Leuz, Alexander Triantis and Tracy Wang, Finance Working Paper Number 155/2007, European Corporate Governance Institute, March 2008.

***Net Operating Loss Carry-forward (NOL) & Acquisition Restrictions: CASE-BY-CASE***
Companies may seek approval of amendments to their certificate of incorporation intended to restrict certain acquisitions of its common stock in order to preserve net operating loss carry-forwards (or "NOLs"). NOLs can represent a significant asset for the company, one that can be effective at reducing future taxable income. Generally, both the amount and timing of a firm's future taxable income cannot be accurately predicted. Under Section 382 of the Internal Revenue Code of 1986 (the "Code") and other rules promulgated by the IRS, in certain circumstances firms "carry forward" these NOLs to offset any current and future earnings and thus reduce the company's federal income tax liability, subject to certain requirements and restrictions. The benefit comes from offsetting future taxable income dollar-for-dollar by the amount of NOLs, thereby reducing or eliminating the company's taxes on such income.

Section 382 of the Code imposes limitations on the future use of the company's NOLs if the company undergoes an, "ownership change." An ownership change, as defined under Section 382, occurs if one or more shareowners, each of whom owns 5 percent or more of a company's stock, increases its aggregate percentage ownership by more than fifty percentage points over the lowest percentage of stock owned by such shareowner over the preceding 3 year period. All percentage determinations are based on the fair market value of a company's capital stock, including any preferred stock. It is important to recognize that certificate amendment(s) to restrict stock ownership (tied to NOLs) may only be enforceable against shares voted in favor of such amendment(s). Due to this circumcision, shares could be transferred in a manner that would constitute an "ownership change."

Upon an ownership change, the IRS limits the amount of income that NOLs can be offset in any year after the change, regardless of how much income a company earns. If a company experiences an ownership change, the amount of taxable income in any taxable year subsequent to the ownership change that can be offset by NOLs existing prior to such ownership change generally cannot exceed the product of (1) the aggregate value of the company's stock, and (2) the federal long-term tax-exempt rate.

Most certificate amendments restrict any person from transferring common stock if the transfer would result in a shareowner (or a "group" of shareowners under the federal securities laws) owning a certain percentage (e.g. 10 percent) or more of the company's common stock. There are normally no restrictions on stock sales if a shareowner supports such certificate amendments and group thresholds are not triggered. However, there can be convoluted procedural requirements and an impact on liquidity under some circumstances. For example, at some firms, shareowners that violate such NOL based restrictions may not be entitled to any rights, including, without limitation, the right to vote certain shares nor receive dividend payment. Firms often utilize a shareowner rights plan (poison pill) in conjunction with NOL oriented acquisition restrictions.

While stock ownership limitations may allow the company to maximize use of its NOLs to offset future income, they may significantly restrict specific shareowners from increasing their ownership stake in the company. Furthermore, because further purchases of company stock normally requires explicit board approval, such ownership limitations can be viewed as an anti-takeover device. The SBA does not favor ownership limits (or transfer restrictions) for these reasons. However, when firms seek takeover protection in order to solely protect NOLs, a review of the company's control protections and corporate governance structure is conducted and balanced against the financial value of the NOLs (relative to the firm's market capitalization).

***Spinoffs: CASE-BY-CASE***
While evaluating spin-offs or corporate divestitures on a CASE-BY-CASE basis, the SBA takes the following factors into account:

- Tax and regulatory advantages
- Planned use of the sale proceeds
- Valuation of spinoff
- Fairness opinion
- Benefits to the parent company
- Conflicts of interest
- Managerial incentives
- Corporate governance changes
- Changes in the capital structure

***Change of Corporate Form (Germany, Australia, New Zealand): CASE-BY-CASE***
This proposal seeks shareowner approval to convert the company from one corporate form to another. Examples of different corporate forms include: Inc., LLP, PLP, LLC, AG, SE. The SBA generally votes FOR such proposals, unless there are concerns with the motivation or financial impact of a change to firm's corporate structure.

***Other business affecting company participation in tender offers: CASE-BY-CASE***
The SBA considers whether our shareowner interests are promoted or weakened.

**OPERATIONAL ITEMS**

This section contains proposals that address normal operating procedures of the company, most of which are of the "housekeeping" nature. While many of these management proposals do not require shareowner approval, some boards decide to submit them to shareowners for ratification. The list of operational items includes: changing the name of the company, routine bylaw amendments, changes to the date, time, or location of the annual meeting, adjourning the meeting, transacting other business matters, general meeting procedures and formalities.

Operational issues submitted by management will be supported absent compelling factors to the contrary. Due to its broad term, the SBA will always vote against proposals to transact other business as it is in the best interest of shareowners not to give directors such discretion to influence corporate decisions without shareowner approval. Conversely, the SBA will not support proposals to reduce quorum requirements, proposals to suppress shareowners' rights, and proposals to adjourn the meeting of shareowners absent compelling reasons to support such proposals.
While many of these proposals are considered to be routine, they are not inconsequential as fiduciaries remain charged with casting their votes. Furthermore, companies may bundle non-routine items with routine items in an attempt to obtain a more favorable outcome, so the SBA must examine these proposals on a case-by-case basis.

***Adjourn Meeting: CASE-BY-CASE***
The SBA generally votes AGAINST proposals to provide management with the authority to adjourn an annual or special meeting absent compelling reasons to support the proposal.

The SBA votes FOR proposals that relate specifically to soliciting votes for a merger or transaction if supporting that merger or transaction. Additionally, the SBA votes AGAINST proposals if the wording is too vague or if the proposal includes "other business."

***Amend Shareowners' Meeting Quorum Requirements: AGAINST***
The SBA generally votes FOR when requiring a simple majority and AGAINST when requiring a super-majority (except where required by law).

***Amend Technical/ Minor Bylaws or Articles of Association: FOR***
The SBA votes FOR bylaw or charter changes that are of a housekeeping nature (corrections or updates to comply with law/listing requirements).

***Amend Bylaws or Articles of Association (Special): CASE-BY-CASE***
The SBA evaluates resolutions to amend bylaw or articles of association on a CASE-BY-CASE basis, considering the merits of the proposed amendment and its potential impact on shareowner value. When several measures, each of which might be approved on a stand-alone basis, are combined ("bundled") into a single proposal the result may be so restrictive as to warrant opposition.

***Amend Business Objectives Clause in Bylaws or Articles of Association: CASE-BY-CASE***
Proposals to amend corporate purpose are voted on a CASE-BY-CASE basis, considering how the changes in business lines may affect our interests as shareowners.

***Name Change: FOR***
Changing a company's name is a major step that has likely gone through extensive management consideration and/or marketing research. We are generally in favor of these proposals.

***Approve General Meeting Formalities: FOR***
This item would authorize the holder of a copy of the minutes of the shareowners' meeting to accomplish any formalities required by respective market laws.

***Change Proxy Card to Allow for 2-way (Pro/Con) Voting: FOR***
This item allows shareowners to communicate their desires more fully, and it ensures that shareowners may exercise their full voting rights.

***Assign to the Usufructuary (beneficiary), instead of the Trustee, the voting rights appurtenant to shares held in trust: CASE-BY-CASE***
The SBA votes AGAINST if the company assigns voting rights to a foundation allied to management.

***Receive/Approve/Amend Reports and Audited Accounts for Previous Financial Reporting Period(s): CASE-BY-CASE***
Generally, we are in favor of these proposals unless we are aware that there are serious concerns about the accounting principles used or doubts about the integrity of the company's auditor. We support accurate audited financial statements. Additionally, we believe annual audits of a firm's financial statements should be mandatory and carried out by an independent auditor.

***Change Method of Preparing Accounts/Distributing Financial Statements to Shareowners: CASE-BY-CASE***
If the changes have been instituted by a nationwide regulation, they will be approved. Otherwise, they will be carefully scrutinized to ensure they are not damaging to our interests. For instance, managers may seek to reclassify accounts to enhance their perceived performance. If this is the case, then managers may earn more in performance-based compensation without adding actual value to the firm.

***Authorize Directors to Appropriate Reservas Voluntarias (Spain): FOR***

***Authorize Directors to Make Transfers in Reserve Accounts: FOR***

***Adopt/Raise/Lower Stake Disclosure Requirement(s): CASE-BY-CASE***
Generally, we vote in favor of these proposals. Although rare, management proposals may be submitted to conform to recent changes in home market disclosure laws or other regulations. However, proposed levels that are below typical market standards are often only a pretext for an antitakeover defense. Additionally, lower disclosure levels also require a greater number of shareowners to disclose their ownership, causing a greater burden to shareowners and to the company. Positions of more than five percent are significant, however, and this is the standard that the US SEC employs.

***Restrict Inter-shareowner Communications: AGAINST***
The SEC has established enforceable guidelines that restrict shareowners or other parties from communicating with each other for the purposes of soliciting proxies or pursuing corporate takeover measures. Therefore, we do not feel that it is appropriate for a company to burden its shareowners with additional restrictions. Furthermore, dialogue among shareowners assists all shareowners in seeing each shareowner's perspective, which promotes the pursuit of wealth maximization for all shareowners.

***Change Date of Fiscal Year-End: FOR***
Companies routinely seek shareowner approval to change their fiscal year end, a decision best left to management. Most countries require companies to hold their AGM within a certain period of time after the close of the fiscal year. While the SBA typically supports this routine proposal, opposition may be considered in cases where the company is seeking the change solely to postpone its AGM.

***Change of Stock Listing Exchange: FOR***
The SBA believes that voting for a change in stock listing (exchange) may lead to an increase in the value of stock.

***Set or Change Date or Place of Annual Meeting Location: CASE-BY-CASE***
Flexibility is necessary in both time and location of board meetings. As such, the SBA generally votes in favor of proposals that provide balance relating to a shareowner meeting's location.

***Limit Voting Rights: AGAINST***
The SBA supports maximization of shareowners' voting rights at corporations. Any attempts to restrict or impair shareowner-voting rights, such as caps on voting rights, holding period requirement, and restrictions to call special meetings, will be strongly opposed.

***Improve Meeting Reports: FOR***
The SBA believes that meeting reports always have room for improvement. We vote FOR these proposals even though only marginal improvements may be realized.
***Abstention Voting Tabulation (unless required by local law): FOR***

***Tabulating Votes: CASE-BY-CASE***
The SBA supports proposals that allow for independent third parties to examine and tabulate ballots.

***Increase/Decrease Majority Required for Passage of Ordinary Resolutions: AGAINST***
The SBA votes AGAINST increases in majority requirements and FOR decreases (except where required by law).

***Increase/Decrease Majority Required for Passage of Extraordinary Resolution (including requirements for By-law/Article repeal or amendment): AGAINST***
The SBA votes AGAINST increases in majority requirements and FOR decreases (except where required by law).

***Prohibit Solicitation of Shareowner Consents to Action in Lieu of Meeting: AGAINST***

***Establish a Distinction Favoring Nominees/Registered Holders/Beneficial Holders: AGAINST***

***Provide for Equal Treatment of Nominees & Beneficial Holders: FOR***

***Allow Directors to Vote on Matters in Which They Are Interested: CASE-BY-CASE***
Generally, the vote will be AGAINST unless it is shown that the directors' interests are not material or the proposal conforms to federal regulations or stock exchange requirements.

***Allow Directors to Meet Over the Telephone or Via Other Telecommunications Media: CASE-BY-CASE***
***Change/Set Procedure for Calling Board Meetings: FOR***
The SBA embraces full disclosure regarding the procedures for calling board meetings. Therefore, we typically vote FOR improvements in these procedures and the disclosure of these procedures.

***Change Quorum Requirement for Board Meetings: CASE-BY-CASE***

***Transact Other Business: AGAINST***
This item provides a forum for questions and any other resolutions that may be brought up at the meeting. In most countries, the item is a formality and does not require a shareowner vote, but companies in certain countries include other business as a voting item. "Other Business" is such a broad term that it is probably in the best interest of shareowners not to give directors such discretion to influence corporate decisions without shareowner approval. Additionally, because shareowners who vote by proxy cannot know what issues will be raised under this item, the SBA cannot support this request when asked for a vote.

**STATE OF INCORPORATION**

The relative rights and powers of management, shareowners, and other company stakeholders can vary significantly from state to state. A company incorporated in one state is entitled to do business and have its governance provisions respected throughout the country. A corporation having no business contacts or connections in a state may nonetheless choose that state as its place of incorporation and that state's laws as those that determine its internal governance structure. The ability of corporations to choose their legal domicile has led many states to compete for revenue from corporate fees and taxes by enacting management-friendly incorporation codes. Additionally, this competition has encouraged states to support an array of antitakeover devices and wide latitude in restricting the rights of shareowners.

***Control Share Acquisition Provisions: CASE-BY-CASE***
Control share acquisition statutes function by denying shares their voting rights when they contribute to ownership in excess of certain thresholds. Voting rights for those shares exceeding ownership limits may only be restored by approval of either a majority or supermajority of disinterested shares. Thus, control share acquisition statutes effectively require a hostile bidder to put its offer to a shareowner vote or risk voting disenfranchisement if the bidder continues buying up a large block of shares.

The SBA votes FOR proposals to opt out of control share acquisition statutes unless doing so would enable the completion of a takeover that would be detrimental to shareowners. Additionally, the SBA votes FOR proposals to restore voting rights to the control shares.

Conversely, the SBA opposes proposals to amend the charter to include control share acquisition provisions or limit voting rights.

***Control Share Cash-Out Provisions: FOR***
Control share cash-out statutes give dissident shareowners the right to "cash-out" of their position in a company at the expense of the shareowner who has taken a control position. In other words, when an investor crosses a preset threshold level, remaining shareowners are given the right to sell their shares to the acquirer, who must buy them at the highest acquiring price.

The SBA votes FOR proposals to opt out of control share cash-out statutes.

***Disgorgement Provisions: FOR***
Disgorgement provisions require an acquirer or potential acquirer of more than a certain percentage of a company's stock to disgorge (or pay back) to the company any profits realized from the sale of that company's stock purchased 24 months before achieving control status. All sales of company stock by the acquirer occurring within a certain period of time (between 18 months and 24 months) prior to the investor's gaining control status are subject to these recapture-of-profits provisions.

The SBA votes FOR proposals to opt out of state disgorgement provisions.

***Anti-Greenmail: FOR***
Greenmail payments are targeted share repurchases by management of company stock from individuals or groups seeking control of the company. They are one of the most wasteful entrenchment devices available to management. Since only the hostile party receives payment, usually at a substantial premium over the market value of his shares, the practice is discriminatory to all other shareowners of the company. With greenmail, management transfers significant sums of corporate cash, not their own, to one entity for the sole purpose of saving their position and fending off a hostile takeover. This is cash that could be put to use for reinvestment in the company, payment of dividends, or to fund share repurchases, with all shareowners participating on an equal basis.

We vote FOR proposals to adopt anti-greenmail charter or bylaw amendments or otherwise restrict a company's ability to make greenmail payments.

***"Fair Price" and similar provisions in two-tiered tender offers: CASE-BY-CASE***
Votes will be cast FOR management proposals to adopt a fair price provision as long as the shareowners vote requirement embedded in the provisions is no more than a majority of the disinterested shares. The SBA will vote AGAINST all other management fair price proposals. In addition, votes will be cast FOR shareowner proposals to lower the shareowners vote requirement embedded in existing fair price provisions.

***Fair Price Provision: CASE-BY-CASE***
Fair price provisions are a variation on standard supermajority voting requirements for mergers, whereby shareowners vote before a significant business combination can be affected. Fair price provisions add a third option, allowing a bidder to consummate a merger without board approval or a shareowner vote as long as the offer satisfies the price requirements stipulated in the provision. Although the price requirements vary from company to company, the common requirement is that in order to consummate a merger, an offeror must pay minority shareowners at least as much as he/she paid to gain a controlling position in the company. Fair price provisions are normally adopted as amendments to a corporation's charter. The provisions normally include a super-majority lock-in, a clause requiring a super-majority shareowner vote to alter or repeal the provisions itself. We vote FOR management proposals to adopt a fair price provision, as long as the shareowner vote requirement imbedded in the provision is no more than a majority of the disinterested shares. We vote AGAINST all other management fair price provisions and FOR shareowner proposals to lower the shareowner vote requirement imbedded in existing fair price provisions.

***Re-incorporation to a Different State: CASE-BY-CASE***
Corporations may change the state in which they are incorporated as a way of strengthening their defense(s) against unwanted takeovers. Conversely, the move may also be a way of loosening takeover defenses by moving to a state that has lax takeover laws. Many companies changed their state of incorporation to Delaware in the 1980's because they viewed it as having a legal climate favorable to management. In 2007, North Dakota changed its laws of incorporation in an effort to create an environment of corporate governance best practices and strong shareowner rights. The SBA will consider proposals to shift the state of incorporation to North Dakota on a case-by-case basis. The opportunity to increase shareowner rights will be weighed against the costs and potential disruption of changing the state of incorporation. Significant governance shortfalls, such as a board's lack of responsiveness to a majority-supported shareholder proposal, will increase the likelihood of a vote to reincorporate the company in North Dakota. A company with a combination or history of governance shortcomings also suggests the need for an environment of increased shareowner protections.

The SBA considers the conditions of the new jurisdiction versus those of the old jurisdiction, generally supporting proposals that require the company to reincorporate to a state that is more shareowner friendly.[72]

***Offshore Re-Incorporation: CASE-BY-CASE***
The SBA believes that in some circumstances the costs of a corporation's reincorporation may outweigh the benefits, primarily tax and other financial advantages. However, reincorporation can also result in the loss of shareowner rights, financial penalties, future detrimental tax treatment, litigation, or lost business. The SBA evaluates reincorporation proposals on a CASE-BY-CASE basis examining the following:

- Economic costs and benefits of an offshore reincorporation
- Comparison of the company's governance provisions prior to and following the transaction
- Comparison of corporation laws of original and destination locations

***Non-Financial Effects of Merger: CASE-BY-CASE***
Some companies have added provisions to their charters that require or allow their boards of directors to evaluate the impact that a proposed change in control could have on employees, host communities, suppliers and others. Evaluating the impact on non-shareowner constituencies presents a target's board with an explicit basis, approved by the shareowners, which it may invoke to reject a purchase offer that may be attractive in purely financial terms. Some state laws allow corporate directors to consider whether the companies have adopted such a charter or bylaw provision.

***Opt Out of Takeover Law: FOR***
The SBA does not favor corporations opting into state takeover laws (e.g. Delaware). Such laws prohibit an acquirer from making a well-financed bid for a target, which provides a premium to shareowners without decimating the balance sheet.

***Approve Stakeholder Provisions: AGAINST***
Stakeholder laws permit directors, when taking action, to weigh the interests of constituencies other than shareowners, including bondholders, employees, creditors, customers, suppliers, the surrounding community, and even society as a whole, in the process of corporate decision making. In other words, such laws allow directors to consider nearly any factor they deem relevant in discharging their duties, giving directors an excuse for any action that may be detrimental to shareowners.

The SBA votes AGAINST proposals that ask the board to consider non-shareowner constituencies or other nonfinancial effects when evaluating a merger or business combination.

***Exclusive Judicial Forum Provisions: CASE-BY-CASE***

In a March 2010 opinion, the Delaware Court of Chancery provided an opportunity for any Delaware corporation to establish the Court as the exclusive forum for "intra-entity" corporate disputes, such as claims of breach of fiduciary duty. Such claims have been used to overturn directors' business judgments on mergers, and other matters. Early adopters of the exclusive forum provision

[72] Subramanian, Guhan, "The Influence of Antitakeover Statutes on Incorporation Choice: Evidence on the 'Race' Debate and Antitakeover Overreaching." Harvard NOM Research Paper No. 01-10, December 2001.

chose to enact bylaw provisions without seeking shareowner approval. However, the Galaviz v. Berg decision by the U.S. District Court for Northern California provided that Oracle's exclusive forum provision was unenforceable, in part due to Oracle's failure to bring the provision before shareowners. Subsequently, a number of U.S. companies have decided to bring the exclusive forum provision to a shareowner vote and others have amended their charter or by-law provisions.[73] The SBA generally opposes restrictions on shareowner ability to pursue derivative claims and to participate in the selection of appropriate venue. Standard access to the court system is considered to be a fundamental shareowner right. Companies should not attempt to restrict the venue for shareowner claims by adopting charter or bylaw provisions that seek to establish an exclusive judicial forum without shareowner approval. Therefore, the SBA generally votes AGAINST management proposals to establish exclusive forum, and votes FOR shareowner proposals requesting that exclusive forum provisions be approved by shareowners. As with many other voting decisions, the SBA will critically examine the company's rationale for limiting shareowners' rights to legal remedy, including choice of venue, and any material harm that may have been caused by related litigation outside its jurisdiction of incorporation.

**CAPITAL STRUCTURE**

The stewardship of a company's capital structure involves a number of significant issues, including dividend policy, taxes, types of assets, opportunities for growth, ability to finance new projects internally, and the cost of obtaining additional capital. While most of these decisions are best left to company management, many financing decisions have a significant impact on shareowners, particularly when they involve the issuance of additional common stock, preferred stock, or the assumption of additional debt. Additional equity financing, for example, may reduce existing shareowners' interest and can dilute the value of an investment. Additionally, shareowners must be weary of potential anti-takeover mechanisms, which are often embedded in management's chosen financing vehicles.

***Subdivision of capital or stock split (reduce nominal/par value, increase # of shares): FOR***

***Reverse stock split (increase nominal/par value, decrease number of shares): FOR***

***Increase Common Stock: CASE-BY-CASE***
The SBA generally supports common stock increases up to 100 percent of the current number of outstanding shares. We will consider additional increases if management demonstrates a reasonable need. It is important that publicly held corporations have a cushion (i.e., authorization for more shares than what is currently needed) for ordinary business purposes, including raising new capital, funding reasonable executive compensation programs, business acquisitions, and facilitating stock splits and stock dividends. While the SBA recognizes the need for companies to have financial flexibility, these proposals raise two governance issues that should be evaluated. First, the increased share authorization could be used to trigger a company's poison pill. Without enough additional shares to purchase, there is no chance for the rights to be exercised. The second governance issue concerns targeted share placements. In the event of a hostile takeover attempt, a large number of shares could be placed with a white knight (a friendly third party) and defeat a possibly worthwhile offer. The probability of these scenarios is lowered if the board does not have an excess amount of common shares authorized.

***Dual Class Stock Authorization: CASE-BY-CASE***
Companies with dual class voting plans have two or more classes of voting common stock, with each class having a different number of votes per share. Dual class capitalization plans are not anti-takeover measures, per se, but they may help management deter takeovers when management controls the class of stock with higher voting rights. This can be done when management purchases or is awarded the majority of new issues with super voting rights, thereby reducing the total voting power of public shareowners. Recapitalization proposals have often been introduced at family controlled companies to ensure that the family retains control.

Academic literature on the corporate governance of dual class firms has gained significant popularity over the past several years. Studies mainly focus on the impact of dual class share structure on five main elements of firm and market behavior:

i) Agency problems
ii) Firm valuation;
iii) Earnings management
iv) Investment decisions
v) Recapitalization

The following findings provide an overview of the findings in the recent literature.

Bebchuk (2000) examined the relationship between dual class stock and corporate governance from an agency perspective. This analysis showed that the agency costs associated with such structures are higher than the costs associated with controlling shareowners that hold a majority of the cash flow rights in their companies. The authors also found the costs of these structures to be higher than the agency costs of attending highly leveraged capital structures.[74]

[73] Claudia H. Allen, "Deleware Corporations—Can Delaware Forum Selection Clauses in Charters or Bylaws Keep Litigation in the Court of Chancery?," April 18. 2011

Masulis (2006) also contributed to the studies on agency problems, citing that as the divergence between insider voting rights and cash-flow rights widened at dual class companies, corporate holdings were worth less to outside shareowners; CEOs received higher levels of compensation; managers were more likely to make shareowner-value destroying acquisitions, and capital expenditures contributed less to shareowner value.[75] Also in relation to agency issues, Tinaikar (2006) found that the detachment of control rights from cash flow rights in dual class share firms induced lower levels of voluntary disclosure in addition to higher levels of executive compensation.[76]

A study by Claessens (2002) on East Asian firms suggested a correlation between discount valuation and dual class share structure.[77] Drawing from the results of Claessens' findings, several studies examined the implications of dual class shares on firm value in several other markets. In an analysis of a large sample of Western European firms, Bennedsen and Nielsen (2006) found evidence supporting the argument that there is a value discount associated with firms of disproportional ownership structures. Their findings strengthened the causal interpretation that the discount is driven by incentive and entrenchment effects. More importantly, the authors found that firms with dual class shares had a significantly higher value discount than did firms with pyramidal ownership.[78] In a comprehensive study of dual class firms in the U.S., Gompers and Metrick (2008) found that firm value decreased with an increase in insider voting rights.[79] In addition, a 30 year study conducted by Martijn Cremers and Allen Ferrell (2009) found that there is a robust negative association, both economically and statistically meaningful, between poor governance and firm valuation for the period of their study, including the years 1978-2006.[80] Puttonen (2007) found dual class stock to be the "single most important provision contributing to the negative valuation" of Nordic firms.[81]

Dual class shares appear to have a significant impact on earnings management as well. Jiraporn (2005) found that dual class stock exacerbated earnings management by increasing the degree of abnormal accruals by 2.6 percent on average. The increase in abnormal accruals was greater compared to the impact of other takeover defenses such as blank check preferred stock (not significant), poison pills (1.9 percent increase) and classified boards (1.5 percent increase). The results were robust even after controlling for firm size, profitability, financial distress, growth opportunities, and information asymmetry.[82]

Dual class share structures influence investment decisions as well. Li (2007) found that after controlling for other determinants of institutional investment, dual class firms had significantly less institutional ownership than did single class firms. Although institutions of all types hold less of the shares of dual-class shares, this avoidance is more pronounced for long-term investors with strong fiduciary responsibilities than for short-term investors with weak fiduciary duties.[83]

However, not all the literature has negative findings on the impact of dual class share structure on shareowner value. In a study on recapitalization of single class stock to dual class stock, Dimitrov and Jain (2004) found that corporate initiatives for dual class recapitalizations enhance shareowner value. The authors found that shareowners, on average, earned significant positive abnormal returns of 23.11 percent in a period of four years following the announcement of a recapitalization. Abnormal returns were even larger (52.61 percent) for dual class firms that issued equity.[84] One example of a company operating under a dual class share structure is Ford Motor Company, with family control via super voting rights.

***Increase authorized share capital where management is given a general mandate to issue shares up to the limit of authorized capital without seeking specific approval (increase requested without reference to specific business purpose): CASE-BY-CASE***
Increases not exceeding 100 percent of currently authorized capital will generally be supported. We recommend a CASE-BY-CASE review on increases above this limit. For countries where requests are for fixed pools of capital with a specified life, we will approve requests that do not exceed 100 percent of the sum of currently issued capital and authorized, unissued capital. We will consider a larger increase if a need is demonstrated. We will apply a stricter standard if the company has not stated a use for the additional shares or has previously authorized shares still available for issue. Finally, proposals that include shares with unequal voting rights will likely be opposed.

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[74] Bebchuk, Lucian Arye, Kraakman, Reinier H. and Triantis, George G., "Stock Pyramids, Cross-Ownership, and Dual Class Equity: The Creation and Agency Costs of Separating Control from Cash Flow Rights" . As published in CONCENTRATED CORPORATE OWNERSHIP, R. Morck, Ed., pp. 445-460, 2000 Available at SSRN: http://ssrn.com/abstract=147590 or DOI: 10.2139/ssrn.147590.
[75] Masulis, Ronald W., Wang, Cong and Xie, Fei, "Agency Problems at Dual-Class Companies" (November 12, 2006). Available at SSRN: http://ssrn.com/abstract=961158.
[76] Tinaikar, Surjit, "The Voluntary Disclosure Effects of Separating Control Rights from Cash Flow Rights" (November 2006). Available at SSRN: http://ssrn.com/abstract=951547.
[77] Claessens, Stijn & Fan, Joseph P.H. & Lang, Larry, 2002. "The Benefits and Costs of Group Affiliation: Evidence from East Asia," CEPR Discussion Papers 3364, C.E.P.R. Discussion Papers, revised.
[78] Bennedsen, Morten and Nielsen, Kasper Meisner, "The Principle of Proportional Ownership, Investor Protection and Firm Value in Western Europe" (October 2006). ECGI - Finance Working Paper No. 134/2006 Available at SSRN: http://ssrn.com/abstract=941054.
[79] Gompers, Paul A., Ishii, Joy L. and Metrick, Andrew, "Extreme Governance: An Analysis of Dual-Class Companies in the United States" (May 1, 2008). AFA 2005 Philadelphia Meetings Available at SSRN: http://ssrn.com/abstract=562511 or DOI: 10.2139/ssrn.562511.
[80] Cremers, Martijn and Allen Ferrell, "Thirty Years of Corporate Governance: Firms Valuation & Stock Returns" (September 2009). Yale ICF Working Paper No. 09-09. Available at http://ssrn.com/abstract=1279650.
[81] Puttonen, Vesa, Ikaheimo, Seppo and Ratilainen, Tuomas, "External Corporate Governance and Performance - Evidence from the Nordic Countries" (January 30, 2007) Available at SSRN: http://ssrn.com/abstract=960431.
[82] Jiraporn, Pornsit, 2005, "An Empirical Analysis of Corporate Takeover Defenses and Earnings Management: Evidence from the U.S.", Applied financial Economics (University of Warwick, U.K.), Vol. 15, No. 5, pp. 293-303.
[83] Li, Kai, Ortiz-Molina, Hernan and Zhao, Shelly, "Do Voting Rights Affect Institutional Investment Decisions? Evidence from Dual-Class Firms" (November 2007). Available at SSRN: http://ssrn.com/abstract=950295.
[84] Dimitrov, Valentin and Jain, Prem C., "Recapitalization of One Class of Common Stock into Dual-class: Growth and Long-run Stock Returns" (September 1, 2004). Available at SSRN: http://ssrn.com/abstract=422080 or DOI: 10.2139/ssrn.422080.

***Increase authorized share capital when a specific business purpose has been specified: CASE-BY-CASE***
As indicated above, we generally vote FOR increases not exceeding 100 percent. The SBA will generally vote AGAINST increases above this limit if they could be used as an anti-takeover defense.

***Reduce authorized share capital: CASE-BY-CASE***
Proposals to reduce capital can cover a variety of corporate actions, ranging from routine accounting measures to reductions pertaining to a significant corporate restructuring in the face of bankruptcy. In addition, proposals to reduce capital can vary significantly from market to market as a result of local laws and accounting standards. Some examples of capital reduction proposals found overseas (e.g. in Germany and Switzerland) include:

- **Reduction in stated capital:**
  This proposal asks shareowners to allow the board to reduce the company's deficit and create a contributed surplus by effecting a reduction in the state capital of the company's common shares. If net assets are in danger of falling below the aggregate of a company's liabilities and stated capital, some corporate law statutes prohibit the company from paying dividends on its shares. Other proposals seek to cancel any unused capital (e.g. from the treasury, conditional capital or the authorized pool), which are generally deemed to be no longer necessary for covering the company's capital requirements.

- **Reduction in connection with cancellation of repurchased shares:**
  A company may also seek a routine reduction in capital corresponding to the cancellation of shares repurchased in connection with an earlier buyback authorization, as typically seen in Scandinavia, Japan, Spain, and some Latin American markets. In most instances, the amount of equity that may be cancelled is usually limited to ten percent by national law.

- **Reduction in connection with dividend payments:**
  If income is not sufficient to enable the payment of a dividend, the board may propose to lower the par value of the company's shares and pay the difference in par value back to the shareowners, effecting a corresponding reduction in capital. This routine authority does not involve any material change relative to shareowner value as such reduction is normally effected proportionately against all outstanding capital.

- **Reduction in connection with restructuring:**
  Some proposals to reduce capital are sought pursuant to significant corporate restructuring. The SBA generally supports such proposals because opposition could lead to insolvency, which is not in shareowners' interests. Assessment of this type of proposal should take a realistic approach to each company's situation and the future prospects for shareowners.

In all instances, the SBA considers whether the reduction in authorized share capital is for legitimate corporate purposes and not to be used as an anti-takeover tactic.

***Approve General Share Issuance with Preemptive Rights: CASE-BY-CASE***
General issuance requests under both authorized and conditional capital systems allow companies to issue shares to raise funds for general financing purposes. Approval of such requests gives companies sufficient flexibility to carry out ordinary business activities without having to bear the expense of calling shareowner meetings for every issuance. Issuances can be carried out with or without preemptive rights. Preemptive rights permit shareowners to share proportionately in any new issuances of stock, guaranteeing current shareowners the first opportunity to purchase shares of new issuances of stock in the class they own in an amount equal to the percentage of the class they already own. Corporate law in many international countries recognizes preemptive rights and requires shareowner approval for the disapplication of such rights. The SBA generally votes FOR issuance requests with preemptive rights, when the amount of shares requested is less than either the unissued ordinary share capital or one-third of the issued ordinary share capital. The SBA favors issuance authority that is limited to five years and expanded shareowner reporting when the issuance request exceeds one-third of its issued ordinary shares.

In some markets, historical abuse, local regulations, and specific listing requirements may dictate alternative levels of appropriate issuance authority. In Hong Kong, pursuant to corporate law and relevant regulations, a listed company may issue additional shares of up to 20 percent of issued share capital without preemptive rights, and it may issue repurchased shares of up to 10 percent of issued share capital for any purpose in one year, provided that prior shareowners approved the mandate. Further, such issuances may be implemented with a maximum 20 percent discount to the market price, which would dilute the interests of existing shareowners. Most of Hong Kong's listed companies submit two separate issuance proposals at their AGM's: an authority to issue shares without preemptive rights (the "general mandate"), and an authority to issue repurchased shares. The SBA supports these proposals as they allow companies to secure financial flexibility by increasing their levels of equity according to business development and investment needs.

However, the SBA is concerned that boards may abuse these authorities in order to serve their own interests by issuing shares to any party. As a result, any evaluation of these types of proposals takes into account the following elements to determine if there is the possibility that a board may abuse its authorities: (i) the potential for substantial dilution in the company's existing share ownership; (ii) the issue price has been set at a significant discount that is under the maximum legal limit of 20 percent; (iii) the decision-making process regarding the choice of share subscribers; (iv) the possibility for an improper use of the authority; and (v)

the past issuance practices of the company, which may include allocations of a substantial amount of shares to one significant shareowner or third party.

Granting a board with such a high level of discretion over a company's capital may negatively affect shareowners' interests. General mandates for share issuances should be analyzed carefully, and the SBA favors lower maximum limits. Accordingly, we support aggregate maximum limit of additional share issuances up to 20 percent of the company's issued share capital, or 10 percent for the general mandate. And when applicable, the SBA supports discount rates capped at 15 percent of market price. Unless these conditions have been met, and the company has provided a detailed plan for such issuances, the SBA may vote against these types of authorizations.

***Approve General Share Issuance without Preemptive Rights: CASE-BY-CASE***
Companies may need the ability to raise funds for routine business contingencies without the expense of carrying out a rights issue. Such contingencies include, but are not limited to, the facilitating of option plans, small acquisitions, or payment for services. Recognizing that shareowners suffer dilution as a result of issuances without preemptive rights, authorizations should be limited to a fixed number of shares or a percentage of capital at the time of issuance. The SBA generally votes FOR issuance requests without preemptive rights up to a maximum of 20 percent above current levels of issued capital.

***Eliminate Preemptive Rights: AGAINST***
Preemptive rights guarantee existing company shareowners the first opportunity to purchase shares or new issues of company stock in the class they own and in an amount equal to the percentage of the class they already own. While shareowners may choose not to exercise their right, preemptive rights at least ensure that existing shareowners will be able to prevent dilution in their relative ownership position when a company issues more stock if they choose to do so. The SBA is generally AGAINST proposals to eliminate preemptive rights, unless the purpose of the issuance is in shareowners' interests, such as to facilitate an acquisition. Conversely, the SBA votes FOR proposals that direct the adoption of preemptive rights.

***Approve Issue of Ordinary Shares with No/Limited/Restricted Voting Rights: AGAINST***
As stated in this section and in preceding sections, the SBA favors the expansion of shareowner rights. Therefore, we will vote AGAINST any proposal to remove, limit, or restrict shareowner rights.

***Specific Share Issuances: CASE-BY-CASE***
Specific shares issuances may be requested in connection with an acquisition, fund raising, issuance to a private party, etc. The SBA evaluates all specific share issuance requests on a CASE-BY-CASE basis as such requests should be judged on their individual merits.

***Approve Issue of Preferred Shares: CASE-BY-CASE***
"Preferred share" typically refers to a class of stock that provides preferred dividend distributions and preferred liquidation rights as compared to common stock; however, preferred shares typically do not carry voting rights. However, preferred shares may carry voting rights in rare circumstances. Therefore, the SBA reviews proposals to issue preferred shares on an individual basis, considering whether the preferred shares carry voting rights. If the preferred shares do have voting rights, then we will likely vote AGAINST the issuance as this dilutes the SBA's voting position.

Likewise, if a company seeks to *amend* its preferred shares to provide for voting rights, we will typically vote AGAINST such a proposal as well because any new shares with voting rights will dilute the SBA's voting position.

If a company wants to issue preferred shares without voting rights and with no conversion rights to common shares, then the SBA will be more likely to vote FOR such an issuance so long as the company issues the preferred shares for legitimate financial needs and not as a tool to entrench management. Conversely, the SBA will likely vote against preferred shares that provide for conversion to common shares as this may dilute our voting position if the conversion is exercised. Furthermore, preferred shares with conversion rights require that the company reserve a sufficient number of common shares in case all of the preferred shareowners exercise all of their conversion rights.

Blank check preferred stock gives the board of directors the power to issue shares of preferred stock at their discretion, with voting, conversion, distribution, and other rights set by the board at the time of issuance. Blank check preferred stock can be used for sound corporate purposes like raising capital, stock acquisition, employee compensation, or stock splits or dividends. However, blank check preferred stock is also perfectly suited for use as an entrenchment device. The company could find a "white knight," sell the knight a large block of shares, and defeat any possible takeover attempt. With such discretion outside the control of common stock shareowners, the SBA typically votes AGAINST proposals to issue blank check preferred stock.

The SBA will vote on a Case-by-Case basis on the proposal to cancel preferred shares. Of course, our decision on a proposal to cancel preferred shares will depend on the status of the preferred shares. If the preferred shares carry voting rights, rights of conversion, or are unissued "blank check" preferred shares, then the SBA will likely vote FOR cancellation of these preferred shares.

In regards to proposals to issue preferred shares, we consider factors other than the dilution of our voting power. For instance, we will consider financial factors, such as the effect that the preferred issuance will have on market capitalization and earnings per share.

***Restructure/Recapitalize: CASE-BY-CASE***
These proposals deal with the alteration of a corporation's capital structure, such as an exchange of bonds for stock. The SBA is in favor of recapitalizations when our overall investment position is protected during the restructuring process.

***Share Repurchase: CASE-BY-CASE***
When a company repurchases shares, it is generally using retained earnings to purchase stock. This is one form of distributing retained earnings to shareowners. Additionally, companies may have share repurchase arrangements in their stock option grants to employees. If the repurchase of shares is motivated because management feels the stock is undervalued, we are in favor of the proposal. If repurchase is motivated as an anti-takeover maneuver, the SBA is opposed and votes AGAINST the proposal. Determining a company's motivation may be impossible.

Accelerated Share Repurchases (ASR) is another means in which companies may buy back outstanding shares. Pursuant to this method, the company repurchases its shares from an investment bank that borrowed such shares from shareowners. Subsequently, the investment bank will buy back shares of the company from the market to return to the shareowners. The company then cancels any shares that it may receive in addition to the initial amount. Because ASRs reduce the number of issued shares for a fixed cost while transferring the risk to the participating investment bank for a negotiated premium, it represents an effective method for companies to repurchase shares. Unlike an open market buyback, ASRs allow a company to immediately exchange a fixed amount of money for shares of its stock. However, recent academic studies have suggested that this practice may be used by management to manipulate earnings figures for incentive compensation plans and reporting purposes.[85]

Some voting items seek to provide management the authority to use financial derivatives in connection with share repurchase authorizations. In Germany, for example, the law requires that the use of financial derivatives for share repurchase programs be authorized explicitly by shareowners. In some instances, shareowners have been given the opportunity to vote separately on the underlying share repurchase program and the use of derivatives.

***Targeted Share Placement (TSP): CASE-BY-CASE***
The SBA votes FOR shareowner proposals requesting that companies first obtain shareowner authorization before issuing voting stock, warrants, rights or other securities convertible into voting stock, to any person or group, unless the voting rights at stake in the placement represent less than 5 percent of existing voting rights. The SBA is in favor of targeted share placements that do not lower our overall return in a takeover situation. We also support TSPs done on a friendly basis where there is minimal dilution.

***Declare Dividends: FOR***
Declaring a dividend is a very good way to release profits to shareowners. Since it is better to be assured of a return today than at some time in the future, the SBA generally supports dividend declarations unless payout is unreasonably low or the dividends are not covered by reserves and cash flow. Any payouts less than 30 percent for most markets are considered low.

***Approve Appropriation of Profits: CASE-BY-CASE***
Generally, the SBA is in favor unless the payout is unreasonably low or the dividends are not covered by reserves and cash flow.

***Amend Eligibility for Dividends: CASE-BY-CASE***
Attention will be focused on whether the new method is detrimental to our interests.

In addition to the general best practices described above, which are intended for all firms, the Institute of International Finance released its *Final Report of the IIF Committee on Market Best Practices: Principles of Conduct and Best Practice Recommendations – Financial Services Industry Response to the Market Turmoil of 2007-2008* in July 2008.

***Tracking Stock: CASE-BY-CASE***
The SBA closely examines the issuance of tracking stock shares, particularly corporate governance rights attached to those shares. Normally, tracking stock is a separate class of common stock that "tracks" the performance of an individual business of a company. Tracking stock represents an equity claim on the cash flows of the tracked business as opposed to legal ownership of the company's assets. Tracking stock is generally created through a charter amendment and provides for different classes of common stock, subject to shareowner approval. Due to their unique equity structure, we examine closely all of the following issues when determining our support for such proposals: corporate governance features of tracking stock (including voting rights, if any), distribution method (share dividend or initial public offering), conversion terms and structure of stock-option plans tied to tracking stock.

[85] Marquardt, Carol, "Managing EPS Through Accelerated Share Repurchases: Compensation Versus Capital Market Incentives." Baruch College-CUNY, September 2007.

***Establish a requirement that shareowners approve new issues of securities: FOR***

***Establish a percentage limit on capital/number of shares which a single shareowner may own: AGAINST***

***Allow Board to issue additional voting shares without preemptive rights during a public tender offer for shares of the company: AGAINST***

***Approve issue of debt securities convertible into ordinary shares or with warrants to purchase ordinary shares: CASE-BY-CASE***

***Approve issue of bonds, debentures, and other debt instruments: FOR***
Generally, we vote in favor of debt issuance for the purpose of financing future growth and corporate needs. However, there is evidence that firms use debt as a surrogate for sound corporate governance practices.

Debt holds managers accountable for corporate performance because if the company does not perform well financially due to managerial behavior, then the company may not be able to meet its financial obligations. When a firm does not meet its financial obligations, managerial reputation and marketability typically suffers. As such, managers, knowing that their capital structure is built on debt, will be inclined to pursue strategies that lead to the firm's economic growth because they want to meet the financial obligations of the firm, thereby simultaneously protecting their own interests and shareowner interests. A 2009 study by Pornsit Jiraporn, Ph.D., et. al., examined the relationship between firms' capital structure and the quality of their corporate governance mechanisms, and the study confirmed that corporations use debt in place of corporate governance tools.[86] The authors found that firms substituted leverage for corporate governance as a means to overcome agency costs. In other words, the authors stated that firms with poor corporate governance mechanisms were highly leveraged.

While the SBA recognizes the need to employ various tools to minimize agency costs and align management interests with shareowner interests, corporations must not abdicate their corporate governance duties solely by expanding their leverage.

***Authorize conversion of convertible stock or bonds: CASE-BY-CASE***
The SBA considers proposals to convert preferred shares or bonds into common shares on a Case-by-Case basis dependent on the firm's motivations. If the conversion is predicated on a capital restructuring that will improve the firm's overall financial performance, then the SBA will vote FOR such a proposal. Alternatively, if the firm submits a conversion proposal as a defensive tactic to entrench management in the face of a corporate takeover, then the SBA will vote AGAINST such a proposal. Additionally, if the conversion will substantially dilute the appurtenant rights of the company's common stock, then we will likely vote AGAINST such a proposal.

***Set limits on conversion rights of convertible securities: FOR***
The SBA favors limitations on the conversion rights of convertible securities to prevent the dilution of our holdings.

***Modify borrowing limits or debt ceiling: FOR***

***Issue warrants, options (outside of normal Co. compensation plans) or other types of subscription rights: CASE-BY-CASE***

***Approve terms for settlement of debt: CASE-BY-CASE***
Consider whether the proposal is in our interest.

***Modifications to rights appurtenant to or terms of particular classes of securities: CASE-BY-CASE***
The modification must be in the best interest of shareowners. For instance, if a company increases the rights of existing common stock shareowners, then the SBA will vote FOR the modification. Conversely, if the company wishes to grant additional rights to preferred shareowners that would dilute existing share rights, then the SBA will vote AGAINST the modification.

***Transfer of Shares: CASE-BY-CASE***
We will generally vote FOR the repeal or relaxation of restrictions on share transfers and vote AGAINST the tightening of restrictions on share transfer if the transfer may be used to institute or strengthen a takeover defense.

***Approve mechanical change in transferring or recording transfers of securities (no effect on ability to transfer): FOR***
Several countries have already introduced or may introduce electronic clearing systems and the SBA supports these initiatives.

[86] Pornsit Jiraporn, et al, "Does Corporate Governance Affect Capital Structure?" available at http://www.fma.org/Texas/Papers/Capital_Governance_FMA.pdf.

***Authorize Directors to make application for one or more exchange listings for an issue of securities: FOR***
Secondary share listings seek to provide a further funding mechanism through which a company can structure and fund opportunities in a secondary market through enhancement of investors' awareness in such market while increasing share liquidity. The SBA supports this favorable resolution.

***Authorize directors to dispose of fractional entitlements and to retain the proceeds for the benefit of the company: FOR***

***Approve private placement of any type of security: CASE-BY-CASE***
Private placement is a method of raising capital through the sale of securities to a relatively small number of investors rather than a public offering. Investors involved in private placement offerings typically include large banks, mutual funds, insurance companies and pension funds.

Because the private placement is offered to a limited number of investors, detailed financial information is not always disclosed and the need for a prospectus is waived. Moreover, in the United States, the authority does not have to be registered with the Securities and Exchange Commission.

The SBA evaluates private placements on a CASE-BY-CASE basis, voting AGAINST it if the private placement contains extraordinary voting rights or if it may be used in some other way as an anti-takeover defense.

***Approve bonus issue of shares funded by capitalization of reserves, share permits or other account: FOR***
Companies routinely carry out bonus issues of shares or increases in par value to existing shareowners, usually through the capitalization of reserves from either the share premium reserve or the retained earnings account. These issuances essentially function as dividends; however, the distribution of new shares could increase liquidity and marketability, while ultimately expanding the company's shareowner base.

***Approve exchange offer made by company to own holders/for another company/by another company: CASE-BY-CASE***
The SBA will consider short-term gains of accepting the offer versus benefits achievable over the long-term by rejecting the offer.

**International Issues Related to Corporate Structure (India-specific):**
The discovery of financial fraud and corporate governance failings at Satyam Computer Services in 2008 led to increased scrutiny of Indian practices in general. Below is an excerpt of the disclosures recommended in the Confederation of Indian Industry's sample code[87] of corporate conduct:

- A tabular form containing details of each director's remuneration and commission should form a part of the Directors Report, in addition to the usual practice of having it as a note to the profit and loss account.
- Costs incurred, if any, in using the services of a Group Resource Company must be clearly and separately disclosed in the financial statement of the user company.
- A listed company must give certain key information on its divisions or business segments as a part of the Directors Report in the Annual Report. This should encompass (i) the share in total turnover, (ii) review of operations during the year in question, (iii) market conditions, and (iv) future prospects. For the present, the cut-off may be 10 percent of total turnover.
- Where a company has raised funds from the public by issuing shares, debentures or other securities, it would have to give a separate statement showing the end-use of such funds, namely: how much was raised versus the stated and actual project cost; how much has been utilized in the project up to the end of the financial year; and where are the residual funds, if any, invested and in what form. This disclosure would be in the balance sheet of the company as a separate note forming a part of accounts.

**EXECUTIVE COMPENSATION**

Stock-based incentive plans are among the most economically significant matters upon which shareowners are entitled to vote. Because the approval of such plans may result in substantial transfers of shareowner equity out of the company to plan participants as awards vest and are exercised, the terms of such plans must be scrutinized carefully in order to properly align directors' interests with those of shareowners. [88]

The SBA believes that director compensation has two purposes:

- To align the interests of shareowners and directors
- To provide value to directors for value received

[87] Available at: www.nfcgindia.org/desirable_corporate_governance_cii.pdf.
[88] CFA Centre for Financial Market Integrity, "The Compensation of Senior Executives at Listed Companies: A Manual for Investors," 2007.

In meeting these purposes, the following five principles should be used by all companies in setting director compensation.

**Five Principles**

1.1. Director compensation should be determined by a completely independent compensation committee and reviewed by the entire board with complete disclosure and approval by shareowners.

1.2. Director compensation should be aligned with the long-term interest of shareowners.

1.3. Compensation should be used to motivate directors to pursue shareowner interests.

1.4. Directors should be adequately and fairly compensated for their time and effort.

1.5. Director compensation should be approached on an overall basis, rather than as an array of separate elements.

Based on these principles, the National Association of Corporate Directors' Blue Ribbon Commission on Executive Compensation recommends the Best Practices listed below.

**Best Practices**

Boards should effectively:

- Establish a process by which directors can determine the compensation program in a deliberate and objective way.
- Set a substantial target for stock ownership by each director and a time period during which the target is to be met.
- Define a desirable total value of all forms of director compensation.
- Pay directors solely in the form of equity and cash – with equity representing 50 to 100 percent of the total; dismantle the existing benefit programs and avoid creating new ones.
- Adopt a policy stating that a company should not hire a director or a director's firm to provide professional services to the corporation.
- Disclose fully in the proxy statement the philosophy and process used in determining director compensation and the value of all elements of compensation.[89]

Disclosure of target compensation levels, performance metrics, and specific award thresholds should be disclosed to investors. When disclosure is deficient, investors are not able to make efficient proxy voting decisions covering executive compensation matters. Although disclosure surrounding executive compensation has improved dramatically over time, most companies in the U.S. do not provide investors with extensive reporting about their incentive compensation framework. A recent study found, "more than 66 percent of the studied sample did not specify targets or provided ambiguous disclosure. The poor quality of disclosure is more prevalent among small-cap companies, with 72 percent of Russell 3000 companies (excluding the S&P 1,500 constituents) failing to disclose what percentile levels of pay they plan to target, as reported in 2011."[90]

In addition to the best practices above, the Institute of International Finance (IFF) has developed best practices and principles of conduct regarding executive compensation tailored to executives within the financial services industry.[91] The IIF states that financial firms should:

- Base compensation on risk-adjusted performance, and align incentives with shareowner interests and long-term, firm-wide profitability
- Ensure that compensation incentives do not induce risk-taking in excess of the firm's risk appetite
- Align payout with the timing of related risk-adjusted profit
- Take into account realized performance for shareowners over time in determining severance pay
- Make the approach, principles, and objectives of each firm's compensation policies transparent to stakeholders

To accomplish the above goals, IIF states that firms should implement the following practices:

- Structure a significant portion of incentive pay in the form of deferred or equity-related components
- Use risk-adjusted compensation metrics, including adjustment for the cost of capital
- Distinguish an employee's "alpha" value added to profits from advantages provided by the firm (e.g., a low cost of funding)
- Link a more material portion of pay packages to the risk time horizon
- Review policies and performance periodically to maintain alignment of compensation policies with the firm's risk appetite
- Ensure effective management oversight to guard against manipulation and arbitrage of the compensation metrics chosen

[89] Stobaugh, Robert B., "Principles and Best Practices for Director Pay." National Association of Corporate Directors and The Center for Board Leadership, 2006
[90] Institutional Shareholder Services (ISS) Corporate Services, "Executive Pay Through a Peer Benchmarking Lens," July 21, 2011.
[91] *See* IIF, *supra* note 25.

- Make incentives for risk-takers as comparable as possible across firms' business groups.

Several of the policies above incorporate risk assessment as a factor in determining appropriate compensation practices. The financial crisis of 2008 revealed the critical need for risk evaluation as particular incentives are considered. With this in mind, Pearl Meyer & Partners released a list of considerations relevant for companies as they assess risk within the framework of compensation plans[92]:

- What risks could threaten the institution's value?
- Do incentive plan metrics reflect the institution's business strategy?
- Are the leverage and ratio of incentive compensation appropriate?
- Is the full range of upside/downside payouts under the incentive plans understood?
- Do plans have protection/controls to avoid excessive risk-taking?
- Do plans focus executives on long-term performance that aligns with shareholder interests?
- How does performance compare to industry/peers?
- Do the plans allow the Committee to exercise discretion?

The SBA will review the quality of corporate disclosure surrounding the relationship between compensation practices and the company's risk exposure(s), specifically whether or not the company has concluded that compensation practices are reasonably likely to have a material adverse effect on the company.

***Set/Approve Directors' Fees/Compensation: CASE-BY-CASE***
The SBA is generally in favor unless the proposed retainer fees appear out of line with national industry practice in the company's country of incorporation.

***Adopt or Amend Stock Awards and/or Option Plan (U.S.): CASE-BY-CASE***
The SBA supports compensation structures that provide incentives to directors, managers, and other employees by aligning their economic interests with those of the shareowners while simultaneously limiting the transfer of wealth out of the company. Therefore, we evaluate incentive-based compensation plans on the total cost to shareowners and the incentive aspects of the plan.

The SBA uses independent consultants to model these costs and incentives. For plans to provide proper incentives, executive compensation should be linked directly with the performance of the business. The consultants engaged by the SBA have proprietary pay-for-performance models that evaluate compensation of the top five executives at each company, covering both U.S and foreign firms. These proprietary models benchmark the compensation of these executives compared with their performance using three peer groups for each company: an industry peer group, a smaller sector peer group, and a geographic peer group. [94]

A 2005 study found that executives that commit fraud generally have greater financial incentives to do so than executives at similar firms have. Executives are more likely to commit fraud if they are faced with incentives from unrestricted stock holdings; however, they are no more likely to commit fraud if they are faced with incentives from restricted stock and unvested and vested options. Executives who commit fraud tend to exercise larger fractions of their vested options, sell more stock, and receive greater total compensation while committing fraud than executives in similar firms. Additionally, the study found evidence that executives commit corporate fraud following declines in company performance. The authors conclude that governance measures need not be consistent across companies, but rather, the measures should depend on executives' financial incentives, especially after declines in performance, and that restrictions on executives' ability to sell shares could help deter fraud. [95]

Typically, companies also use peer groups when developing compensation packages for their executives. A primary purpose of a peer group is to provide a benchmark against which to determine total direct compensation (TDC). A company's choice of peers can have a significant impact on the ultimate scope and scale of executive compensation. However, these peer groups may be flawed in that the peer groups will be developed to maximize executive compensation regardless of executive performance. In fact, a 2000 study by Bizjak, Lemmon, and Naveen found that the "vast majority" of firms that use peer groups set their executive compensation at or above the fiftieth percentile of the peer group.[96] Issuer-developed peer groups may exhibit the following red flags: 1) too many firms listed (more than 15); 2) bias toward "peers" that are substantially larger and/or more profitable; 3) multiple peer groups with unusually high CEO pay, particularly if not direct competitors; 4) too many industries and geographic markets included; 5) peers that do not compete with the issuer for executive talent; and 6) unexplained year-to-year peer group changes. Such red flags are of concern to investors because of the potential to game the pay-setting process. Firms may select a peer group composed of companies that are of a material size difference, which can substantially inflate compensation benchmarking and may be an indication of weak board oversight. An article from The Conference Board stated that companies selecting top executives at larger companies as peers can boost the 25$^{th}$, 50$^{th}$, and 75$^{th}$ compensation percentiles in a comparison group. These findings are independent of firm performance, thus presenting a compensation benchmark that emphasizes higher-paid executives. A 2007 study also found such peer inflation to be the case, noting that "the selection bias towards highly paid companies in the

[92] For a more extensive discussion, see Pearl Meyer & Partners, *Trends and Issues*, "Top 10 Executive Compensation Issues in the New Economy," 2009.
[94] Moody s Investor Services, "Expanded Disclosure On U.S. Executive Compensation Offers New Clues for Creditors," July 2008.
[95] Johnson, S., Ryan, H.E., Jr., and Tian, Y.S., 2005. Executive Compensation and Corporate Fraud.
[96] Bizjak, M. John, Lemmon, L. Michael, and Naveen, Lalitha. 2000 "Has the Use of Peer Groups Contributed to Higher Pay and Less Efficient Compensation?"

compensation peer groups appears to contribute to the ratcheting of CEO pay over time."[97] The study found that firms chose a median peer with $470 thousand higher total pay than its best-matched unselected peer. Boston University professor Ana Albuquerque found a similar increase in CEO pay due to peer selection. She also concluded that "firms for which the 'peer-pay-effect' reflects higher CEO talent perform better in the future, whereas firms perform worse when it reflects opportunism."[98] A 1999 study by Porac, Wade, and Pollock examined the peer groups that firms use to compare their executive compensation packages. They found that companies usually anchor these peer firms in their own primary industry, but if the industry is doing poor, the firms CEO's are paid excessively, or shareowners are powerful and active, these defined peers could extend beyond the firm's industry.[99] A review done in 2011 of peer groups used by companies in the Standard & Poor's 1500 stock universe found a marginal tendency towards benchmarking against firms that had larger revenues.[100] This may be done to help justify the firm's own executive compensation structure.

To prevent companies from "gaming" the system with their peer groups, governance research firms score companies on their executive compensation practices. For example, with a forced curve and a school letter-grade system, a company's pay-for-performance policies are ranked using fundamental performance measures such as stock returns, earnings-per-share (EPS) growth, return-on-assets (ROA), and return-on-equity (ROE). This information is used to guide voting decisions on each compensation issue as well as to evaluate the compensation committee's performance.

The SBA evaluates equity-based incentive plans using a cost-based analysis. The potential cost of an equity plan is expressed in terms of shareowner value transfer (SVT), which is measured using a binomial model that assesses the amount of shareowners' equity that will flow out of the company to participants either as options are exercised or restrictions on awards lapse.

When analyzing the potential cost of a new plan or an amendment to add shares to an existing plan, the SBA estimates the potential total cost of a company's equity compensation program, including: (1) new shares being reserved, (2) shares available under all existing equity compensation plans, and (3) shares subject to outstanding awards (or "overhang"). Note that, for purposes of the binomial model, new shares, available shares, and shares underlying outstanding grants are referred to as A, B, and C shares, respectively, in our analyses. SVT is expressed in dollar terms and as a percentage of the company's market value. As part of the evaluation protocol for determining a vote decision on a plan proposal, the total potential cost (SVT) of all a company's equity-based incentive plans is compared to a company-specific cap that is both industry - and performance-based.

A company's SVT is fueled by three elements - its current share request, plus the number of shares previously reserved under its equity plans that have not yet been granted, plus the number of shares that have been granted and not yet exercised or (in the case of full-value awards) vested.

The SBA's current approach provides an unbiased dollar cost estimate of a company's equity compensation program. If the potential cost of the equity compensation program exceeds the company-specific allowable cap, the SBA generally votes against the equity plan proposal because it is too costly for shareowners.

Companies with sustained positive stock performance may exhibit high SVT costs attributable to overhang if option holders retain their options for prolonged periods. Such a combination likely reflects employees' confidence in their company's future prospects. However, the SBA may vote against a new share request due to excessive cost that is driven primarily by overhang. Although positive stock performance will typically result in a higher allowable cap for a company, the high cost of overhang may still represent a significant component of SVT. In addition, although most full-value awards (such as time-based restricted shares) fully vest after no more than three or five years, most stock options are granted with 10-year terms, and thus may impact overhang for a longer period than full-value awards if not exercised within five years after they are granted.

Beginning in 2008, the SBA incorporated a case-by-case policy in situations where a company keeps its employees and the employees keep the options. Such a case may represent successful retention of employees, who have a positive outlook on the future performance of the company. This approach involves an evaluation of companies with excessive SVT cost. For these companies, we would examine the company's: (1) performance, (2) overhang, (3) dilution attributable to equity compensation, and (4) overall compensation practices. For companies with excessive SVT cost, the SBA would consider, on a case-by-case basis, a carve-out of a portion of cost attributable to overhang, considering the following criteria:

1. **Stock performance:**
   A company with sustained positive stock performance will merit greater scrutiny. Five-year total shareowner return (TSR), year over year performance, and peer performance could play a significant role in this determination

2. **Overhang and exercise behavior:**
   We would assess whether optionees have held in-the-money options for a prolonged period (thus reflecting their

[97] Faulkender, Michael W. and Yang, Jun, "Inside the Black Box: The Role and Composition of Compensation Peer Groups," (March 15, 2007). AFA 2008 New Orleans Meetings Paper.
[98] Albuquerque, Ana M., De Franco, Gus and Verdi, Rodrigo S., "Peer Choice in CEO Compensation," (July 21, 2009). Available at SSRN: http://ssrn.com/abstract=1362047.
[99] Porac, F. Joseph, Wade, B. James, and Pollock, Tim. 1999 "Industry Categories and the Politics of the Comparable Firm in CEO Compensation."

[100] Equilar, Inc., "2011 S&P 1500 Peer Group Report—An Analysis of Peer Groups at S&P 1500 Companies."

confidence in the prospects of the company). Note that this factor would require detailed disclosure regarding a company's overhang, such as tranches of all outstanding grants with corresponding exercise prices, vesting provisions, terms, forfeiture rates, and their distribution with respect to the employee base. We also consider the dividend payment policy on unvested stock and whether, if paid, such dividends are recouped by the company in the event the stock does not vest.

3. **New share request**:
We would evaluate the new share request and calculate the expected duration of the request in addition to the shares currently available under the equity compensation program, based on the company's three-year average burn rate (or a burn-rate commitment that the company makes for future years). For example, an expected duration in excess of five years could be considered problematic.

4. **Overall compensation practices**:
An evaluation of overall practices could include: (1) stock option repricing provisions, (2) liberal share recycling provisions, (3) evergreen provisions, (4) high concentration ratios (of grants to top executives), or (5) additional practices outlined in the independent consultant's current poor pay practices policy.

In addition to these performance and cost calculations, the SBA uses a set of guiding principles to make voting decisions on compensation plans.

The board committee should have discretion to tailor plans to fit individual and company needs at any point in the life of the plans. However, shareowners also need safeguards against possible misuse of plan structures. To avoid conflicts of interest, insiders and affiliated directors should not sit on the board's compensation committee. Additionally, the SBA typically votes against plans which do not limit individual plan dilution levels to a range of 3 percent to 5 percent of a company's outstanding common stock, and simultaneously do not limit the total dilution resulting from all plans to a range of 6 percent to 10 percent of outstanding common stock.

Stock-based incentive plans should require some financial sacrifice and/or risk. Plans that include only restricted stock or other forms of outright grants should be kept to minimal levels due to their higher costs and decreased incentive elements. While each plan is judged primarily on cost and how well the plan will align the goals of management with those of shareowners, the SBA typically votes against plans that permit unrestricted stock or time-lapsing restricted stock awards that fully vest in less than 4 years. When plans include provisions like cashless exercise, no particular strike price, evergreen provisions, payment of dividends on unvested shares, and repricing ability, and the extent to which a plan can effectively align the interests of management is mitigated. Some financial risk on the part of the option holder is important to efficiently achieve this goal.

Option repricing is a serious detriment to the incentive aspect of these plans. If the company has a history of repricing underwater options, or if the plan specifically permits this practice, the plan is doubtful to meet the standards required under the consultant's model. There are very rare instances where repricing is acceptable, but several strict conditions must be met including a dramatic decline in stock value due to serious macroeconomic or industry-wide concerns and the necessity to reprice options in order to retain and motivate employees.

The voting decision of the SBA will take into account any other factors relevant in determining whether a proposed plan is a reasonable way to achieve the ultimate goal of maximizing shareowner value.

***Adopt/Amend Executive or Employee Stock Option Plan (International): CASE-BY-CASE***

The SBA supports stock option plans, which provide incentives to directors, managers, and other employees by aligning their economic interests with those of the shareowners while limiting the transfer of wealth out of the company. Option plan evaluations are therefore based on the total cost to shareowners and give effect to the incentive aspects of the plan. Specific analysis includes all of the following:

- exercise price (should be >= 100% market price of shares);
- total dilution (should be <= 10% of fully-diluted issued capital);
- the plan is to have a disinterested administrator; and
- "repricing" of underwater options is prohibited.

If total dilution exceeds 10 percent, special consideration will be given towards industry practice within the specific foreign capital market, the company's performance relative to its industry, and percentage of stock options awarded to top executives. If proxy disclosure is inadequate to gauge certain aspects of compensation plans, we are not likely to support these option plans.

***Adopt Bonus 162(m) Plan (US): CASE-BY-CASE***
The SBA reviews proposals to adopt performance-based cash bonus plans for executives on a case-by-case basis. These plans are put to a shareowner vote to preserve the tax deductibility of compensation in excess of $1 million for the five most highly compensated

executives, pursuant to section 162(m) of the Internal Revenue Code. A vote against these plans does not prevent the bonus from being paid, but only precludes the ability to take a tax deduction.[101] As such, the SBA generally favors these proposals but will vote against them when executive compensation is egregious as evidenced by one or more of the following: a gross misalignment of pay and performance, lack of defined performance criteria, or no or excessively high maximum payout.

***Authorize Allotment of Share Options to Director(s) Pursuant to an Approved Stock Option Plan: FOR***

***Authorize Directors to grant stock options to executives or staff of the company or its affiliates (where further information is not known): AGAINST***

***Authorize Employee Stock Ownership Plans (ESOP's): FOR***
Generally vote in favor using similar criteria for stock option plans (i.e. dilution parameters, plan features, etc.)

***Establish a requirement that shareowners approve severance pay or other special compensation to company officers or directors: FOR***

***Ratify or renew management/profit-sharing contract with other companies (in which the company retains or gains management control over the other): FOR***

***Cancel management/profit-sharing contracts with other companies: FOR***

***Establish a requirement that directors hold shares in the company: FOR***
We encourage stock ownership by directors and believe directors should own an equity interest in the companies upon which boards they are members. However, we do not currently support any type of minimum or absolute ownership levels (e.g. 10,000 shares of stock, $25,000 of stock, etc.).

***Authorize (Revoke Appropriation) Directors to Set Retirement Payment for Retiring Director(s): CASE-BY-CASE***
We favor this management proposal only if it clearly states that it affects employee directors. If it is not clear who will be affected by the proposal, we vote AGAINST it.

***Approve Retirement Bonus for Directors (Japan): CASE-BY-CASE***
The SBA votes on proposals to approve retirement bonus for directors on a CASE-BY-CASE basis. We treat such payouts as routine resolutions provided that retirees have been executives of the company. However, the SBA opposes payment of retirement bonuses to outside directors as the appointment of affiliated parties as directors, and their subsequent retirement with full benefits, continues to be a problem in Japan. Because this practice transforms key oversight positions into a form of reward to friends and affiliates of management, this is a highly unacceptable practice and a wasteful use of shareowners' funds. Due to the limited level of disclosure provided in Japanese proxies describing the way these payments are calculated, shareowners are not able to assess the true merits of such rewards. As such, the SBA will vote against this resolution when one or more of the individuals to whom the grants are being proposed have been designated as an outsider particularly because the size of these payments is left at the board's discretion.

***Approve Deep Discount Stock Option Plan (Japan): CASE-BY-CASE***
Deep discount stock option plans act like restricted stock plans, which are not allowed in Japan. The exercise price of the options is set at JY 1 per share, but the recipient is usually not allowed to exercise the options until retirement. These plans are most often adopted as a substitute for the retirement bonus system, and are an explicit attempt to link director compensation with share price performance. Because companies typically seek to reserve very modest size of grants, the SBA is not concerned with dilutive effects associated with such plans. However, when the options may be exercised prior to retirement, with no disclosure of performance hurdles which must be met, or when the conditions for exercise are not clearly specified, the SBA will oppose the resolution. A near-zero exercise price means that grantees do not bear the same downside risks as shareowners who purchase their shares at market price, thereby weakening the alignment of grantees' interests with those of ordinary shareowners.

***Set/Amend Exercise Delay (European style options): CASE-BY-CASE***

***Adopt Compensation Scheme: CASE-BY-CASE***
Consider the appropriateness of the compensation scheme.

***Approve amendments to employee profit sharing plan: CASE-BY-CASE***
Consider potential dilution as compared to potential productivity increases.

***Option Exchange Programs/Repricing Options: CASE-BY-CASE***
While the SBA is strongly opposed to the repricing of stock options, there are very rare instances where we may accept repricing. In such scenarios, the SBA will evaluate such proposals on a CASE-BY-CASE basis, considering:

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[101] "Section 162(m) Requirements, Implications and Practical Concerns," Exequity, September 2008.

- Presence of a dramatic decline in stock value attributed to serious macroeconomic or industry-wide concerns
- Necessity to reprice options in order to retain and motivate employees
- Historic trading patterns, i.e. the stock price should not be so volatile that the options are likely to be back "in-the-money" over the near term
- Rationale for the re-pricing, e.g., was the stock price decline beyond management's control?
- Value of exchange for the company and shareowners
- Plan for surrendered options, e.g., placed in reserve, etc.
- Option vesting, e.g., does the new option vest immediately or is there a black-out period?
- Term of the option, i.e. the term should remain the same as that of the replaced option
- Exercise price, i.e. should be set at fair market or a premium to market
- Participants, i.e. executive officers and directors should be excluded.

If the surrendered options are added back to the equity plans for re-issuance, then we also take into consideration the company's three-year average burn rate.

In addition to the above considerations, we evaluate the intent, rationale, and timing of the repricing proposal. The proposal should clearly articulate why the board is choosing to conduct an exchange program at this point in time. Repricing underwater options after a recent precipitous drop in the company's stock price demonstrates poor timing. Repricing after a recent decline in stock price triggers additional scrutiny and a potential AGAINST vote on the proposal. At a minimum, the decline should not have happened within the past year. Also, we consider the terms of the surrendered options, such as the grant date, exercise price, and vesting schedule. Grant dates of surrendered options should be far enough back, at least two to three years, so as not to suggest that repricings are being done to take advantage of short-term downward price movements. Similarly, the exercise price of surrendered options should be above the 52-week high for the stock price. The SBA is likely to vote against members of the compensation committee when the company repriced options or completed a self tender offer without shareowner approval.

A study of option exchanges made between 2004 and 2009 analyzed the client recommendations of the largest U.S. proxy advisor and their impact on subsequent firm performance.[102] The study's researchers observed a positive stock price reaction to exchange offers, suggesting that shareowners view these proposals as value increasing. The study found the stock price reaction to be significantly less positive when the exchange exhibited certain features favored by a major proxy advisor, including shareowner approval.

The SBA votes FOR shareowner proposals to put option repricings to a shareowner vote.

***Options Backdating: AGAINST***

Options backdating has had serious implications for companies and shareowners, resulting in financial restatements, the de-listing of companies, and the termination of executives. According to an ISS study on the stock option timing scandal, option timing has allowed some executives to prosper without building long-term shareowner value. In addition, many investors view option -timing as stealing from corporate coffers, especially since many companies expend cash on stock buybacks to counteract the dilutive impact of their executives' option profits.[103]

As of November 2007, more than 220 U.S. companies had announced internal or regulatory investigations related to their stock option practices. The revelation of backdating results in an average loss to shareowners of about 8 percent. This translates to about $500 million per firm. By contrast, the authors estimated that the average potential gain from backdating to all executives in these firms is under $600,000 per firm annually.[104]

Since the passage of the Sarbanes-Oxley Act in 2002, companies have been required to report option grants within two business days. While this rule change has made it more difficult for companies to manipulate grant dates, a significant number of firms have missed these deadlines, raising concerns among some investors that option-timing is still occurring.

A 2005 empirical study on the timing of CEO stock option awards found that abnormal stock returns are negative before the award dates and positive afterwards, and the returns around unscheduled awards appear to have intensified over time, suggesting that executives have gradually learned how to better time awards to their advantage or become more aggressive in their timing efforts.[105]

According to an academic study, backdating can be curtailed in several ways. For instance, if the two-day reporting is strictly enforced, it will substantially reduce the scope of backdating. In 2006, more than 20 percent of the option awards were reported late, with about 10 percent more than one month late. The study empirically found that managers can gain significant economic benefits from grant manipulations both via back- and forward-dating of stock options.[106]

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[102] David F. Larcker, Allan L. McCall, and Gaizka Ormazabal, "Proxy Advisory Firms and Stock Option Exchanges: The Case of Institutional Shareholder Services," Stanford Rock Center for Corporate Governance at Stanford University working paper No. 100 (April 15 2011).
[103] ISS, 2006, "An Investor Guide to the Stock Option Timing Scandal."
[104] Narayanan, M.P., Schipani, Cindy A. and Seyhun, Hasan Nejat, "The Economic Impact of Backdating of Executive Stock Options." Michigan Law Review, 2006.
[105] Lie, Erik, 2005, "On the Timing of CEO Stock Option Awards", *Management Science*, Volume 51, No. 5, May 2005, pp. 802-812.
[106] Narayanan, M.P and H. Nejat Seyhun, 2006, "The Dating Game: Do Managers Designate Option Grant Dates to Increase Their Compensaion?"

Another academic paper on stock options grants manipulation found that approximately 18.9 percent of grants between 1996 and 2005 have been backdated or manipulated in some fashion. These fractions is highest for unscheduled, at-the-money grants and among firms that are small, operate in the tech sector, and have high stock price volatility. In addition, firms that use smaller auditing firms, i.e. firms outside the Big Four, are more likely to file their grants late. The incidence of backdating was more than halved as a result of the two-day filing requirement that took effect in 2002, but it remains high for grants that are filed late. At the firm level, the authors of the study estimated that 29.2 percent of firms manipulated grants to top executives at some point between 1996 and 2005.[107]

A study by Goldman Sachs found that the stock prices of many companies that have publicly announced investigations into option granting practices have moved notably lower after such announcements. The study revealed that stock underperformance occurs even though stock option backdating may not necessarily be illegal if conducted in accordance with the company's compensation plan, properly disclosed, and properly accounted for.[108]

Furthermore, according to a CRS Report for Congress on the backdating of stock options, while corporate executives appear to have profited handsomely from undisclosed backdating, there is, potentially, a significant cost to shareowners. Companies that have backdated their stock options may face costs from earnings hits, reduced executive performance, delisting, actions of bondholders, additional taxes, and probes, fines, and lawsuits; all of these costs can deteriorate shareowner value.[109]

In cases where a company has practiced options backdating, the SBA votes AGAINST or WITHHOLD on a CASE-BY-CASE basis when voting on the members of the compensation committee. Our vote depends on the severity of the practices and the subsequent corrective actions on the part of the board. We vote AGAINST or WITHHOLD from the compensation committee members who oversaw the questionable options grant practices or from current compensation committee members who fail to respond to the issue proactively, depending on several factors, including, but not limited to:

- Reason and motive for the options backdating issue, such as inadvertent vs. deliberate grant date changes
- Length of time of options backdating
- Size of restatement due to options backdating
- Corrective actions taken by the board or compensation committee, such as canceling or repricing backdated options, or recoupment of option gains on backdated grants
- Adoption of a grant policy that prohibits backdating, and creation of a fixed grant schedule or window period for equity grants going forward.

An ISS study on the stock option timing scandal found that the option-timing scandal calls into question the oversight provided by boards and compensation committee members at these companies. When a compensation committee fails to perform its fiduciary responsibilities and provide adequate oversight of the executive pay policies and process, shareowners eventually suffer.[110]

***Adopt or Amend Employee Stock Purchase Plan: CASE-BY-CASE***

Employee stock purchase plans (ESPP) are normally broad-based equity plans that allow employees to purchase stock via regular payroll deductions, often at a reduced price. Equity-based compensation can be a useful tool in aligning the interests of management and employees with those of the shareowners. ESPPs provide low cost financing for corporate stock and can improve employee productivity, both of which should, in theory, lead to increased shareowner value. Numerous studies favorably link ESPPs with improved corporate performance.[111] To avoid incurring an expense under Financial Accounting Standard 123R, companies must offer a non-compensatory ESPP. The SBA uses a set of criteria to evaluate ballot items. These criteria include the presence of evergreen provisions, opt-out features, reset features, purchase limits, pay deductions, matching contributions, holding requirements, and tax deductibility. The SBA generally supports ESPP proposals that pass the criteria of a consultant's model based on the size and cost of the plan, as well as the company's overall use of equity compensation. The combined cost of the ESPP plus any other equity-based compensation plans is compared to the average level of the company's peers and several absolute limits, in the same fashion as detailed in the above section, "Adopt or Amend Stock Awards and/or Options Plan". The plan is generally accepted if the combined amount of equity used across all programs is deemed reasonable.

***Restrict Executive Pay: CASE-BY-CASE***

The SBA supports levels of compensation that are consistent with our goal of aligning management's interests with shareowners' interests. Generally, the SBA believes that shareowners should not be involved in setting or limiting the absolute level of executive compensation, which is a matter for the compensation committee to determine, and if a problem arises with respect to executive pay, providing or withholding support of the individual compensation committee members is the appropriate recourse. Absolute limits that may or may not be tied to certain criteria may inhibit the compensation committee's ability to fulfill its duties, particularly for companies that have a track record of reasonable compensation. When the company's executive compensation and performance have been in line with that of peers, there is no justification for shareowners to require an arbitrary cap.

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[107] Heron, Randall A. and Erik Lie, 2006, "What Fraction of Stock Option Grants to Top Executives have been Backdated or Manipulated?"
[108] Goldman Sachs Group, 2006, "ESO Backdating – What a Mess!"
[109] Congressional Research Services, 2007, "Stock Options: The Backdating Issue."
[110] ISS, 2006, "An Investor Guide to the Stock Option Timing Scandal."
[111] 2006 Employee Stock Purchase Plan Report, Equilar, Inc., 2006.

***Disclosure of Executive Compensation: CASE-BY-CASE***
It is important that shareowners have the opportunity to review all elements of compensation to senior officials in order to evaluate the performance of the board, specifically the compensation committee, in monitoring management. Proposals for more detail will be evaluated based on the depth of the disclosure required.

***Executive Severance Agreements or Golden Parachutes: CASE-BY-CASE***
Pursuant to final rules adopted by the SEC in early 2011 and as part of their annual general meetings, companies are required to provide shareowners with advisory (non-binding) votes on golden parachute packages in the event of mergers or acquisitions (M&A). Golden parachute disclosure is required only for executive compensation that is based on or otherwise relates to the applicable M&A transaction(s). Golden parachute disclosure is required to be provided in both tabular and narrative formats, and must include all arrangements whether or not they discriminate in scope, terms or operation in favor of executive officers, and without a *de minimis* exception of any kind. Agreements or understandings between the acquirer and the named executive officers of the target firm are required to be disclosed to investors, but are not subject to the say-on-golden parachute vote. Golden parachute votes are only required in transactional filings where shareowners are being asked to approve the transaction. Importantly, companies are not required to conduct say-on-golden parachute votes if the golden parachute arrangements have already been voted upon in an annual say-on-pay vote and have not been modified in order to increase the size of the benefit since such prior vote.

Since shareowners may not be afforded the opportunity to vote on the adoption of a golden parachute itself, the SBA will consider voting against compensation committee members for approving the adoption of excessive or egregious golden parachutes such as those with payouts exceeding 2.99 times salary plus bonus and those that would be paid in addition to contractual severance payments. The SBA will also consider voting against compensation committee members for approving the adoption of "tin parachutes," which are paid to a broad class of employees and serve as a takeover deterrent.

Golden parachutes are a special kind of employment contract for directors, officers, and other key employees. This change in control ("CIC") [112] severance package typically includes a continuation of the individual's base salary for two to three years or a lump sum payment valued at two to three times the base salary rate, plus retirement and other benefits guaranteed in the contract following termination. In some cases, these periods and multiples can be significantly longer than three years and greater than three times. Golden parachutes do not include certain types of compensation that are deemed not related to the transaction, such as previously vested equity awards, deferred compensation and compensation from *bona fide* post-transaction employment agreements. Provisions have been outlined in the Internal Revenue Code to try to curb excessive parachute payments. This provision calls for a 20 percent excise tax to be levied on excess parachute payments. Unfortunately, it has had the opposite affect and has caused companies to gross-up the parachute payments to executives. According to an analysis by the RiskMetrics Group, 66.2 percent of companies would provide excise tax gross-ups to executives in connection with a change in control. [113] The SBA supports initiatives to reduce the time frame of severance agreements, to tie them to executive performance, and for outside executives, to sunset agreements after an initial "honeymoon" period. The SBA also supports and votes FOR shareowner proposals requiring shareowner ratification of golden parachutes unless the proposal requires shareowner approval prior to entering into employment contracts. Shareowners should allow the compensation committee to set benefit levels, provided that shareowner approval is sought when benefits will exceed 2.99 times salary plus bonus to allow for tax advantages.

Similarly, the SBA believes that there are certain criteria that can be included in severance agreements that would prevent excessive and undue compensation from being awarded. Specifically, severance agreements should be structured so that executives are not awarded full payments in the event of poor performance. Executive compensation should be based on a solid foundation of pay for performance, and if an executive has not performed, severance packages should afford the company leniency to reduce payouts. Companies should not be required to pay for work that has not been performed. Further, executives should not receive severance payments under a broad executive plan if they are also eligible for severance payments under their employment contract. A double trigger standard for severance payouts to executives following a change in control event is fast evolving into a governance best practice. Advocates of a double trigger argue that companies that enter into severance (golden parachute) agreements that allow for payments to departing senior executives upon a change in control, should be subject to a double trigger that makes payouts contingent upon both a) an actual change in control and b) the termination of an executive (or a substantial diminution of the executive's duties). The proponents of the proposal also argue that by allowing the accelerated vesting of equity awards or the easing of restrictions on stock upon a change in control, departing executives receive windfalls from awards that may not vest for several additional years and that such unearned payouts have no real benefit to shareowners as they are not aligned with the principle of pay for performance. The SBA supports the adoption of compensation policies that require any future senior executive severance agreements that provide for payments made upon a change in control to be double triggered and not allow for accelerated vesting of unvested equity awards.

***Posthumous Executive Compensation or Golden Coffins: CASE-BY-CASE***
Some executives may receive provision for severance packages, vested shares, salary, bonuses, perquisites and pension benefits even after death. [114] Most public companies include death benefits with other types of termination-related pay due their CEOs, with

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[112] Within employment agreements and executive compensation plans, a CIC is typically defined as an occurrence of one or more of the following: 1) a certain percentage of the company s stock is acquired outright (or via a merger); 2) a sale of all or a substantial amount of the company s assets; 3) a liquidation of the company; or 4) a certain percentage of the board of directors is replaced. CIC s are also defined in the tax code within IRC Section 280G and 490A.
[113] "Gilding Golden Parachutes, The Impact of Excise Tax Gross-Ups" RiskMetrics Group November 2008.
[114] "Companies Promise CEOs Lavish Posthumous Paydays," Wall Street Journal, June 10, 2008.

variations for whether the person is fired, becomes disabled or dies in office. Death benefits may be layered on top of pensions, vested stock awards and deferred compensation, which for most CEOs already amount to large sums. Though not all companies provide it, the most common posthumous benefit is acceleration of unvested stock options and grants of restricted stock—accelerated vesting provisions are not supported by SBA proxy voting guidelines. According to compensation consultant Equilar, as of 2006, 17.2 percent of Fortune 100 companies disclosed that their CEO is entitled to receive death benefits. Death benefits are defined as termination payments triggered by death. Typically, these payments are structured in a similar fashion to severance and change-in-control benefits where basic payments are set as a multiple of base salary and/or bonus. Death benefits structured in this manner may be a form of poison pill (anti-takeover device), and are likely to result in compensation levels that contradict performance. Companies often claim that pay packages that include death benefits are designed for executive retention, but death clearly severs any retention rationale. Because golden coffin provisions may pay out significant long-term compensation that is unrelated to performance after the death of the executive, the SBA supports their removal from compensation frameworks at any firm that does not provide similar benefits to its other managers or does not require such compensation to be approved by shareowners.

***Link Executive Compensation to Social Performance: CASE-BY-CASE***
These types of resolutions ask companies to compensate executives on the basis of their progress on various social issues. Generally, the SBA does not support such proposals. While it is important for corporations to be socially responsible and ethical, shareowners should not enforce a social mandate through the manipulation of compensation levels. Shareowners have the right to address any social issue on an individual basis with their companies. The SBA believes executives should be compensated based on numerous factors and that linking pay matters with social issues is generally inappropriate.

***Link Pay to Performance: CASE-BY-CASE***
The SBA supports executive compensation plans that align management interests with those of shareowners and reward executives based on good long-term performance. The SBA generally endorses shareowner proposals advocating the use of performance-based equity awards (e.g., indexed options, premium-priced options and performance-vested awards), unless the proposal is overly restrictive (e.g., all awards to top executives must be structured in a certain way, such as only in the form of indexed options). Some advocates, largely in response to compensation requirements tied to the Troubled Asset Relief Program (TARP) and Capital Purchase Program (CPP) of the Economic Emergency Stabilization Act of 2008, have proposed various reporting and award restrictions to executive compensation practices. Some investors may urge board of directors to adopt more rigorous executive compensation reforms in order to improve the pay-for-performance features of the companies' plans and help restore investor confidence, stipulating the benefits afforded to companies participating in the TARP program justify these more demanding executive compensation reforms. Ken Hugessen, an expert on executive compensation, proposes evaluating compensation packages by comparing the total compensation relative to other executives, financial performance, and other companies along several dimensions, including total shareowner return, company growth, returns, and profits.[115]

A 2005 study investigated the link between CEO pay and skill, defined as the ability to continue positive company performance and reverse poor performance. For small firms, the link was found to be strong when the CEO receives high incentive pay, when there was a large monitoring shareowner, and when environmental constraints on managerial decisions were absent; for large firms, there is no such evidence. The study also found that the performance of firms that experienced CEO turnover was related to differences in pay between the departing CEO and the incoming CEO. If the compensation package has a high incentive component, new CEOs receiving higher pay are more likely to reverse prior poor performance than CEOs receiving the same pay or lower pay than the departing CEO. The authors estimated that when pay and skill are linked, highly paid CEOs earn abnormal annual returns that are eight percent higher than poorly paid CEOs. Additionally, the mean return of companies in which pay and skill are related is nearly eight percent higher than companies in which pay and skill are not related.[116]

A 2009 study examined the proportion of CEO incentive compensation relative to their peers. The study found that firms that pay their CEOs in the top ten percent of pay earn negative abnormal returns over the next five years, by approximately 13 percentage points. The effect was found to be stronger for CEOs who receive higher incentive pay relative to their peers.[117] The authors found that for each dollar that was paid to those CEOs, there was a corresponding reduction in shareowner value by a factor of 100.

A similar study from 2009 investigated the fraction of the aggregate compensation of the top-five senior executives compared to the CEO. The authors found the higher a CEOs "compensation pay slice" the lower a firm's future value. This relationship was also found to contribute to lower profitability, lower stock returns accompanying acquisitions, and lower performance sensitivity of CEO turnover.[118]

***Mandatory Holding Periods: CASE-BY-CASE***
The SBA supports shareowner proposals asking companies to adopt a holding period for their executives, which means to hold stock after option exercise. The SBA will take a CASE-BY-CASE approach on these proposals based on these factors:

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[115] Hugessen, K., 2006 (Mar 30). Pay Without Performance: What Went Wrong and What We re Going to Do About It. Presentation to Toronto CFA Society.
[116] Daines, Robert, Nair, Vinay B. and Kornhauser, Lewis A., "The Good, the Bad and the Lucky: CEO Pay and Skill" (August 2005). Univ. of Pennsylvania Institute for Law and Economics, Research Paper Series, Forthcoming Available at SSRN: http://ssrn.com/abstract=622223 or DOI: 10.2139/ssrn.622223.
[117] Cooper, Michael J., Gulen, Huseyin, and Rau, P. Raghavendra, "Performance for pay? The relationship between CEO incentive compensation and future stock price performance" (December 2009), Krannert Graduate School of Management, Purdue University.
[118] Bebchuk, Lucian A., Cremers, Martjin, and Peyer, Urs, "The CEO Pay Slice" (October 2009 update) Harvard Law School, Yale School of Management, and INSEAD.

- Whether the company has any holding period or officer ownership requirements in place
- Actual officer stock ownership and how that compares to the shareowner proponent's suggested holding period or the company's own stock ownership or retention requirements

*For further information on the SBA's model stock ownership and retention guidelines, please see *Perspectives on Executive Compensation*, available at www.sbafla.com.

***Supplemental Executive Retirement Plans (SERPs): CASE-BY-CASE***
SERPs are non-qualified, executive-only retirement plans under which the company provides an additional retirement benefit to supplement what is offered under the employee-wide plan where contribution levels are capped.

SERPs are different from typical qualified pension plans in two ways. First, they do not receive the favorable tax deductions enjoyed by qualified plans. The company pays taxes on the income it must generate in order to pay the executive in retirement. Therefore, some critics contend that the executive's tax obligation is shifted to the company. Second, SERPs typically guarantee fixed payments to the executive for life. Unlike defined contribution plans, SERPs transfer the risk of investment performance entirely to the firm. Even if the company or its investment performs poorly, the executive is entitled to receive specified stream of payments.[119]

In the face of rising executive pay in the past decade, companies have not kept pace with modifying their SERP formula. The typical SERP formula not only includes base salary, but may also include variable compensation like bonus or equity compensation. Furthermore, most SERP formulas largely depend on the highest level of compensation received in the years proceeding an executive's retirement. Some companies even provide additional years of service not worked for a newly hired executive to account for pension forfeited at the previous company. All of these enhancements create substantial lifetime costs to the company and its shareowners.

Together, CEO pensions and deferred compensation comprise managers' "inside debt." As evidenced by Wei and Yermack in 2009, "if a manager's inside debt holdings become especially large…he might manage the firm too conservatively, reducing overall risk in ways that transfer wealth from stockholders to debtholders."[120] This has a positive effect on bond value; however, this positive affect is typically not as large as the negative affect felt by shareholders. Thus, large inside debt holdings can have a negative effect on company value.

Generally, we support shareowner proposals if there is evidence of abuse in the SERP program or post-employment benefits that indicate the company is employing especially large manager inside debt holdings and should not have broad discretion in administering such plans. The SBA supports the limitation of SERP policy to base compensation, rather than the extension to variable compensation or other enhancements, since this may significantly drive up the costs to the company and its shareowners due to the inefficiencies of SERPs. Otherwise, we give the compensation committee latitude in this decision.

***Pension Plan Accounting for Executive Compensation: FOR***
These shareowner proposals ask companies not to include the impact of company pension fund income in the calculation of earnings used in determining executive bonuses and performance compensation. The SBA supports shareowner proposals to exclude pension fund income in the calculation of earnings used in determining executive bonuses and compensation plans.

***Expensing Stock Options: FOR***
The SBA supports the general principle of stock option expensing. Stock options should be expensed along with other forms of compensation given that the exercise of options results in a transfer of shareowner value. Expensing options should provide additional discipline against overuse. Expensing stock options, as with other forms of compensation, also increases the clarity of a company's true earnings. The SBA believes stock options have a cost and should be included as an expense on the company's income statement.

A Bear Sterns research report on the acceleration of stock options identified 759 U.S. firms, which accelerated their stock options in 2006, up from 439 companies in 2005. The 73-percent increase occurred in anticipation of adopting FAS No. 123(R), which requires the expensing of stock options. The study estimates that over $6 billion of employee stock option expense has vanished from future income statement recognition through vesting acceleration.[121]

In accordance with the passing of FAS 123(R) in 2005, all companies are now required to expense stock options. That being the case, it is possible to restrict the right of transferability until after the vesting of a transferable stock option (TSO), as well as to subject an employee's proceeds from the sale of their TSOs to separate vesting requirements, which suggests further restrictions can be placed on these options to protect the plan from overuse. According to a study completed by Citigroup, Citi-Issued Options (CIOs) can be used to help clarify a company's true earnings as an alternative method to TSOs. CIO's possess two key features that eliminate the need to analyze the exercise and forfeiture behavior of the company's employees in pricing the options: transferability and reversion to company upon forfeitures, which in turn creates the cleanest method for expensing stock options.[122]

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[119] Bebchuk, Lucian Arye and Fried, Jesse M., "Pay without Performance: Overview of the Issues" . Journal of Corporation Law, Vol. 30, No. 4, pp. 647-673, 2005. Also see Bebchuk, Lucian A., Cohen, Alma, and Spamann, Holger, "The Wages of Failure" (Working Draft, November 22, 2009).
[120] Wie, Chenyang, and David Yermack, "Stockholder and Bondholder Reactions To Revelations of Large CEO Inside Debt Holdings: An Empirical Analysis." September 2009.
[121] McConnell, Pat et al, 2006, "Employee Stock Options: 749 Companies Accelerate Stock Options Vesting", Bear Sterns Equity Research – Accounting and Tax Policy.
[122] Ortner, William et al, 2006, "Equity Compensation and the Capital Markets", Citigroup – Corporate Equity Derivatives Research.

***Recoup Bonuses or Incentive Compensation through "Clawback" Provisions: CASE-BY-CASE***
When companies or shareowners propose provisions discussing the recoupment of executive bonuses or incentive compensation, these provisions are referred to as "clawback" provisions. In other words, a company's board of directors may claw back, or recoup, an executive's bonus or incentive compensation after it has been paid to the executive. Most commonly, these provisions address situations where the company's restated financial statements show that an executive did not achieve the performance results necessary for the executive to receive a bonus or incentive compensation. For instance, if a company with a clawback provision is forced to restate its financial statements and the restated financial statements reveal that an executive did not achieve the performance necessary to receive a bonus or incentive compensation, then the company may recoup the bonus or incentive compensation, especially if the executive misstated the financial statements through fraud, misconduct, or negligence just to receive his or her bonus or incentive compensation.

Clawback provisions are a relatively new tool, but they are receiving much press in light of the U.S. recession that began in December 2007 as a result of the crisis in the U.S. financial sector. The meltdown in the U.S. financial sector brought numerous financial restatements with it, which showed in some instances that executive bonuses and incentive compensation payments were unjustified. This led shareowners to propose clawback provisions to recoup some or all of these payments.

In addition to shareowners, the U.S. government has experimented with clawback provisions. Section 304 of the Sarbanes-Oxley Act of 2002 states that the CEO and the CFO of an issuer must reimburse the issuer for bonuses or incentive compensation received if the issuer had to restate its financial statements as a result of misconduct. When the U.S. government became a proxy shareowner for the U.S. public under the Troubled Asset Relief Program, it enacted broader, more stringent clawback provisions than what SOX contained. With TARP, the U.S. government predicated monetary assistance on the condition that companies receiving TARP funds claw back executive bonuses or incentive compensation "if the payment was based on materially inaccurate financial statements or performance metrics." Section 954 of the Dodd-Frank Act requires the SEC to adopt rules prohibiting the national securities exchanges and associations from listing any company that fails to implement a clawback policy pursuant to which incentive based compensation can be recouped from current and former executives under specific triggers. These criteria are more stringent than the clawback provisions in Sarbanes-Oxley's Section 304.

In the February 2009 edition of "Executive Compensation Trends", Equilar noted that the prevalence of clawback policies at publicly traded Fortune 100 companies grew from 17.6 percent in 2006 to 64.7 percent in 2008. In addition, even companies outside the financial services sector are increasingly adding or expanding clawback provisions.

The SBA adopts the position that clawback provisions are essential to performance-based compensation plans. To align executive interests with the interests of shareowners, executives should be compensated for achieving performance benchmarks. Equally, an executive should not be rewarded if he or she does not achieve established performance goals, and if restated financial statements reveal that the executive was falsely rewarded, then he or she should be forced to repay any unjust compensation received.

Specifically, the SBA considers clawback proposals on a CASE-BY-CASE basis. If it is later determined that fraud, misconduct, or negligence significantly contributed to a restatement of financial results that led to the awarding of unearned incentive compensation, the SBA will evaluate these proposals, taking into consideration:

- If the company has adopted a formal recoupment bonus policy, or
- If the company has chronic restatement history or material financial problems.

***Compensation Consultants - Disclosure of Board or Company's Utilization: FOR***
External compensation consultants should be independent to ensure that advice is unbiased and uncompromised. Multiple business dealings or significant revenue from the company may impair the independence of a pay consultant's opinions, advice, or recommendations to the compensation committee.

The following policy is typically used by compensation consultants to ensure that conflicts of interest are mitigated when the consultant provides other services to a company in addition to executive pay advice:

- The consultant establishes a Code of Conduct, which articulates a commitment to providing impartial services.
- Senior consultants have the responsibility to review and resolve all potential conflicts of interest before the engagement proceeds.
- A senior consultant not on the team performing the work reviews the executive pay recommendations.
- The consultant has a policy in place, which precludes consultants who advise the company on executive pay to engage with the company on any other services provided by the consultant.

Such safeguards and procedures are designed to separate compensation consultancy work from other services provided from the consultant to company.[123]

In a study examining the effect of compensation consultants on CEO pay of 880 firms from the S&P 1500 for fiscal year 2006, the authors found evidence of greater compensation in the presence of a compensation consultant, consistent with a rent extraction role, as suggested by critics. However, the study found no evidence proving that the potential conflicts of interest between the firm and compensation consultants as the primary driver of excessive CEO pay.[124]

Additionally, another study found that while there was no direct relationship between potential conflicts of interest and executive pay, there was some evidence that directors and executives may use compensation consultants to legitimize unusually high levels of executive pay. According to the authors' results, executive pay was highest when a company engages three or more compensation consultants.[125]
In December 2007, the United States House of Representatives Committee on Oversight and Government Reform issued a report examining whether the compensation consultants hired by large publicly traded companies meet the required standards of independence. The report is based on nonpublic information provided to the Committee by the leading compensation consultants in the United States. For each consultant, the Committee requested and received data on the value of the executive compensation services and other services provided to the 250 largest publicly traded companies as determined by *Fortune* magazine. The report revealed that compensation consultant conflicts of interest were widespread. Fees earned by compensation consultants for providing other services often far exceeded those earned for advising on executive compensation. Moreover, many Fortune 250 companies do not disclose their compensation consultants' conflicts of interest. Finally, the report also suggested that there appeared to be a correlation between the extent of a consultant's conflict of interest and the level of CEO pay.[126]

An article written by founder and managing director of compensation consulting firm James F. Reda & Assoc. suggested that boards needed to consider following a number of criteria when seeking outside advice for executive compensation. First, consultants must maintain independence from management, which also allows for visibility and good reputation. Second, the compensation consultants must have expertise in the industry the company operates, as well as direct and relevant experience. More importantly, the consultants must have a wealth of executive compensation resources, which are seamlessly integrated and includes proficiency with all pay elements and performance measurement analytical techniques. Fourth, the consultant must strive to align the company's business goals and its executive pay strategy. Finally, nationwide and worldwide coverage is a key component, which combined with the above, allows for the consultants to demonstrate greater creativity and have the capability to create custom designs.[127]

The SBA generally votes FOR shareowner proposals seeking disclosure regarding the Company, Board, or Compensation Committee's use of compensation consultants, such as company name, business relationship(s), fees paid, and identification of any potential conflicts of interest.

***Pension Plan Income Accounting: FOR***
We generally vote FOR shareowner proposals to exclude pension fund income in the calculation of earnings used in determining executive bonuses and compensation as pension assets may provide potential for manipulation and help boost companies' reported earnings.

***Pre-Arranged Trading Plans (10b5-1 Plans): FOR***
The SBA generally votes FOR shareowner proposals calling for certain principles regarding the use of prearranged trading plans (10b5-1 plans) for executives. These principles include:

- Adoption, amendment, or termination of a 10b5-1 Plan must be disclosed within two business days in a Form 8-K.
- Amendment or early termination of a 10b5-1 Plan is allowed only under extraordinary circumstances, as determined by the board.
- The plan must provide that ninety days must elapse between adoption or amendment of a 10b5-1 Plan and initial trading under the plan.
- Reports on Form 4 must identify transactions made pursuant to a 10b5-1 Plan.
- An executive may not trade in company stock outside the 10b5-1 Plan.
- Trades under a 10b5-1 Plan must be handled by a broker who does not handle other securities transactions for the executive.

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[123] Waxman, Henry A. (prepared for), 2007, "Conflicts of Interests among Executive Compensation Consultants", U.S. House of Representatives, Committee on Oversight and Government Reform, available at: http://www.erieri.com/PDF/Executive-Consultant-Conflicts.pdf.
[124] Brian Cadman, Mary E. Carter and Stephen Hillegeist: "The Role and Effect of Compensation Consultants on CEO Pay", March 2008.
[125] Murphy, Kevin and Tatiano Sandino, "Executive Pay and Independent Compensation Consultants," June 2008.

[126] United States House of Representatives Committee on Oversight and Government Reform: "Executive Pay: Conflict of Interest Among Compensation Consultants." December 2007.
[127] James Rada: "How "Independent" Is Your Compensation Adviser?", The Corporate World, March/April 2008.

A study by Stanford's Alan Jagolinzer reveals that trades executed within 10b5-1 plans were more lucrative for the insiders than trades executed by insiders at the same firms who had not adopted such plans, and that early terminations of 10b5-1 plans are associated with impending disclosures of negative corporate news. 10b5-1 plans are intended to eliminate executives' flexibility over transactions in company stock so that they are able to diversify their financial portfolio. However, Jagolinzer's study seems to suggest that the 10b5-1 plans may have been abused. The SBA believes that 10b5-1 plans, with proper safeguards and controls, can be an effective tool for executives.

A related issue of concern is the use of "prepaid variable forward contracts" by company management. These contracts are stock sale arrangements whereby an executive agrees to sell, at some point in the future, a specified number of shares and receives immediate payment of cash (from a brokerage firm or other third party) for a portion of the sale price. If the stock price falls, the brokerage takes the loss; if it goes up, the executive shares in at least some of the profits with no downside risk.[128] The SBA discourages such arrangements as they go beyond the ability to diversify an executive's company holdings.

***Share Buyback Holding Periods: AGAINST***
Because a share buyback is often an indication of the company's confidence in its own stock, the announcement of a share buyback may increase a company's stock price. However, share buyback may occur in stages and not all at once. Also, companies may not actually repurchase shares if market conditions are not attractive even though they have made prior announcement of share buyback.

The SBA generally votes AGAINST shareowner proposals prohibiting executives from selling shares of company stock during periods in which the company has announced that it may or will be repurchasing shares of its stock. Conversely, we vote FOR the proposal when there is a pattern of abuse by executives exercising options or selling shares during periods of share buybacks.

***Tax Gross-Up Shareowner Proposals: FOR***
Tax gross-ups are reimbursements to senior executives paid by the company to cover an executive's tax liability. Tax gross-ups are a costly benefit to shareowners, since it generally takes at least $2.50 and as much as $4 to cover each $1 of excise tax that must be "grossed-up."[129] Providing gross-ups to executives has become widespread and represents a clear disconnect between pay and performance. A recent study found that approximately two-thirds of the S&P 500 index disclosed they would provide excise tax gross-ups to one or more top executives. At 80 percent of those companies, tax gross-ups would have been triggered if the executives had received change-in-control ("CIC") severance at the end of the prior fiscal year—with the aggregate potential gross-up payments for all named executive officers at those companies averaging $13.9 million.[130] Influential executive compensation consultant Ira Kay of Watson Wyatt recommends, "…eliminating full tax gross-ups for new executives and fazing them out of existing agreements."[131] Anti-tax gross-up shareowner proposals ask the board to adopt a prospective policy that forbids the payment of tax gross-ups to executives unless such payments are provided to other managers at the firm. The SBA generally votes FOR proposals calling for companies to adopt a policy of not providing tax gross-up payments to executives, except in situations where gross-ups are provided pursuant to a plan, policy, or arrangement applicable to management employees of the company, such as a relocation or expatriate tax equalization policy.

***Advisory Vote on Executive Compensation (Say-on-Pay), Management Proposals: CASE-BY-CASE***

**Background and Overview**
High levels of investor concern about escalating levels in executive pay have prompted a number of developments this decade, including the implementation of shareowner votes on pay programs in a growing number of markets. These include the U.K., Australia, the Netherlands, Sweden, Norway, and Spain. With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, U.S. public companies also became subject to Say-on-Pay requirements.

Pursuant to final rules adopted by the SEC in early 2011 and as part of their annual general meetings, companies are required to provide shareowners with advisory (non-binding) votes on executive compensation packages for named executive officers, and the desired frequency of such votes on compensation (every 1, 2, or 3 years). Foreign private issuers, or non-U.S. privately held firms, are not required to conduct say-on-pay and frequency votes. The advisory vote on compensation covers the Compensation, Discussion & Analysis (CD&A) disclosure, executive compensation tables, and accompanying narrative in a company's proxy filing. Companies are required to discuss in their CD&A narrative whether and, if so, to what extent they have taken into account the results of their most recent say-on-pay shareowner vote in determining compensation policies and decisions. As well, consideration of any prior say-on-pay votes need to be covered to the extent they are material to compensation decision-making.

Academic reviews and empirical evidence of international experience with the adoption of say-on-pay reveal some benefits to the increased awareness brought on by the mandate. A 2007 study examined the effect of 2002 legislation in the UK requiring publicly traded companies to submit reports on executive compensation to a non-binding shareowner vote at the annual general meeting. The authors found that, as a result of the legislation, CEO cash compensation and CEO total compensation became more sensitive to negative operating performance.[132] Another study indicates that the UK requirement to require shareowner voting on compensation

[128] Hodgson, Paul, "Investing in Corporate Governance: Forward Sales – Sharing the Gain, Avoiding the Pain," The Corporate Library, July 2009
[129] "New Study on Tax Gross-ups," Risk & Governance Weekly, 12/5/08.
[130] Papadopoulos, Kosmas, "Gilding Golden Parachutes: the Impact of Excise Tax Gross-Ups," RiskMetrics Group, 11/24/08.
[131] Kay, Ira, and Steven Seelig, "A Reasonable Approach to Severance and Change-in-Control Payments," Watson Wyatt Insider, August 2007.
[132] Balachandran, S., Ferri, F., and Maber, D., 2007. Solving the Executive Compensation Problem Through Shareowner Votes? Evidence From the U.K.

practices has produced markedly fewer rewards for underperforming senior executives and lowered CEO compensation at those companies with poor operating performance.[133]

A 2007 Millstein Center Policy Briefing reviewed the UK's experience with "say on pay" rights. The author asserted that advisory shareowner votes on executive pay could be adapted to the U.S. and other markets and would be a step in the right direction for aligning corporate pay with performance as part of a package of accountability reforms, including legislation and adaptation of market practices.[134] A 2008 study by Jie and Walkling indicates that shareowner votes on executive compensation are likely to create value for firms with overpaid CEOs and firms more likely to respond to the shareowner votes.[135] The findings of such studies, along with investor discontent regarding executive compensation levels, led to increasing demand for advisory votes in the U.S., culminating with the inclusion of such shareowner votes in the Dodd-Frank Act. The earliest U.S. companies to provide shareowners with a say-on-pay vote were TIAA CREF in 2007, followed in 2008 by Aflac, RiskMetrics, H&R Block, Jackson Hewitt, Zale, and Littlefield. The number of companies facing say-on-pay proposals jumped to approximately 100 in 2009. As of January 21, 2011, shareowner advisory votes under the Dodd-Frank Act are in effect for all public U.S. companies (with some exceptions for smaller capitalization companies).

**Current Policy**
The SBA votes on management proposals for an advisory vote on executive compensation on a CASE-BY-CASE basis. Further, the SBA votes AGAINST these resolutions in cases where boards have failed to demonstrate good stewardship of investors' interests regarding executive compensation practices. The following principles and factors are considered:

1. The following <u>five global principles</u> apply to all markets:

   - Maintain appropriate pay-for-performance alignment with emphasis on long-term shareowner value: This principle encompasses overall executive pay practices, which must be designed to attract, retain, and appropriately motivate the key employees who drive shareowner value creation over the long term. It will take into consideration, among other factors: the linkage between pay and performance; the mix between fixed and variable pay; performance goals; and equity-based plan costs;

   - Avoid arrangements that risk "pay for failure": This principle addresses the use and appropriateness of long or indefinite contracts, excessive severance packages, and guaranteed compensation;

   - Maintain an independent and effective compensation committee: This principle promotes oversight of executive pay programs by directors with appropriate skills, knowledge, experience, and a sound process for compensation decision-making (e.g., including access to independent expertise and advice when needed);

   - Provide shareowners with clear, comprehensive compensation disclosures: This principle underscores the importance of informative and timely disclosures that enable shareowners to evaluate executive pay practices fully and fairly;

   - Avoid inappropriate pay to non-executive directors: This principle recognizes the interests of shareowners in ensuring that compensation to outside directors does not compromise their independence and ability to make appropriate judgments in overseeing managers' pay and performance. At the market level, it may incorporate a variety of generally accepted best practices.

2. For U.S. companies, the SBA votes CASE-BY-CASE considering the following factors in the context of each company's specific circumstances and the board's disclosed rationale for its practices:

   <u>Relative Considerations:</u>

   - Assessment of performance metrics relative to business strategy, as discussed and explained in the CD&A
   Evaluation of peer groups used to set target pay or award opportunities
   - Alignment of company performance and executive pay trends over time (e.g., performance down: pay down)
   - Assessment of disparity between total pay of the CEO and other Named Executive Officers (NEOs)

   <u>Design Considerations:</u>

   - Balance of fixed versus performance-driven pay
   - Assessment of excessive practices with respect to perks, severance packages, supplemental executive pension plans, and burn rates

[133] Ferri, Fabrizio and David Maber, "Solving the Executive Compensation problem through Shareholder Votes? Evidence from the U.K.," November 2007.
[134] Davis, S. (2007), Does Say On Pay Work? Lessons on Making CEO Compensation Accountable, Policy Briefing No. 1, Millstein Center for Corporate Governance and Performance, Yale School of Management.
[135] Cai, Jie and, Ralph A. Walkling, "Shareholders Say on Pay: Does it Create Value?," December 8, 2008, Drexel College of Business Research Paper No. 2008-06.

- Vesting provisions and dividend payment on earned shares

Communication Considerations:

- Evaluation of information and board rationale provided in CD&A about how compensation is determined (e.g., why certain elements and pay targets are used, and specific incentive plan goals, especially retrospective goals)
- Assessment of board's responsiveness to investor input and engagement on compensation issues (e.g., in responding to majority-supported shareowner proposals on executive pay topics).

3. For international companies, the SBA vote's recommendations for annual "say-on-pay" resolutions put forward by management on a case-by-case basis in each market where such proposals routinely appear on proxy ballots. As noted, these currently include the U.K., Australia, the Netherlands, Sweden, Norway, and some companies in Denmark. Evaluations take into account specific proposal wording, local market regulations and prevailing practices, and local governance and best practice codes. The key factors influencing evaluations generally fall into the following categories:

- Pay in relation to performance, usually based on the design of programs and actual grants (e.g., the use of rigorous performance hurdles)
- Equity-based awards, which should not exceed levels recommended under local best practice codes
- "Pay for failure" arrangements, such as long-term contracts that could lead to multiple-year severance packages
- The quality of pay disclosures (e.g., specifying incentive goals that generated past-year rewards and/or forward-looking targets)
- In some markets, aspects of non-executive directors' pay (e.g., codes in several markets discourage stock-based grants to non-executive directors)
- Voting recommendations typically look to the preponderance of evidence, i.e. an AGAINST recommendation may result when a preponderance of negative features outweighs the positive features presented in a remuneration report.

***Advisory Vote on Executive Compensation (Say-on-Pay), Shareowner Proposals: FOR***
Generally, the SBA votes FOR shareowner proposals that call for non-binding shareowner ratification of the compensation of the Named Executive Officers and the accompanying narrative disclosure of material factors provided to understand the Summary Compensation Table. The SBA supports a granular assessment of executive compensation at any given company, rather than an all-or-nothing vote. Preferably, this would allow for separate votes on one-time compensation awards, CEO pay, and senior executive compensation.

***Director Compensation: CASE-BY-CASE***
The SBA votes CASE-BY-CASE on compensation plans for non-employee directors, based on the cost of the plans against the company's allowable cap.

Occasionally, director stock plans that set aside a relatively small number of shares when combined with employee or executive stock compensation plans will exceed the allowable cap. The SBA votes FOR the plan if ALL of the following qualitative factors in the board's compensation are met and disclosed in the proxy statement:

- Director stock ownership guidelines with a minimum of three times the annual cash retainer

  Vesting schedule or mandatory holding/deferral period

  - A minimum vesting of four years for stock options or restricted stock; or deferred stock payable at the end of a four-year deferral period.

- Mix between cash and equity:

  - A balanced mix of cash and equity, for example 40% cash/60% equity or 50% cash/50% equity; or
  - If the mix is heavier on the equity component, the vesting schedule or deferral period should be more stringent, with the lesser of five years or the term of directorship.

- No retirement/benefits and perquisites provided to non-employee directors

- Detailed disclosure provided on cash and equity compensation delivered to each non-employee director for the most recent fiscal year in a table. The column headers for the table may include the following: name of each non-employee director, annual retainer, board meeting fees, committee retainer, committee-meeting fees, and equity grants.

***Director Retirement Plans: AGAINST***
The SBA votes AGAINST retirement plans for non-employee directors. Conversely, the SBA votes FOR shareowner proposals to eliminate retirement plans for non-employee directors.

***Non-Employee Director Compensation Plan: CASE-BY-CASE***
Non-employee director compensation should be composed of a mix of cash and stock awards. Although some board members may already own considerable amounts of stock, the SBA believes that directors should not be compensated solely in cash. Director compensation plans will be evaluated by comparing the cash compensation plus the approximate value of the equity-based compensation per director to a peer group with similar size and enterprise value. The initial compensation that is provided to new directors is also considered. Plans are generally approved when the per-director total cost falls within one standard deviation of the mean pay for the peer group. In most cases, non-employee directors have full-time employment elsewhere, making it unnecessary to offer retirement benefits for serving on the board. The cash retainer and equity compensation are generally adequate compensation for board service. Therefore, the SBA typically supports shareowner proposals requesting the limitation or elimination of retirement benefits for non-employee directors.

***Stock Options to Non-Executive Directors (International Markets): CASE-BY-CASE***

**Background and Overview**
Granting options to non-executive directors is currently an accepted practice in the U.S. and Canada. However, in the U.K., Australia and some Continental European countries, such as Belgium and the Netherlands, local codes of best practice recommend against the granting of stock options to non-executive directors. French law even takes this a step further by limiting the grant of options strictly to corporate officers or employees.

As indicated below, the codes advocate the principle that option grants do not necessarily align non-executive directors' interests with those of shareowners, as stock options arguably confer potential upside to directors but none of the downside that shareowners face. In addition, such exposure to a company's financial performance may make non-executives either less or more risk averse from a strategic point of view, taking the focus away from oversight of management processes and accountability.

The Netherlands (Tabaksblat Code): "The remuneration of a supervisory board member should not be dependent on the results of the company". "A supervisory board member shall not be granted any shares and/or rights to shares by way of remuneration" and "Any shares held by a supervisory board member in the company on whose board he sits are long-term investments".

Belgium (Lippens Code): "Non-executive directors should not be entitled to performance-related remuneration such as bonuses, stock related long-term incentive schemes, fringe benefits or pension benefits."

France (Bouton Code): "Directors who are neither corporate officers nor employees are barred by law from receiving options."

**Review of Current Policy**
In most markets, stock option plans featuring potential grants to non-executive directors are generally considered acceptable. In the U.K., the SBA's policy is consistent with local best practice, as articulated by the National Association of Pension Funds (NAPF) on the basis of the Combined Code. According to the ABI (Associations of British Insurers)/NAPF guidelines on executives' remuneration, "participation in share incentive schemes should be restricted to bona fide employees and executive directors." A similar policy applies in Australia, where stock options for non-executives are not accepted either.

In international markets, the SBA will vote on plans that include option grants to non-executives on a CASE-BY-CASE basis. Country-specific opposition to options grants will be taken into consideration.

***Pay-for-Superior Performance: FOR***
The SBA generally votes FOR shareowner proposals based on an individualized analysis that requests the board establish a pay-for-superior performance standard in the company's executive compensation plan for senior executives. The proposal has the following principles:

- Sets compensation targets for the Plan's annual and long-term incentive pay components at or below the peer group median
- Delivers a majority of the Plan's target long-term compensation through performance-vested, not simply time-vested, equity awards
- Provides the strategic rationale and relative weightings of the financial and non-financial performance metrics or criteria used in the annual and performance-vested long-term incentive components of the plan
- Establishes performance targets for each plan financial metric relative to the performance of the company's peer companies
- Limits payment under the annual and performance-vested long-term incentive components of the plan to when the company's performance on its selected financial performance metrics exceeds peer group median performance.

The following factors are considered when evaluating this proposal:

- What aspects of the company's annual and long-term equity incentive programs are performance-driven?
- If the annual and long-term equity incentive programs are performance driven, are the performance criteria and hurdle rates disclosed to shareowners or are they benchmarked against a disclosed peer group?
- Can shareowners assess the correlation between pay and performance based on the current disclosure?
- What type of industry and stage of business cycle does the company belong to?

Recent research by Ertimur, Ferri, and Muslu shows greater success for shareowner proposals that focus on the pay setting process, such as subjecting certain compensation items to shareholder approval, rather than proposals seeking specific pay limits.[136] The study showed an average reduction of $2.3 million in CEO in firms targeted by proposals sponsored by institutional proponents and calling for greater link between pay and performance.

***Shareowner Proposal to Require Supermajority of Independent Board Members to Approve CEO Compensation: AGAINST***
The SBA generally votes AGAINST shareowner proposals to seek approval of an amendment to the bylaws in order to provide that a company's CEO's compensation must be approved by two-thirds of all independent directors of the board. "Independent director" shall mean any director who is not a present or former employee or officer of the Corporation, and who meets criteria for qualifying as an "independent" director under the applicable listing requirements of the New York Stock Exchange.

Proponents of this proposal argue that approval of this proposal would ensure that the company provides a CEO pay package that is widely supported by its independent directors; increase the likelihood that the company's independent directors are kept informed of, and feel shared responsibility for, CEO compensation decisions; and would not prevent a small committee or subcommittee to study, examine and determine CEO compensation. Instead, it would only require that decisions made by such a committee or subcommittee to be subsequently ratified by additional independent directors to meet the bylaw's requirements.

The SBA believes that shareowners should not be involved in setting executive compensation, particularly where a company has a track record of reasonable executive compensation. Such matters should be left to the board's compensation committee, which has the ultimate responsibility of examining all aspects of the compensation program for the company's executive officers. In addition to being unnecessarily restrictive, this proposal would establish procedures that could usurp the role of this committee. The SBA believes that shareowners would be better served through a shareowner advisory vote on executive compensation, which would provide shareowners with a more effective mechanism to voice their concerns over a company's executive compensation practices. However, the SBA does encourage the company's board of directors to review the work of the compensation committee to ensure that best practices are followed.

## CORPORATE SOCIAL RESPONSIBILITY (CSR)
## VOTING ON ENVIRONMENTAL, SOCIAL AND POLITICAL ISSUES

The SBA acknowledges that many beneficiaries are concerned about the social, political, and moral implications of investment decisions within the Florida Retirement System. As part of the SBA's asset management responsibilities, investments are undertaken with a strong focus on maximizing long-term returns, controlling costs, and achieving appropriate diversification in order to minimize risk. Historically, the SBA has been proactive on many corporate governance issues, emphasizing those factors that directly impact investment values. Increasingly, investors are incorporating emerging issues, such as the environment, into their investment calculus. As a result, many companies are intensifying their approach to corporate responsibilities and expanding the scope of their disclosures related to burgeoning risk factors. The SBA is a leading advocate for full and transparent disclosures across a broad spectrum of corporate governance issues.

In the December 2006 issue of the *Harvard Business Review*, Michael Porter and Mark Kramer discussed the link between competitive advantage and corporate social responsibility. Their starting point was a forceful critique of current CSR trends, which, they argued, are misinformed by the idea that business and society were in tension, when in fact they are interdependent. They contended that the prevailing justifications for CSR, namely moral obligation, sustainability, license to operate, and reputation create at best generic rationales that fail to help companies identify the social issues where they can have the biggest positive impact. As a consequence, CSR in practice is unfocused and not coordinated among different business units, often even excluding a company's core operations. CSR activities are thus driven by external audiences instead of the internal needs and opportunities of businesses. The authors proposed that companies should abandon this reactive perspective of CSR and instead, incorporate CSR into their strategic planning. Strategic CSR will focus on a company's operations by focusing on cost control and better customer service, thereby increasing competitiveness. Companies need to take a tactical, proactive approach regarding CSR. For Porter and

[136] Yonca Ertimur, Fabrizio Ferri, and Volkan Muslu, "Shareholder Activism and CEO Pay" August 7, 2009.

Kramer, the essential test to guide CSR is not whether a cause is worthy, but whether it presents an opportunity to create a meaningful mutual benefit for society and business, which will lead to corporate social integration.

Whereas U.S. companies in the past viewed sustainability as something between goodwill utopianism and a public relations exercise, today's younger CEOs see sustainability issues as an upper echelon agenda item, says McKinsey's Lenny Mendonca. One of the firms at the forefront of identifying and quantifying how specific environmental and social practices improve corporate performance is Innovest Strategic Value Advisors. Matthew Kiernan, CEO of Innovest, argues that sustainability strategies are a good proxy of management quality. Many major investment banks now share this point of view. For instance, Goldman Sachs, Deutsche Bank Securities, UBS, Citigroup, Morgan Stanley, and other brokerages have formed research teams addressing sustainability. The evidence is still scarce that addressing social and environmental sustainability will help with short-term financial performance goals. Nevertheless, there is an emerging consensus within the financial community that sustainability is a long-term imperative, even for corporate survival.

Recently, factors such as environmental, social, and governance (ESG) issues have been incorporated in the valuation of companies due to the increased awareness of the implications of these issues on the financial position of companies. The evaluation of ESG risks can be used to understand the strategic direction of a company, or industries as a whole, as well as allow for the prediction of future costs or burdens to the company due to these factors. Understanding these issues may allow investors to develop a competitive advantage, by recognizing industry patterns. It has been determined by the United Nations Environment Programme Finance Initiative (UNEP FI) and the UN Global Compact Principles for Responsible Investment (PRI) that ESG factors can affect the long-term performance of investments, and by July 2007, more than 200 international corporations, representing over $9 trillion in assets, had endorsed the PRI.[137] Furthermore, researchers have made great strides recently in quantifying ESG issues. For instance, a CFO.com article revealed that finance Professor Anant Sundaram and the Allwin Initiative for Corporate Citizenship at Dartmouth's Tuck School of Business has developed a Fossil Fuel Beta (FFB) for determining fossil fuel prices and green house gas emission liabilities throughout the value chain. As such, the metric may provide the market with a method of quantifying a firm's sustainability reports, thereby, allowing sustainability to be factored into a firm's market value.

Accordingly, the SBA may vote AGAINST shareowner initiatives to ban precatory proposals as it would eliminate the proper exercise of shareowner rights, especially as it relates to these issues.

**Consumer Issues**

**Background and Overview**
The recent wave of recalls and warnings from products produced in China has ignited concerns about the complex risks associated with product safety, including the potential management of certain global supply chains. Companies operating in the global economy are increasingly called upon to assume greater responsibility for social and environmental compliance in their supply chain operation, in particular as it relates to toxic chemicals risks in the workplace or consumer human exposure to toxic chemicals in products.

According to ISS Governance Services' 2007 Policy Survey, 62 percent of respondents felt it was important for U.S. companies to report to shareowners on the environmental and social practices of the supply chain as a part of routine filings and disclosure. Over seventy-eight percent of respondents felt that workplace safety performance was an important disclosure criterion.

Toxic chemical and product safety concerns may pose substantial challenges to both manufacturing and retail companies. In the short term, companies may face supply shortages. In the long term, companies may be challenged by persistent supply-chain disruptions and legislative, legal, and reputational risk, which affect companies' political and social costs. As a result, long-term institutional investors may face significant risk exposure at companies that fail to properly manage product safety in their supply chain.

**Review of Current Policy**
The SBA evaluates a number of shareowner proposals each season on the issue of toxic chemicals. In past years, proponents have focused on the phase-out of certain high profile chemicals by eliminating, or evaluating the feasibility of eliminating, persistent and bioaccumulative toxic (PBT) chemicals, brominated flame retardants (BFRs), polyvinyl chloride (PVC) plastics, bisphenol-A, lead, and mercury, and have requested that companies use safer materials. These proposals have also asked for what new initiatives management can or will take to respond to these toxic chemical public policy challenges beyond those initiatives or actions already required by law.

The SBA will continue to evaluate such shareowner proposals on a case-by-case basis, weighing issues such as: current regulations, recent significant controversy/litigation/fines stemming from toxic chemicals, and the current level of disclosure by the company on this topic. Resolutions requiring that a company reformulate its products are unlikely to be supported by the SBA.

The SBA will generally support resolutions requesting that a company disclose its policies related to toxic materials unless substantial information is already provided by the company. This existing policy works appropriately for manufacturers but falls short of addressing companies further down the supply chain, notably retailers. Consistent with the mounting concerns over product recalls

[137] CFA Centre for Financial Market Integrity, "Environmental, Social, and Governance Factors at Listed Companies: A Manual for Investors," 2008.

and our client survey results, the intent of the SBA's approach on product safety is to expand the scope of the current toxic chemicals policies to be more applicable to issues related to product safety and global supply chain management. This would essentially imply that companies beyond manufacturers would be evaluated individually and relative to industry peers to determine if their policies and disclosure provide shareowners with the necessary information to consider the company's management of the potential risks associated with toxic chemicals and product safety.

***Product Safety: FOR***
Product recalls due to safety hazards or the inclusion of toxic materials reiterate the importance of high safety standards and secure manufacturing processes throughout the supply chain network. Company failure to implement effective safety standards, and to enforce them throughout the supply chain, creates risk beyond the obvious consumer hazards. Shareowners face the potential for substantial loss in the event of product recalls, class action liability, damage to brand reputation, or supply chain failures and supply shortages due to substandard safety practices or the use of toxic materials. Therefore, proposals for increased disclosure in this context are generally appropriate, provided the request is not duplicative of currently available company reports or practices.

- Generally, the SBA votes FOR proposals requesting increased disclosure regarding oversight procedures, product safety risks, or the use of toxic materials in the manufacturing of company products.

- Generally, the SBA votes FOR proposals requesting increased disclosure regarding oversight procedures, product safety risks, or the use of toxic materials in the company's global or domestic supply chain network.

***Genetically Engineered (GE) Organisms: CASE-BY-CASE***
Genetically engineering organisms involves the introduction of new genes into plant and animal organisms in order to spawn new traits in animals or produce exceptional growth in agriculture. The U.S. Department of Agriculture (USDA), the Food and Drug Administration (FDA), or the Environmental Protection Agency (EPA) currently regulates engineered or genetically modified organisms. Shareowner proposals in this area generally request the removal of genetically engineered food (animals), ingredients from crops (products), changes in product labeling, or their related study.[138] The SBA votes on such shareowner proposals on a CASE-BY-CASE basis. For those proposals that request changes to a company's business strategy or operations, the SBA generally votes AGAINST since we do not attempt to mandate business strategies for the companies we own.

***Community Reinvestment: FOR***
Equality in mortgage lending is the basic motivation behind these proposals. The Community Reinvestment Act (CRA) of 1977 was developed to encourage banks to improve their lending practices in the communities from which they receive deposits; however, since the law's introduction, the banking business has changed significantly. Now, more than half of mortgage lending is done by non-depository financial institutions such as mortgage companies, insurance companies, or a corporate subsidiary. Also, these financial institutions are not affected by the CRA because they are non-depository. Critics of the CRA contend that the legislation lacks teeth; however, given the projected pace of banning consolidation, the CRA's only sanction has found new importance. The only sanction for poor CRA performance is for regulators to deny an institution's request for expansion, including applications to open new branch offices, as well as for its mergers or acquisitions of other institutions. The law's regulations allow individuals or groups to protest the expansion and merger applications of a specific lender if they believe that institutions are not meeting the credit needs of its local community. Proponents of these proposals request the board of directors to develop a policy' which includes all financial subsidiaries of the corporation (both depository and non-depository) under a general program for community reinvestment similar to that required of individual depository subsidiaries under the CRA and to report annually to shareowners on its achievements. The SBA supports shareowner initiatives aimed at promoting fair and open lending standards.

***Tobacco Production, Marketing, & Health Issues: CASE-BY-CASE***
Shares should be voted in a manner designed to enhance shareowner benefit while at the same time respecting the regulations and legal structures relevant to the tobacco industry. We do not believe that shareowners are responsible for instructing management on business strategies or tactics. However, in cases of negligence on the part of management, the SBA has a responsibility to protect shareowner value and will support shareowner proposals aimed at maintaining or restoring shareowner value.

***Educational Plan on Abortifacient Effect of Drugs: ABSTAIN***
This proposal asks for an education plan that would inform "literate and non-literate" women of the possible abortifacient effects of the company's products. Due to the complex and sensitive nature of these proposals, the SBA ABSTAINS from voting on these issues.

***Pharmaceutical Pricing Policy: AGAINST***
These resolutions ask companies to adopt price restraint policies and report to shareowners. The SBA supports unfettered prices dictated only by the forces of a free market. Therefore, we will not support shareowner initiatives seeking to restrain a company's ability to charge what the market will bear.

***Pharmaceutical Product Reimportation: CASE-BY-CASE***
The SBA generally supports proposals requesting that companies report on the financial and legal impact of their policies regarding prescription drug reimportation unless such information is already publicly disclosed. However, the SBA generally votes AGAINST proposals requesting that companies adopt specific policies to encourage or constrain prescription drug reimportation.

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[138] Fetter-Degges, Jan, "Environment: Bioengineering." Social Issues Service, 2007 Background Report – J1. 6 March 2007.

***Consumer Lending: CASE-BY-CASE***
Requests for reports on the company's lending guidelines and procedures, including the establishment of a board committee for oversight, are voted on a CASE-BY-CASE basis by the SBA, taking into account:

- Whether the company has adequately disclosed mechanisms in place to prevent abusive lending practices
- Whether the company has adequately disclosed the financial risks of the lending products in question
- Whether the company has been subject to violations of lending laws or serious lending controversies
- Peer companies' policies to prevent abusive lending practices.

**Climate Change and the Environment**

**Investor Network on Climate Risk**
The Investor Network on Climate Risk (INCR) is a network of institutional investors and financial institutions that promotes better understanding of the financial risks and investment opportunities posed by climate change. INCR is coordinated by Ceres, a coalition of investors and environmental groups working to advance sustainable prosperity.

The Investor Network on Climate Risk was launched at the first Institutional Investor Summit on Climate Risk at the United Nations in November 2003. INCR's membership has since grown from 10 investors managing $600 billion in assets to more than 50 investors managing nearly $4 trillion of assets. Members include asset managers, state and city treasurers and comptrollers, public and labor pension funds, including the SBA, foundations, and other institutional investors. INCR leverages the collective power of these investors to promote improved disclosure and corporate governance practices on the business risks and opportunities posed by climate change. INCR has achieved dramatic results, including the following:

- INCR brought together 500 investors, Wall Street and corporate leaders at the United Nations in 2005 for the second Institutional Investor Summit on Climate Risk to address the growing financial threats and opportunities posed by climate change.
- Launched a 10-point action plan, endorsed by 28 investors, which seeks deeper analysis, disclosure and action from Wall Street firms, securities regulators and companies on the business risks and opportunities of climate change.
- INCR members have invested over $1.2 billion of their assets in renewable energy and other clean technology ventures in the past 18 months. The investments cover such technologies as hydrogen fuel cells, ethanol, geothermal facilities and advanced materials.
- Persuaded more than two-dozen Fortune 500 companies to improve their climate policies, practices and disclosure, including leading oil, auto and insurance companies.
- Produced research reports to help investors better understand the implications of global warming. Prominent reports included: an August 2006 report, "From Risk to Opportunity: How Insurers Can Proactively and Profitably Manage Climate Change"; and the March 2006 report entitled, "Corporate Governance and Climate Change: Making the Connection", which analyzed how 100 of the world's largest companies are addressing the business challenges of climate change.
- Published the Global Framework for Climate Risk Disclosure, a standardized set of guidelines for improving corporate disclosure on the risks and opportunities for climate change. The framework was developed in collaboration with investors worldwide.

**SEC Climate Risk Disclosure**
Recent weather events, such as Hurricane Katrina, suggest to some observers that climate change is inevitable and have caused a series of debates on ways to prevent further climate evolution. More specifically, it has been argued that further climate change due to greenhouse gas emissions threatens national security, and could cause danger to civilians, damage infrastructure, and require costly deployment of the military. Therefore, companies have begun to develop policies targeting adoption, as well as risk-reduction and preparedness, which could minimize costs for policy development and implementation in the future and provide economic benefits. Investing in infrastructure firms, for example, would provide an economic benefit, while providing a small way to help avoid the dangers of an evolving climate.[139]

[139] Busby, Joshua, 2007, Mixed Sources, "Climate Change and National Security."

Securities and Exchange Commission (SEC) rules stipulate that "specific known trends, events, or uncertainties that are reasonably likely to have a material effect on a company's financial condition or operating performance" must be discussed as part of a company's SEC filings. Still, SEC rules do not clearly require such disclosure on global warming and carbon dioxide emissions. This results in non-disclosure and uneven disclosure by companies, making it extremely difficult for investors to assess climate risk in their investments.

In April 2004, in coordination with Ceres, 15 leading institutional investors with nearly $800 billion in assets, including eight state treasurers and comptrollers, four labor pension fund leaders, the New York City Comptroller, and the California State Teachers' Retirement System (CalSTRS), called on the SEC to eliminate any doubt that publicly traded companies should be disclosing the financial risks of global warming in their securities filings. In two separate letters to SEC Chairman William Donaldson, the pension fund leaders said that climate change poses material financial risk to many of their portfolio companies and that those risks should be analyzed as a matter of routine corporate financial disclosure to the SEC. While several oil and gas companies have agreed in recent months to include such information in their reports with the SEC, the SEC has not made a formal change in its policy.

In October 2004, in partnership with the Wirth Chair in Environmental and Community Development Policy at the University of Colorado, Ceres convened a leadership forum on "Climate Change Risks and the SEC: Problems and Opportunities" at the Aspen Institute in Washington, DC. Four-dozen participants from public pension funds, businesses, nonprofits, governments, foundations, the United Nations, and academia considered the risks climate change poses to companies and investors, the quality of existing climate risk disclosure, and measures the SEC could take to improve it. Participants agreed that companies' lack of rigorous analysis and reporting of climate risk stems from strategic failures at the highest level, top management and the board room, and too much emphasis on short-term results, a trend reinforced by financial markets. Participants also concluded that the SEC should apply its existing requirements for disclosure of material risks to climate risk and make this clear in an interpretive release. More information is available here: Climate Change Risks and the SEC: Summary Report.

***Ceres Principles: FOR***
Ceres, formerly known as the Coalition for Environmentally Responsible Economics Principles, is a 10-point environmental code of conduct drafted by environmental groups and investor advocates to be adopted by companies in any industry. The issues stressed are protection of the biosphere, prevention of environmentally harmful accidents, conservation of natural resources, proper reduction and disposal of waste, marketing of safe products and services, and appointments of environmental experts to corporate boards.

In a 2010 report by Ceres entitled "The 21st Century Corporation: The Ceres Roadmap for Sustainability[140]," environmentalists and investor advocates outline their 20 key expectations for sustainability by 2020. These 20 expectations fall under four main categories: governance for sustainability, stakeholder management, disclosure and performance. With these initiatives, Ceres hopes to improve board oversight, product transparency and overall performance. By far, the biggest priority of Ceres lies with performance, which will be the ultimate measure for evaluating a company's progress towards achieving sustainability. The SBA supports the Ceres Principles consistent with prudent fiduciary standards.

***Energy and Environment: CASE-BY-CASE***
In conjunction with the Ceres Principles, we are in favor of companies taking actions toward energy conservation and environmental solutions. We generally vote in favor of proposals that ask companies to disclose historical, current, or projected levels of pollutants emitted into the environment and to disclose any control measures to shareowners. The SBA evaluates such proposals, taking into account whether the company has clearly disclosed the following in its public documents:

- **Physical Risk Analysis:**
  Estimates for potential damage to company assets, operations, and supply chain due to climate risk should be provided. Climate risk assessment should include an overview of current climate and weather impacts on company operations, as well as specific risks to operations in the event that climate change results in more extreme weather conditions. In addition, company analysis should include possible means of adapting to such climate risks and the potential costs of adaptation.

- **Regulatory Risk Analysis:**
  Any expected increase in governmental environmental regulation should be evaluated with attention to company-specific impacts. The approximate cost of complying with current or proposed environmental laws, particularly those related to the regulation and reduction of greenhouse gas emissions should be disclosed.[141]

Emissions Disclosure should include the following: 1. Historical, current, and projected greenhouse gas emissions, 2. Company actions to reduce greenhouse gas emissions or other environmental pollutants, and 3. Targets and goals for the reduction of emissions and environmental pollutants.

***Environmental and Sustainability Disclosure: FOR***

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[140] Moffat, Andrea. "The 21st Century Corporation: The Ceres Roadmap for Sustainability." March, 2010.
[141] Ceres Global Framework for Climate Risk Disclosure, October 2006.

With rising awareness of climate risk scenarios, there is increasing shareowner interest in full company disclosure of environmental and sustainability issues. Such issues are now seen as factors likely to impact a company's long term growth and profitability. Therefore, analysis of a company's environmental positioning and related risk exposure is increasingly a required component of the investment decision making process. The 2007 Carbon Disclosure Project provided an appreciation of corporate concern regarding climate risk as 81 percent of S&P 500 respondents considered climate change to present commercial risks for their businesses, compared to only 69 percent that saw climate change as presenting commercial opportunities.[142] A recent study evaluated corporate disclosure of climate change and the likelihood that companies would respond to the Carbon Disclosure Project's request for information. The empirical evidence supports the conclusion that companies that have already been targeted by shareowners, through a shareowner proposal, are more likely to respond to requests for information.[143] This underscores the importance of active shareowner engagement to encourage companies to bolster disclosure regarding sustainability risk management.

The Global Reporting Initiative (GRI) was developed by CERES and the United Nations Developments Programme (UNEP). The GRI allows companies to increase disclosure relevant information to shareowners. The SBA encourages companies to support GRI disclosure standards:

- Generally, the SBA votes FOR shareowner proposals seeking greater disclosure of a company's environmental practices and contingency plans.
- Generally, the SBA votes FOR shareowner proposals which seek greater disclosure of a company's environmental risks and liabilities, as well as company opportunities and strengths in this area.
- Generally, the SBA votes FOR shareowner proposals asking companies to report in accordance with the GRI.

For each proposal, the SBA considers whether such information is already publicly provided by the company. Redundant information requests should be avoided. As such, the SBA may consider voting AGAINST requests for reporting if the company has already disclosed reports to the public, and has responded to the Carbon Disclosure Project.

***Global Warming and Greenhouse Gas Emissions Disclosure: FOR***
Global warming and greenhouse gas emissions create the potential for the most imposing and widespread environmental dangers. Specific recognition and disclosure of a company's preemptive actions in this category are therefore appropriate. Such disclosure allows shareowners to more effectively quantify the company-specific risk, and to assess management's ability to position the company appropriately.

- The SBA votes FOR shareowner proposals seeking disclosure of liabilities or preparation of a report pertaining to global warming and climate change risk.
- The SBA votes FOR shareowner proposals seeking disclosure of how a company will respond to increasing social and regulatory pressures around climate change.

***Energy Efficiency: CASE-BY-CASE***
It has been argued that the green movement is not strictly public sector-driven, and an increased number of companies are beginning to increase their efforts to become more environmentally friendly. While some have implemented mandatory LEED certification, others have provided economic incentives for engaging in energy conservation. In addition, there is no doubt that there are initial economic barriers to this process, but many corporations have begun to voluntarily take part in energy consumption reduction, which will reduce the economic burden in the future. This process can be achieved through better market transparency and measurement standards globally, which will lead to changes in behavior.[144]

Proposals addressing environmental and energy issues generally seek greater disclosure on an issue, or seek to improve a company's environmental practices, in order to protect natural resources. The negative financial implications for companies with poor environmental practices include liabilities associated with site clean-ups and lawsuits, while proponents argue that energy efficient products and clean environmental practices are sustainable business practices that will contribute to long-term shareowner value. Shareowners claim that the majority of independent atmospheric scientists agree that global warming poses a serious problem to the health and welfare of this country, citing the findings of the Intergovernmental Panel on Climate Change. Shareowners argue that companies can report on their greenhouse gas emissions within a few months at reasonable cost.

The SBA votes on proposals requesting a company report on its energy efficiency policies on a CASE-BY-CASE basis, considering:

- The current level of disclosure related to energy efficiency policies, initiatives, and performance measures;
- The company's level of participation in voluntary energy efficiency programs and initiatives;

[142] http://www.riskmetrics.com/pdf/CDP5.pdf.
[143] Reid, Erin and Michael Toffel, "Responding to Public and Private Politics: Corporate Disclosure of Climate Change Strategies," August 2008.
[144] Florance, Miller and Spivey, 2007, "Does Green Pay Off?"

- The company's compliance with applicable legislation and/or regulations regarding energy efficiency; and
- The company's energy efficiency policies and initiatives relative to industry peers.

***Water Supply, Utilization and Conservation Disclosure: FOR***
As a vital natural resource and a key input to operations, sustainable water supply is a critical social and corporate issue. Company disclosure should include crucial water supply issues, as well as contingency planning to ensure adequate supply for anticipated company demand levels.

- Vote for shareowner proposals seeking disclosure of water supply dependency or preparation of a report pertaining to sustainable water supply for company operations.

***Environmental and Sustainability Directives: AGAINST***
Proposals that request a company engage in specific environmental actions are evaluated on the potential to contribute to long-term shareowner value. However, the SBA applies a stricter standard of approval for any proposal which would compel directors to adopt a particular strategic, social, or environmental initiative. Ideally, proposals would be designed to create a meaningful mutual benefit for society and business, leading to improved corporate performance and social integration.[145] The decision to implement such directives is most appropriately made by company management, but shareowner input should assist management in choosing a mutually beneficial path. The SBA generally votes against proposals which compel environmental action. However, proposals which reflect the following criteria would be given additional consideration and may be voted on a CASE-BY-CASE basis:

- The potential to lower costs, increase customer satisfaction, create additional competitive advantages, and increase shareowner value.
- Synergy of the proposal with a company's strategic initiatives and underlying competitive advantage.
- Adaptability of the proposal to a company's current or proposed cost-cutting or emissions-reducing initiatives.
- The degree to which a company's labor and capital resources would be diverted from revenue-generating activities.
- The degree to which additional capital and labor would be required in order to fulfill any proposed mandate.
- Whether the proposal was binding or advisory, with a lesser degree of scrutiny for advisory proposals.
- A clearly defined net environmental benefit once all resource costs of engagement are taken into account.

***Concentrated Area Feeding Operations (CAFO): FOR***
Concentrated animal feeding operations are livestock feeding operations generally defined as facilities containing more than 1,000 animal units (AUs) and/or facilities that allow pollutants associated with animal feeding to enter the local water sources. Environmental advocacy groups have been critical of these operations, citing that the discharge of nitrogen and phosphorus from these facilities pollutes local water sources, ground water, and the soil resulting in significant damage to the ecosystem. Additionally, animal welfare and community groups have also accused these "factory farms" of inhuman treatment of the animals and the displacement of local livestock farmers. Proponents of CAFOs generally argue that these methods are the safest, least costly, and most efficient approach to animal feeding and processing.

Certain shareowner organizations have requested that companies report on the impact of the CAFOs that they source from on the environment and consider the potential financial and legal implications of sourcing from such facilities. Poultry and livestock companies that have received criticism of their CAFO operations note that the facilities are owned and operated by independent entities that are not required to comply with policies dictated by the company. Certain legal decisions have established the precedent that a company can be held liable for the actions of the contract farms it sources from. Fines and remediation expenses stemming from these cases have been significant and could have a notable impact on the companies' operations and shareowner value.

The SBA generally supports resolutions requesting that companies report to shareowners on the risks and liabilities associated with CAFOs unless:

- The company has publicly disclosed guidelines for its corporate and contract farming operations, including compliance monitoring; or
- The company does not directly source from CAFOs.

***Facility Safety (Nuclear and Chemical Plant Safety): CASE-BY-CASE***

[145] From Porter, Kramer, Harvard Business Review, December 2006.

Resolutions requesting that companies report on risks associated with their operations and/or facilities are examined on a case-by-case basis, considering:

- The company's compliance with applicable regulations and guidelines;
- The level of existing disclosure related to security and safety policies, procedures, and compliance monitoring; and,
- The existence of recent, significant violations, fines, or controversy related to the safety and security of the company's operations and/or facilities.

***Operations in Protected Areas: FOR***
Shareowner proposals seeking additional disclosure on a company's operations in regions protected or established under national or international categorization guidelines can be an important mitigating factor when addressing increased risk and oversight. Such areas, which include wildlife refuges, national forests, and IUCN categorized areas, expose companies to increased oversight and the potential for associated risk and controversy. Therefore, restrictions to the company's operations, damaging public opinion, and costly litigation resulting from failure to comply with the requirements associated with protected or categorized regions could have a significant impact on shareowner value. Such proposals will be favored if a company operates in such regions, but fails to provide a level of disclosure comparable to industry peers or accepted standards.

The SBA generally supports requests for reports outlining potential environmental damage from operations in protected regions unless:

- Operations in the specified regions are not permitted by current laws or regulations;
- The company does not currently have operations or plans to develop operation in these protected regions; or;
- The company provides disclosure on its operations and environmental policies in these regions comparable to industry peers.

***Recycling: CASE-BY-CASE***
A coalition of socially responsible investors, environmentalists, and religious groups has promoted the concept of extended product responsibility, a responsibility shared by industry, consumers, and the government for the environmental impact of a product over its life cycle. Producers were encouraged to prevent pollution and reduce resource and energy use in each stage of the company's product life cycle, including the end of the life cycle. The campaign originated with the beverage industry and in 2002 was extended to the computer industry.

The SBA votes on proposals to adopt a comprehensive recycling strategy on a case-by-case basis, taking into account:

- The nature of the company's business and the percentage affected;
- The extent that peer companies are recycling;
- The timetable prescribed by the proposal;
- The costs and methods of implementation; and
- Whether the company has a poor environmental track record, such as violations of applicable regulations.

***Renewable Energy: CASE-BY-CASE***
Requests for reports on the feasibility of developing renewable energy sources are generally supported unless the report is duplicative of existing disclosure or irrelevant to the company's line of business. However, the SBA generally votes against proposals requesting that the company invest in renewable energy sources as such decisions are best left to management's evaluation of the feasibility and financial impact that such programs may have on the company.

***Animal Testing and Welfare Policies: CASE-BY-CASE***
Currently, the SBA generally ABSTAINS from voting on these types of proposals.

***Equal Employment: FOR***
The SBA believes proposals that promote and attempt to enhance or improve equal employment should be supported.

***Corporate Board Diversity: FOR***
Shareowners should encourage companies to diversify the make-up of their boards of directors. Proponents of board diversity ask that the company's board of directors or nominating committee make a greater effort to seek out qualified women and minorities for the board. In addition, most resolutions ask that the company report back to the shareowners on its efforts and issue a public statement of commitment to board inclusiveness.

***Sexual Orientation and Domestic Partner Benefits: CASE-BY-CASE***
The SBA generally votes in favor of proposals seeking to amend a company's equal employment opportunity (EEO) statement in order to prohibit discrimination based on sexual orientation, unless the change would result in excessive costs for the company. However, proposals to extend company benefits to, or eliminate benefits from domestic partners, are typically opposed given that benefits decisions should be left to the discretion of the company.

**International Issues, Labor Issues and Human Rights**

***China Principles: AGAINST***
The U.S. Business Principles for Human Rights of Workers in China are designed to commit companies to human rights and labor standards defined by the International Labor Organization (ILO) and the United Nations Covenants on Economic, Social and Cultural Rights, and Civil and Political Rights.

1. No goods or products produced within our company-owned facilities or those of our suppliers shall be manufactured by bonded labor, forced labor, within prison camps, or as part of reform-through-labor or reeducation-through-labor programs.

2. Our facilities and suppliers shall adhere to wages that meet workers' basic needs, and to fair and decent working hours, at a minimum adhering to the wage and hour guidelines provided by China's labor laws and policies.

3. Our facilities and suppliers shall prohibit the use of corporal punishment, as well as any physical, sexual, or verbal abuse or harassment of workers.

4. Our facilities and suppliers shall use production methods that do not negatively affect the occupational safety and health of workers.

5. Our facilities and suppliers shall not call on the police or military to enter their premises to prevent workers from exercising their rights.

6. We shall undertake to promote the following freedoms among our employees and the employees of our suppliers: freedom of association and assembly, including the rights to form unions and to bargain collectively; freedom of expression, and freedom from arbitrary arrest or detention.

7. Employees working in our facilities and those of our suppliers shall not face discrimination in hiring, remuneration, or promotion based on age, gender, marital status, pregnancy, ethnicity, or region of origin.

8. Employees working in our facilities and those of our suppliers shall not face discrimination in hiring, remuneration, or promotion based on labor, political, or religious activity, or on involvement in demonstrations, past records of arrests or internal exile for peaceful protest, or membership in organizations committed to non-violent social or political change.

9. Our facilities and suppliers shall use environmentally responsible methods of production that have minimum adverse impact on land, air, and water quality.

10. Our facilities and suppliers shall prohibit child labor, at a minimum complying with guidelines on minimum age for employment within China's labor laws.

Eight ILO conventions have been identified by the ILO's Governing Body as being fundamental to the rights of human beings at work irrespective of levels of development of individual member states.
The ILO Core Conventions and the dates of their adoption are:

- Forced Labour—1930
- Freedom of Association and Protection of the Right to Organize—1948
- Right to Organize and Collective Bargain—1949
- Equal Remuneration—1951
- Abolition of Forced Labour—1957
- Discrimination (Employment and Occupation)—1958
- Minimum Age Convention—1973
- Elimination of the Worst Forms of Child Labour—1999

Furthermore, companies are expected to work cooperatively with human rights organizations both to ensure that their enterprises and suppliers are in compliance with these principles. They will also issue an annual statement to the Human Rights for Workers in China Working Group (CWG) detailing their efforts to uphold these standards and to promote these basic freedoms. Proponents of this resolution claim that making all lawful efforts to implement or increase activity on each of the China Principles will help address poor working conditions and human rights abuses at Chinese factories that produce goods for U.S. firms. Companies that mistreat workers can impair productivity, raise turnover costs, and increase supply chain instability. It is also beneficial as companies can avoid being blacklisted by states and municipalities, many of whom have limited their contracts with companies that fail to adopt strict labor standards in countries recognized for committing gross human rights violations. Labor violations can also strategically alienate host communities for future enterprises as well as expose the companies to reputation and brand risk in their core markets.

However, companies generally argue against having to join another initiative or adopting separate codes of conduct for every country in which they conduct business. Some also fail to see any benefit of CWG participation in terms of membership fees or in needing any guidance from the organization on how to address labor and human rights issues in China. In addition, poor

enforcement of labor laws by local governments due to bribery and conflicting interests in maintaining gross-domestic-product (GDP) growth while improving working environments also hinder worker advocacy groups. Traditionally, firms in the retail and extractive industries are most commonly scrutinized by advocates of the China Principles in light of poor working conditions and the use of sweatshop labor.

The SBA generally votes AGAINST proposals to implement the China Principles unless there are serious controversies surrounding the company's operations in China and if the company does not have a code of conduct with standards similar to those declared by the International Labor Organization (ILO).

***Codes of Conduct: CASE-BY-CASE***

Workplace codes of conduct are designed to safeguard workers' rights in the international marketplace. Advocates of workplace codes of conduct encourage corporations to adopt global corporate standards that ensure minimum wages and safe working conditions for workers at U.S. companies that operate factories in developing countries. Furthermore, U.S. companies that outsource portions of their manufacturing operations to foreign companies are expected to ensure that the products received from those contractors do not involve the use of forced labor, child labor, or sweatshop labor. A number of companies have implemented vendor standards, which include independent monitoring programs with respected local human rights and religious organizations to strengthen compliance with international human rights norms. Approximately 20 percent of large capitalization companies in global equity markets have adopted some form of labor code for its suppliers, covering forced (child) labor, workplace discrimination, worker safety, and freedom of association. [146, 147]

Recent evidence shows how sourcing from overseas vendors with labor problems can lead to significant public relations problems for U.S. companies. In addition, more companies have faced consumer boycotts and legal fines as consumers have focused on human rights and labor standards. Studies have shown that 75 percent of respondents would avoid shopping in stores that sold goods produced in sweatshops. [148] Another study found that 76 percent of Americans would pay more for sweatshop-free and child labor-free clothing. [149]

Several organizations, including Amnesty International, the Fair Labor Association (FLA), and the Ethical Trading Initiative (ETI), have developed labor codes and related principles which have been adopted by several multi-stakeholder initiatives and used in their evaluation of supply chain management. Generally, Amnesty International principles are not as comprehensive in some areas, relative to the FLA and/or ETI. The SBA favors incorporation of operational monitoring, code enforcement, and robust disclosure mechanisms. [150] The SBA prefers to see companies with supply-chain risks proactively engage an independent monitoring organization to provide objective oversight, and publicly disclose such evaluation. Although there is no generally recognized standard for companies to use, a very good starting point is participation and membership in the FLA.

In 2011, the United Nations Human Rights Council approved the "Guiding Principles on Business and Human Rights," which represent the culmination of six years of research and extensive consultation involving governments, companies, business associations, investors, and other non-governmental organizations around the world.

Proposals to implement certain human rights standards and policies at company facilities are evaluated by the SBA on a CASE-BY-CASE basis. In examining these proposals, the following should be considered:

- The degree to which existing human rights policies and practices are disclosed
- Whether or not existing policies are consistent with internationally recognized labor standards
- Whether company facilities are monitored (and how)
- Company participation in fair labor organizations or other internationally recognized human rights initiatives, such as endorsement of the Guiding Principles on Business and Human Rights by the United Nations Human Rights Council.
- The company's primary business model and methods of operation
- Proportion of business conducted in markets known to have higher risk of workplace labor right abuse
- Whether the company has been recently involved in significant labor and human rights controversies or violations
- Peer company standards and practices
- Union presence in company's international factories

***Community Impact Assessments: CASE-BY-CASE***

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[146] RiskMetrics Group, Corporate Social Issues Reporter, April 2008. Study encompassed over 1,800 companies within the S&P 500 index, the Toronto Stock Exchange 300 index, and the MSCI EAFE index ex-Japan. Study identified that the highest risk industries included Retailing, Food & Staples Retailing, Consumer Durables & Apparel, Household & Pensonal Products, and Food, Beverage & Tobacco.
[147] "Factory Labour Standards in Emerging Markets: An Investor Perspective," F&C Asset Management, REO Research Series, January 2009.
[148] PepsiCo 2002 proxy filing, and PepsiCo s April 21, 2002 letter to RiskMetrics Group (RMG). As You Sow Foundation and Walden Asset Management March 31, 2002 letter to Coca-Cola shareowners.
[149] Marymount University Center for Ethical Concerns, 1999 National Survey: The Consumer and Sweatshops. Arlington, VA, November 1999.
[150] "Incorporating Labor and Human Rights Risk into Investment Decisions." Aaron Bernstein, Harvard Labor and Worklife Program, Occasional Paper Series No. 2, September, 2008.

Community impact assessment proposals ask companies to evaluate and report on their policies and practices on a range of issues that may include requests to review potential environmental and public health damage resulting from a certain regional operation or requests for companies to study and develop a report on the potential environmental and public health damage of its operations.

Because companies find themselves operating in markets where stakeholders have competing interests, the possibility of social, cultural, and environmental impacts resulting from operations is a credible risk that many companies face. As social and environmental controversies, fines, and litigation can have a significant negative impact on a company's financials, public reputation, and license to operate in developing markets, many companies that operate in such markets develop internal controls aimed at mitigating their exposure to these risks by enforcing, supplementing, and in many cases, exceeding local regulations and laws. Many companies also establish outreach programs to the community, stakeholders, and government to promote a collaborative approach to public health and sustainable development.

The SBA employs a case-by-case approach on requests for reports outlining the potential community impact of company operations in specific regions, considering:

- Current disclosure of applicable risk assessment report(s) and risk management procedures
- The impact of regulatory non-compliance, litigation, remediation, or reputational loss that may be associated with failure to manage the company's operations in question, including the management of relevant community and stakeholder relations
- The nature, purpose, and scope of the company's operations in the specific region(s)
- The degree to which company policies and procedures are consistent with industry norms

***Internet Privacy and Censorship: CASE-BY-CASE***
Proposals seeking to adopt policies to protect freedom of access to the internet are fast becoming a social issue garnering the attention of shareowners. Resolution sponsors argue that the Chinese government is using IT companies' technologies to track, monitor, identify, and, ultimately, suppress political dissent. In the view of proponents, this process of surveillance and associated suppression violates internationally accepted norms outlined in the U.N. Universal Declaration of Human Rights. Such restrictions not only violate human rights, but they also decrease the quality of service provided by companies in the industry and threaten the integrity and viability of the industry as a whole. As such, proponents believe that companies like Yahoo, Google, Microsoft, Cisco Systems and Oracle, with operations in such markets should develop adequate standards that can be used when conducting business in countries with authoritarian governments.

The difficulty for IT firms is that the capabilities cited, monitoring, interception, keyword searches, and recording of Internet traffic are inherent in a wide range of products that companies sell to government agencies, state-owned communications or IT entities, or resellers throughout the world. They are designed to protect the integrity of Internet communications networks against theft, sabotage, viruses, and unlawful intrusion, especially in an age where governments face constant attacks against their national IT infrastructure.

Active measures to address these concerns are generally aimed at government policy makers as well as the major Internet and technology companies that operate in these markets. On one hand, the companies suggest that by providing their products, they are providing access to information that would not otherwise be available. Furthermore, management at these companies suggest that they are bound to respect the laws and policies of the countries in which they operate, and that failure to defer to such regulations could lead to the loss of license to operate in a country. As such, while industry dialogue on how to address these issues is taking place, management at most companies in the private sector believe that this issue would be better addressed by a more universal, public policy approach.

Conversely, some human rights advocates and organizations believe that it is incumbent on private companies to use their technological and economic influence to encourage such governments to relax censorship policies and increase freedom of expression. Moreover, these organizations believe that generally accepted international agreements protect such freedoms, and assert that private industry has a moral imperative to develop explicit policies for operating in these markets that would protect human rights or at least inform the public of instances where legal agreements require a company to allow forms of censorship or monitoring. In the event that such policies are not feasible or cannot be implemented, some stakeholders have suggested that companies should cease business relationships with government agencies that are unwilling to protect these basic human rights. Finally, many of the advocates who support more stringent human rights protections related to Internet access believe that companies that fail to develop appropriate policies for operating in challenging markets are actually limiting their long-term opportunities by "fragmenting" technology in such a manner that would restrict the growth of universal communication and technology standards globally in favor of market specific solutions. Such market specific solutions, advocates contend, could lead to ethically unsound practices and financially unsustainable over the long term.

Various measures have been suggested to discourage companies from abetting Internet censorship abroad. Rep. Christopher Smith (R-N.J.) introduced the Global Online Freedom Act in the 109th and 110th Congress, most recently in January 2007. Much like the resolution proposed at Yahoo, the act would require U.S. companies doing business abroad to take steps to protect their users from government retaliation and to alert users of instances of censorship. The bill has been assigned to a committee. Human Rights Watch, a global human rights advocacy organization, has also proposed a voluntary code for companies doing business in nations that censor the Internet.

The SBA generally votes in favor of disclosure-based resolutions relating to Internet policies unless the company has already taken proactive steps to address the issue in question. In evaluating the merits of the proposal, the SBA examines the level of current applicable disclosure on the topic, the level of stakeholder engagement, nature and scope of the company's operations as well as the scope of the proposal, applicable legislation, and the company's past history of controversy and litigation as it pertains to human rights. These guidelines will seek to encourage disclosure that is not overly costly or burdensome to the company, while including pertinent information for shareowners to evaluate the potential risks associated with the management of these emerging human rights concerns.

***Operations in High-Risk Markets: CASE-BY-CASE***
In recent years, concerned shareowners of companies operating in regions that are politically unstable, including terrorism-sponsoring states, have requested both a withdrawal of operations in a high-risk market as well as having requested a report on operations in a high-risk market. Such concerns are focused over how their investment may, in truth or by perception, support potentially oppressive governments. Operations in these regions, proponents contend, may lead to potential reputational, regulatory, or supply chain risks as a result of operational disruptions.

Countries determined by the U.S. Secretary of State to have repeatedly provided support for acts of international terrorism are designated pursuant to three laws: the Export Administration Act, the Arms Export Control Act, and the Foreign Assistance Act. Taken together, these laws can lead to the four categories of sanctions. These authorities may also penalize persons and countries engaging in certain trade with state sponsors of terrorism. Currently, there are five countries designated under these authorities: Cuba, Iran, North Korea, Sudan, and Syria.

The SBA votes on a CASE-BY-CASE basis when evaluating requests to review and report outlining the company's potential financial and reputation risks associated with operations in "high-risk" markets, such as a terrorism-sponsoring state or otherwise, taking into account:

- The nature, purpose, and scope of the operations and business involved that could be affected by social or political disruption
- Current disclosure of applicable risk assessment(s) and risk management procedures
- Compliance with U.S. sanctions and laws
- Consideration of other international policies, standards, and laws
- Whether the company has been recently involved in significant controversies or violations in "high-risk" markets.

***Outsourcing/Offshoring: CASE-BY-CASE***
Foreign outsourcing, the transfer of work from a domestic facility to a foreign market to achieve greater efficiencies, has developed into one of the most contentious shareowner action issues in recent years. Also known as "off-shoring," foreign outsourcing first gained hold in manufacturing industries as management at toy, apparel, and other production-heavy companies found that they could increase profit margins by assigning manufacturing contracts to facilities in markets where labor costs were a fraction of those in the United States. However, in the last few years, this approach has become more prevalent in the service and technology industries, prompting the question: Is foreign outsourcing beneficial to the economy in general, and shareowner value in specific, over the long term? While thorough disclosure is an important part of sound corporate governance policy and serves to protect shareowner interests, there are also certain costs and considerations associated with reporting.

As such, the relevance of the proposal to the company's core business shall be considered and the SBA shall ensure that the requested report is not duplicative of existing disclosure. This approach to policy and analysis of outsourcing proposals allows the SBA to independently consider the risks and opportunities of foreign outsourcing at a specific company, and to provide a vote recommendation consistent with leading corporate governance standards and considering the long-term impact on shareowner value.

Proposals calling for companies to report on the risks associated with outsourcing shall be voted on a CASE-BY-CASE basis, considering the risks associated with certain international markets, the utility of such a report to shareowners, and the existence of a publicly available code of corporate conduct that applies to international operations.

***Conflict Minerals: CASE-BY-CASE***
As a part of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, the SEC mandates that public users of 'conflict minerals' sourced from the Democratic Republic of Congo (DRC) annually report on the scope of their due diligence into their suppliers in addition to making disclosures about any payments made to foreign governments for the acquisition or production of these resources. "Conflict minerals" are defined by the act to include columbite-tantalite (coltan), cassiterite, gold, wolframite, or their derivatives or any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the DRC. Because of the nature of the conflict in the DRC, the acquisition, extraction, and production of many natural resources often violate the basic human rights of workers through labor practices, poor working conditions, systematic rape, and slave labor. In addition to moral concerns, companies can expose themselves to reputational and supply chain risks. Basic disclosure and due diligence and reporting requirements can increase transparency to the board of directors and external auditors as well as inform shareholders of potential risks. However, compliance costs may be costly and economically infeasible for smaller companies or firms that do not significantly rely on DRC-sourced resources. The SBA will take a CASE-BY-CASE approach to voting based on a company's reliance on conflict minerals and the economic feasibility of compliance costs.

***Northern Ireland (MacBride Principles): FOR***
The MacBride Principles call on U.S. companies with operations in Northern Ireland to promote fair employment practices there. Signatories of the MacBride Principles must make reasonable, good faith efforts to abolish all differential employment criteria whose effect is discrimination on the basis of religion.[151] The situation in Northern Ireland continues to reflect religious discrimination in employment.

The SBA supports the MacBride Principles as part of Section 121.153, F.S. and feels the principles should be adopted and implemented. The SBA is in favor of firms reporting their relationships in and with Northern Ireland.

***High-Performance Workplace: FOR***
A "high-performance workplace" can be described as one that provides workers with the information, skills, incentives, and responsibility to make decisions essential for innovation, quality improvement, and rapid response to change. The SBA believes that high-performance workplaces are correlated with both productivity and long-term financial gain. Empowering workers makes employees more productive and their companies more competitive, hopefully enhancing shareowner value in the process. The SBA votes FOR these resolutions.

***Military Production: CASE-BY-CASE***
These resolutions focus on asking defense contractors to report on the export of military goods and services. Such disclosures may involve sensitive and confidential information. Foreign military sales (FMS) constitute a considerable portion of the business conducted by major U.S. defense contractors. Military arms exports may be accompanied by "offset" agreements, in which companies rebate a portion of the purchase price back to the purchasing country. These agreements are known as offsets because they help offset the cost of the purchase itself and may take a variety of forms, both direct and indirect offsets. Direct offsets are those that involve defense articles or services as part of the military export, such as subcontracting to businesses in the purchasing nation, transfers of technology, financial assistance, and joint ventures. Indirect offsets can involve goods and services unrelated to the military export. Supporters of military production shareowner proposals have noted that a U.S. Commerce Department study reported that between 1993 and 2006, U.S. companies reported export sales of $84.3 billion and that related offset agreements were $60 billion, or 71.2 percent of export sale value.[152]

Shareowner proponents typically argue that taxpayers incur the costs of these agreements, especially when they exceed the dollar value of a foreign military sale itself—because they finance the original research and development of the military equipment whose technology or manufacturing license is subject to transfer or grant. Information about offset agreements is closely guarded by companies participating in such deals. Defense manufacturers are required to submit annual summaries of all offset agreements to the U.S. Department of Commerce, and to provide itemized details regarding new offset agreements they enter into on a yearly basis. The Department of Commerce uses this information to prepare an annual report for Congress.

Weapons sales by U.S. defense contractors to other governments are subject to a number of regulatory frameworks. U.S. defense contractors have two avenues to pursue foreign sales of weapons-related products and services. First, they may sell weapons to foreign countries indirectly through foreign military sales (FMS), a process by which weapons manufacturers sell to the U.S. Department of Defense (DOD), which subsequently negotiates agreements with foreign governments. Under the FMS system, DOD contractors do not negotiate with DOD clients. Alternatively, U.S. defense contractors can apply for export licenses through the U.S. Department of State in order to participate in direct commercial sales (DCS). In doing so, companies negotiate directly with a purchasing agent or country and must register with the U.S. State Department and apply for an export license. To prevent illegal defense exports and technology transfers, the U.S. State Department works with other governmental bodies to implement end-use monitoring checks. From a regulatory perspective, the U.S. Department of State's Directorate of Defense Trade Controls (DDTC), in accordance with the Arms Export Control Act (AECA) and the International Traffic in Arms Regulations (ITAR), is charged with controlling the export and temporary import of defense articles and defense services covered by the United States Munitions List (USML).

Proponents of foreign military sales resolutions generally argue that weapons sales by U.S. defense contractors create unintended conflicts worldwide. Proponents maintain that military contractors have an obligation to weigh the ethical dimensions of their sales, in some cases above the effect of these sales on shareowner value, in order to increase global security. These proposals may ask companies to establish a board committee to develop ethical criteria for their military contracts and to report to shareowners on those criteria and on details of the company's foreign military sales.

Defense contractors claim that defense and foreign policy decisions, including those pertaining to arms sold abroad, fall within the purview of the legislative and executive branches of government, which are responsible for determining and advancing the United States' security interests. Moreover, the kind of information typically sought by shareowner proponents is, in their opinion, highly sensitive and confidential. Disclosure of such information could put the company at a disadvantage in the competitive bidding process and also could breach contractual and confidentiality agreements.

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[151] Northern Ireland Statistics and Research Agency, Source Book 2001 and 2000 Labour Force Survey Religion Report, March 2001.
[152] According to the U.S. Department of Commerce - Bureau of Industry and Security s report, "Offsets in Defense Trade: Twelfth Report to Congress", released in December 2007, U.S. companies entered into 582 offset agreements with 42 countries related to export sales totaling $84.3 billion between 1993 and 2006. In 2006 alone, U.S. defense contractors reported 44 new offset agreements with 20 countries, with a total value of approximately $3.4 billion. These agreements equaled 70.9 percent of the $4.8 billion in related export contracts.

***Nuclear Proliferation: CASE-BY-CASE***
Some shareowners are concerned about profitability and safety of operating nuclear power plants, storage and disposal of spent nuclear fuel, depleted uranium, and plant decommissioning. Nuclear utilities are concerned about deregulation and the fact they may not generate enough cash flow to justify their continued operations.

There have been an increasing number of shareowner-sponsored resolutions asking a company to cease production or report on the risks associated with the use of depleted uranium munitions or nuclear weapons components and delivery systems, including disengaging from current and proposed contracts. Such contracts are monitored by government agencies, serve multiple military and non-military uses, and withdrawal from these contracts could have a negative impact on the company's business.

Depleted uranium is a heavy metal considered to be a low-level nuclear waste metal comprised of what is left after most of the fissile radioactive isotopes of uranium are used. The material is relatively inexpensive; however, because of its extremely high density, it has been used for certain military and industrial applications.

There has been some scientific concern over the long-term health effects of exposure to depleted uranium. Some peer reviewed studies have suggested that exposure to depleted uranium can result in birth defects and complications, difficulty breathing, kidney damage, and some types of cancer. Exposure to depleted uranium can be through inhalation, ingestion, or exposure to fragments of the metal.

Due to its relatively short history, scientific research does not find a consensus on depleted uranium's long-term health and environmental effects. Some, including the Pentagon, assert that there is a minimal link, if at all, between depleted uranium exposure and illnesses among veterans exposed to depleted uranium weapons; others assert depleted uranium radiation and toxicity can/may cause detrimental long-term health damage. Conversely, opponents of depleted uranium usage argue that its use should be postponed until scientific data can validate its safety. Meanwhile, the military argues that no other metal can be as effective in warfare as depleted uranium.

***Political Contributions and Expenditure Reporting: CASE-BY-CASE***
These resolutions address the issue of corporate non-partisanship and disclosure of contributions related to political campaigns, political action committees (PACs), and other special interest organizations. We believe companies should provide data on the amount and rationales for making such donations. Some organizations, primarily labor unions, are addressing "soft dollar" policies and some are requesting shareowner approval of campaign contributions.

Due to the controversial 5-4 Supreme Court ruling in *Citizens United v. Federal Election Committee*, which removed federal limits on corporate political spending, shareowner demand for disclosure of political contributions is greater than ever[153]. The number of shareowner proposals for improved disclosure is expected to increase as critics argue that the removal of federal limits on corporate political spending will increase the pressure on companies to give. Their argument is that removing federal limits on contributions will only make these contributions riskier. A December 2011 paper examined pre- and post-Citizens political activity and found that in most industries, such activity correlates negatively with measures of shareowner power (concentration, rights), positively with signs of managerial agency costs (corporate jet use by CEOs), and negatively with shareowner value (industry-relative Tobin's q).[154]

One standard for corporate disclosure and board procedure was advocated by The Conference Board (TCB), which recommends corporations review their political expenditures to, "examine the proposed expenditures to ensure that they are in line with the company's values and publicly stated policies, positions, and business strategies and that they do not pose reputational, legal, or other risks to the company." [155] The Center for Political Accountability (CPA) continues its advocacy for political spending reporting by U.S. companies and other shareowner groups continue to submit resolutions covering more narrow and prescriptive items such as lobbying disclosure, shareowner approval of contribution amounts, and reporting on trade association spending.

The SBA typically evaluates proposals to improve the disclosure of a company's political contributions and trade association spending on a CASE-BY-CASE basis, considering the following factors:

- Recent significant controversy or litigation related to the company's political contributions or governmental affairs;
- The public availability of a company policy on political contributions and trade association spending including information on the types of organizations provided support;
- The business rationale for supporting political organizations; and
- The board oversight and compliance procedures related to such expenditures of corporate assets.

***Political Nonpartisan: CASE-BY-CASE***
These resolutions call for companies to maintain scrupulous political neutrality to avoid entanglements detrimental to its business. They ask that the appearance of coercion in encouraging its employees to make political contributions be avoided.

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[153] Aguilar, Melissa Klein. "SEC Ruling Could Lead to More Shareholder Proposals." The Filing Cabinet. Compliance Week. January 26, 2010.
[154] Coates, John C. "Corporate Politics, Governance, and Value Before and After Citizens United" Harvard Law School. December 23, 2011.
[155] Paul DeNicola, Bruce F. Freed, Stefan C. Passantino, and Karl J. Sandstrom. "Handbook on Corporate Political Activity." March 2011, Conference-Board.org.

The SBA examines proposals requesting the company to affirm political nonpartisanship in the workplace on a CASE-BY-CASE basis. We will generally not favor such resolutions provided that:

- The company is in compliance with laws governing corporate political activities; and
- The company has procedures in place to ensure that employee contributions to company-sponsored political action committees (PACs) are strictly voluntary and not coercive.

***Prepare Additional Reports: CASE-BY-CASE***
These resolutions ask companies to prepare additional reports to shareowners such as equal employment. The SBA favors such proposals when they are worthy of management's attention and not disclosed to shareowners.

***Sweatshop Labor: CASE-BY-CASE***
These resolutions usually ask for a report on supplier standards that the company uses when purchasing goods abroad or to adjust the salaries of contract workers to "ensure adequate purchasing power and a sustainable community wage." The SBA evaluates such proposals in a similar manner to Codes of Conduct (please see above policy narrative).

***U.S. Business and Health Care Reform: CASE-BY-CASE***
Shareowners may at times ask companies to evaluate and report on the impact of various health care reform proposals. These resolutions ask the board of directors to examine the company's position on the important public policy issue of national health care and to report how the company's health care position will affect the economic, social, and personal welfare of shareowners, employees, customers, suppliers, communities and the nation as a whole. The scope of these shareowner proposals as well as future legislation is very broad. The other relevant issues generally examined include the company's exposure to health care costs, its industry, its disclosure about its costs, its responsiveness to the issue and its lobbying activities regarding health care.

Frequently, proposals for healthcare reform rely on the principles stated in a 2004 Report of the Institute of Medicine (IOM), which in part recommended that healthcare should be universal, continuous and affordable to families.[156] It is accepted that employee health has a positive relationship with productivity and employee morale, making this issue an important one for companies to consider. Healthcare costs have risen dramatically in recent years as well, making it harder for companies and individuals to pay escalating premiums and attracting attention at the federal level, including calls for government intervention and reform. The rate of increase of healthcare costs has greatly exceeded those of inflation and wage growth. Companies are faced with the dilemma of rising costs of providing health care coverage or declines in worker health and productivity, as well as problems with employee morale, if provision of such coverage is reduced.

In evaluating proposals to adopt Health Care Reform policies, we consider the information that is publicly available from a company to determine whether the company has given due consideration to the issue and has been transparent in its deliberations on the issue. Given the complex nature of the costs and benefits of health care and the national importance level attached to this issue, the health care principles proposed by a shareowner or recommended by the IOM may be overly restrictive to set upon any one company. We acknowledge the negative effect uninsured workers can have on a company's productivity and morale, but believe that company management and boards are better informed in most cases to judge the appropriate level of coverage to offer. We note that the Institute of Medicine's report was a call specifically to the policy leaders of the nation, specifically the President and Congress, to act immediately in finding a solution to this widening crisis. This issue is vexing to all companies alike, and in general we refrain from imposing specific solutions with uncertain benefit to shareholders upon individual companies, particularly while the issue is being scrutinized at the state and federal level.

***U.S. Business and Human Rights Guidelines: CASE-BY-CASE***
Shareowners have asked companies to adopt guidelines for determining how management will make decisions on investing in or withdrawing from countries where there is a pattern of ongoing and systematic violations of human rights. These proposals target specific companies because of business operations most recently in Burma (brutal military regime) and China ("laogai" forced prison labor). While observers may condemn any nation found guilty of unfair human rights practices, the SBA currently abstains from voting on these resolutions.

## MUTUAL FUND PROXIES

Like shareowners of publicly held corporations, shareowners of mutual funds are allowed a voice in fund governance. While some funds proscribe annual meetings in their charter documents, all funds must call special meetings of shareowners to amend substantive governance matters such as board composition, investment advisory agreements, distribution agreements, and changes to fundamental investment restrictions. To this end, mutual fund managers issue and solicit proxies similar to the way that stock corporations do. Voting the SBA's mutual fund proxies is an integral component of the SBA's corporate governance program.

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[156] The IOM report and summary can be found here: http://www.iom.edu/CMS/3809/4660/17632.aspx.

It is important that shareowners exercise care when voting their proxies. In more practical terms, mutual fund proxies raise issues that differ substantially from those found in the proxies of public companies. Though mutual fund proxy holders are also frequently asked to elect trustees and ratify auditors, most of the other agenda items are related to the special nature of this type of security. For example, mutual fund investors are asked to vote on changing fundamental investment policies and restrictions and approving or amending investment advisory and subadvisory agreements. As with elections of directors of corporations, it is preferable to see mechanisms that promote independence, accountability, responsiveness, and competence in regards to the mutual fund. One empirical study has shown a positive link between the quality of a mutual fund's board and its future performance and Sharpe ratio. [157]

The investment objectives of mutual funds vary significantly. While some funds seek to maintain a stable net asset value per share, others focus on generating a continuous flow of income through dividends or capital appreciation. Therefore, the risk borne by shareowners of mutual funds varies, with those funds offering the chance of the highest return typically also involving the greatest potential for loss.

**Fund Investment Objectives and Fundamental Policies**
The investment objectives of mutual funds vary significantly and are expressed in rather general terms. Examples from currently authorized FRS Investment Plan mutual funds include:

- Seeks to obtain as high a level of current income as is consistent with preservation of capital and liquidity
- Seeks maximum total return consistent with preservation of capital and prudent investment management
- Seeks long-term growth of capital and income without excessive fluctuations in market value
- Seeks long-term growth of capital and future income rather than current income
- Seeks long-term capital growth.

A mutual fund's investment process is typically identified in its declaration of principal investment strategies and risks and fundamental policies and restrictions. The principal investment strategy identifies the financial market asset class or sub-sector in which the fund typically invests, e.g. the fund normally invests at least eighty percent of its assets in stocks included in the S&P 500. Conversely, a fundamental investment restriction identifies prohibited activities, e.g. the fund may not invest more than twenty-five percent of the value of its total assets in the securities of companies primarily engaged in any one industry.

**Fund Structure**
Beyond a fund's investment objectives and fundamental policies, fund structure may also affect shareowner value. The majority of investment funds are open-end investment companies, meaning that they have no set limit on the number of shares that they may issue.

**Share Structure**
A change in fee structure or fundamental investment policy requires the approval of a majority of outstanding voting securities of the fund, which under the Federal Investment Company Act of 1940 is defined as the affirmative vote of the lesser of either sixty-seven percent or more of the shares of the fund represented at the meeting, if at least 50 percent of all outstanding shares are represented at the meeting, or fifty percent or more of the outstanding shares of the fund entitled to vote at the meeting. Failure to reach this "1940 Act majority" subjects the funds to additional solicitation and administrative expenses.

***Election of Directors: CASE-BY-CASE***
Similar to the election of directors of corporations, it is preferable to see mechanisms that promote independence, accountability responsiveness, and competence within the mutual fund. The SBA generally votes FOR directors up for election. However, votes on director nominees should be determined on a CASE-BY-CASE basis, considering the following factors:

- Director independence and qualifications
- Board structure
- Attendance at board and committee meetings
- Number of mutual funds' boards and/or corporate boards (directorships) upon which a nominee sits

The SBA WITHHOLDS VOTES FROM DIRECTORS WHO:

- Attended less than 75 percent of the board and committee meetings without a valid reason for the absences
- Ignored a shareowner proposal that was approved by a majority of the votes cast for two consecutive years
- Ignored a shareowner proposal that was approved by a majority of the shares outstanding
- Are interested directors and sit on the audit or nominating committees

[157] Carl R. Chen and Ying Huang, "Mutual Fund Governance and Performance: A Quantile Regression Analysis of Morningstar s Stewardship Grade," Corporate Governance: An International Review, 2011, 19(4): 311-333.

- Are interested directors and the full board serves as the audit or nominating committee OR the company does not have one of these committees
- The SBA may withhold from audit committee directors when the company does not provide annual auditor ratification, especially in the case of substantial non-audit fees or other poor governance practices.

***Converting Closed-end Fund to Open-end Fund: CASE-BY-CASE***
The SBA evaluates conversion proposals on a CASE-BY-CASE basis, considering the following factors:

- Past performance as a closed-end fund
- Market in which the fund invests
- Measures taken by the board to address the discount
- Past shareowner activism, board activity, and votes on related proposals.

***Proxy Contests: CASE-BY-CASE***
The SBA votes on proxy contests on a CASE-BY-CASE basis, considering the following factors:

- Past performance relative to its peers
- Market in which fund invests
- Measures taken by the board to address the issues
- Past shareowner activism, board activity, and votes on related proposals
- Strategy of the incumbents versus the dissidents
- Independence of directors
- Experience and skills of director candidates
- Governance profile of the company
- Evidence of management entrenchment.

***Investment Advisory Agreements: CASE-BY-CASE***
Votes on investment advisory agreements should be determined on a CASE-BY-CASE basis, considering the following factors:

- Proposed and current fee schedules
- Fund category/investment objective
- Performance benchmarks
- Share price performance as compared with peers
- Resulting fees relative to peers
- Assignments (where the advisor undergoes a change of control)

When considering a new investment advisory agreement or an amendment to an existing agreement, the proposed fee schedule should be compared with those fees paid by funds with similar investment objectives. Proposed fees that are significantly higher than fees for similar funds may be justified if the fund in question has performed admirably or if management explicitly states other factors that contribute to the higher rate. Any increase in advisory fees of more than 10 percent of the prior year's fees are judged on a CASE-BY-CASE basis to determine its long-term impact on shareowner value, and management must offer a detailed, specific and compelling argument justifying such a request.

***Approve New Classes or Series of Shares: FOR***
The SBA generally votes FOR the establishment of new classes or series of shares.
Boards often seek authority for a new class or series of shares for the fund to grow the fund's assets. The ability to create classes of shares enables management to offer different levels of services linked to the class or series of shares that investors purchase. Also, fee structures can be varied and linked to the series of shares, which allows investors to choose the purchasing method best suited to their needs. The board can use separate classes and series of shares to attract a greater number of investors and increase the variety of services offered by the fund.

***Change Fundamental Restriction to Non-fundamental Restriction: CASE-BY-CASE***
Proposals to change a fundamental restriction to a non-fundamental restriction should be evaluated on a CASE-BY-CASE basis, considering the following factors:

- The fund's target investments
- The reasons given by the fund for the change
- The projected impact of the change on the portfolio

***Change Fundamental Investment Objective to Non-fundamental: AGAINST***
The SBA generally votes AGAINST proposals to change a fund's fundamental investment objective to a non-fundamental investment.

The SBA maintains that shareowners should maintain control over this aspect of a fund because a fund's fundamental investment objective represents its raison d'etre, which often is the very reason that the shareowners originally invested in the fund. Formal

shareowner approval should not be difficult to obtain in the event that the original investment objective of the fund proves unfeasible.

***Change in Fund's Sub-classification: CASE-BY-CASE***
Votes on changes in a fund's sub-classification should be determined on a CASE-BY-CASE basis, considering the following factors:

- Potential competitiveness
- Current and potential returns
- Risk of concentration
- Consolidation in target industry

***Disposition of Assets/Termination/Liquidation: CASE-BY-CASE***
Votes on dispositions of assets/terminations/liquidations should be determined on a CASE-BY-CASE basis, considering the following factors:

- Strategies employed to save the fund
- The fund's past performance
- Terms of the liquidation

***Authorize the Board to Hire or Terminate Sub-advisors without Shareowner Approval: AGAINST***
The SBA generally votes AGAINST proposals authorizing the board to hire or terminate sub-advisors without shareowner approval. Typically, the management company will seek authority, through the investment advisor, to hire or terminate a new sub-advisor, modify the length of a contract, or modify the subadvisory fees on behalf of the fund. These investment decisions are normally made with majority shareowner approval, as determined by Section 15 of the Investment Company Act of 1940. However, funds may apply to the SEC for exemptions to this rule, and the SEC often grants these exemptions. These exemptions are usually structured so that they do not apply to the investment sub-advisory agreement that is in place at the time, but apply to any future subadvisory agreement into which the fund enters.

***Distribution Agreements: CASE-BY-CASE***
Votes on distribution agreements should be determined on a CASE-BY-CASE basis considering the following factors:

- Fees charged to comparably sized funds with similar objectives
- The proposed distributor's reputation and past performance
- Competitiveness of the fund in the industry
- Terms of the agreement

As long as a proposed distribution agreement does not call for an excessive fee rate, such agreements may be supported as a means of increasing asset size and realizing economies of scale.

***Master-Feeder Structure: FOR***
The SBA generally votes FOR the establishment of a master-feeder structure. The master-feeder fund structure achieves economies of scale from sharing fixed expenses of portfolio management among a larger asset base. In addition, this structure can facilitate fund administration and greater diversification by means of a larger portfolio of securities than could be achieved by individual funds.

***Mergers: CASE-BY-CASE***
The SBA generally evaluates mergers and acquisitions on a CASE-BY-CASE basis, determining whether the transaction enhances shareowner value by giving consideration to:

- Resulting fee structure
- Performance of both funds
- Continuity of management personnel
- Changes in corporate governance and the impact on shareowner rights

***Change the Fund's Domicile: CASE-BY-CASE***
The SBA votes on fund reincorporations on a CASE-BY-CASE basis, considering the following factors:

- Regulations of both states
- Required fundamental policies of both states
- Increased flexibility available

When changing the domicile of a fund, the SBA considers the corporate laws of the state in which the fund is seeking to reincorporate as they apply to management investment companies. Shareowner rights can be particularly limited in certain states, including Delaware, Maryland, and Massachusetts.[158]

***1940 Act Policies: CASE-BY-CASE***
Votes on 1940 Act policies should be determined on a CASE-BY-CASE basis, considering the following factors:

- Potential competitiveness
- Regulatory developments
- Current and potential returns
- Current and potential risk

The SBA generally votes FOR these amendments as long as the proposed changes comply with the current SEC interpretation and do not fundamentally alter the investment focus of the fund.

***Name Change Proposals: CASE-BY-CASE***
The SBA votes on name change proposals on a CASE-BY-CASE basis, considering the following factors:

- Political and economic changes in the target market
- Consolidation in target market
- Current asset composition

***Changes to the Charter Document: CASE-BY-CASE***
The SBA votes on changes to the charter document on a CASE-BY-CASE basis, considering the following factors:

- The degree of change implied by the proposal
- The efficiencies that could result
- The state of incorporation
- Regulatory standards and implications

The SBA generally votes AGAINST any of the following changes:

- Removal of shareowner approval requirement to reorganize or terminate the trust or any of its series
- Removal of shareowner approval requirement for amendments to the new declaration of trust
- Removal of shareowner approval requirement to amend the fund's management contract, allowing the contract to be modified by the investment manager and the trust management, as permitted by the 1940 Act
- Allow the trustees to impose other fees in addition to sales charges on investment in a fund, such as deferred sales charges and redemption fees that may be imposed upon redemption of a fund's shares
- Removal of shareowner approval requirement to engage in and terminate subadvisory arrangements
- Removal of shareowner approval requirement to change the domicile of the fund

***Shareowner Proposals to Establish Director Ownership Requirement: CASE-BY-CASE***
The SBA generally favors the establishment of a director ownership requirement and considers a director nominee's investment in the company as a critical factor in evaluating his or her candidacy. This decision should be made on an individual basis and not according to an inflexible, across-the-board standard. As a related matter, if the director has invested in one fund of the family, he is considered to own stock in the fund.

***Shareowner Proposals to Terminate Investment Advisor: CASE-BY-CASE***
Votes on shareowner proposals to terminate the investment advisor should be determined on a CASE-BY-CASE basis, considering the following factors:

- Performance of the fund.
- The fund's history of shareowner relations.
- Performance of other funds under the advisor's management.

***Shareowner Proposals to Reimburse Shareowners for Expenses Incurred: CASE-BY-CASE***
Voting to reimburse proxy solicitation expenses should be analyzed on a CASE-BY-CASE basis. In cases where the dissident position is supported, believing it to be in the best interests of shareowners, the SBA generally votes FOR reimbursing such proxy solicitation expenses.

***Shareowner Proposals to Adopt a Policy to Refrain from Investing in Companies that Substantially Contribute to Genocide or Crimes against Humanity: CASE-BY-CASE***

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[158] Lucian Bebchuk and Alma Cohen, "Firms' Decisions Where to Incorporate." National Bureau of Economic Research Working Paper 9107, August 2002.

The SBA will evaluate such proposals with an adherence to the requirements and intent of the Protecting Florida's Investments Act (the PFIA, §215.473 of the Florida Statutes), which prohibits investment in companies involved in proscribed activities in Sudan or Iran.