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SDCERA clarifies investment officer termination

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Unfortunately the *U-T San Diego's* January 25, 2012 article "Pension strategist when challenged on risk: "Bring it on!" omits key facts and includes a misleading headline, which requires clarification.

The headline creates the impression that SDCERA's Portfolio Strategist is the focus of the article. In fact, it's an article about a Civil Service Commission hearing to determine whether the San Diego County Employees Retirement Association (SDCERA) had a legitimate basis for terminating investment officer Jeff Baker's employment.

The core issue is simple: Mr. Baker was terminated for repeatedly violating SDCERA's *Data and Information* policy. When he was confronted with the first violation in October 2009, Baker vowed not to break the policy again. However, SDCERA later discovered that despite his promise, Baker had violated the policy again. During the hearing neither Baker nor his attorney refuted this evidence.

Unfortunately, the case Baker and his attorney presented was unrelated to the basis of the termination. They focused on Baker's baseless whistleblower claim, which two independent bodies, the County Office of Internal Affairs and the Civil Service Commission, have already determined had no probable cause because the information had already been publicly disclosed. This tactic appears to be an attempt to distract from the real issues of the case:

- Like any well-managed organization, SDCERA has policies establishing expectations for employee behavior
- Employees are expected to abide by their employer's policies
- SDCERA warned Baker when he violated the policy the first time
- Upon repeated violation of policy, Baker was held accountable

In addition to repeatedly violating policy, Baker was uncooperative with the investigation into the violations, despite warnings that failure to cooperate would be considered insubordination. Under County rules, insubordination can result in disciplinary action up to and including termination.

SDCERA strives to uphold the public trust by operating with integrity and fairness. To succeed in this, our employees must uphold these standards as well. Baker demonstrated he could not be counted on to uphold these standards, which led to his termination.

Investment Officer Termination: Myths and Facts

MYTH: Baker was terminated for exposing risk in excess of SDCERA policy limits.

FACT: Baker was terminated for repeatedly violating policy. His termination had nothing to do with any comments he made concerning risk limits. In the Civil Service hearing, Baker did not contest that he had committed the policy violations upon which his termination was based; rather, he attempted to excuse them by arguing that he was a whistleblower (see below).

MYTH: Baker was a whistleblower who had a responsibility to bring the risk limits to light.

FACT: Baker made statements about already public information; being a whistleblower requires revealing previously undisclosed information.

The Board of Retirement received several reports about the volatility of the Hoisington Investment both before SDCERA entered into the investment and on several occasions afterward. Specific examples include: the volatility of the Hoisington investment was discussed with the Board in detail before the investment was approved on August 19, 2010; details of the risk in the Treasury Program versus the benchmark were discussed with the Board at the February 17, 2011 Board meeting; and the modeling of the Hoisington investment was discussed with the Board at the December 16, 2010 Board meeting—all long before Mr. Baker committed his violations of the information policy. The Board was well informed and understood the nature and performance of the investment.

MYTH: SDCERA's portfolio is risky.

FACT: In July 2010, SDCERA implemented a strategically diversified asset allocation that significantly lowered risk and is focused on moderate but steady gains in up markets and protecting assets during volatile markets. SDCERA's one-year performance through September 30, 2011 was in the top 5% compared to its peers (public plans over \$1 billion). The fund is simultaneously lowering risk, generating consistently positive returns and outperforming its peers.

The article's reference to "risk limits" is actually referring to tracking error, which measures the difference between an investment's performance and its benchmark. A benchmark is an estimate of how an investment will perform. Differences may result from market volatility or because the benchmark doesn't fully reflect the unique features of the investment. The asset class in question is Treasuries—widely considered to be a safe investment. The tracking error showed a particular investment, Hoisington, performed differently than the 10-year treasuries benchmark. These differences were expected and should not be interpreted to indicate inherent riskiness of the investment strategy. Hoisington has proven to be a good investment choice: it has played a key role of SDCERA's downside protection strategy, which helped protect SDCERA's 21% fiscal year gains during recent market volatility.

MYTH: SDCERA took on higher risk than allowed.

FACT: The Investment Policy Statement focuses on actual (realized) tracking error based on 36-months of experience. Violating policy would require 36-months of actual SDCERA experience (that is, SDCERA would need to be invested for 36-months)—not the different information Baker used. SDCERA had only been invested in Hoisington for three months at the time Baker made his calculations. As to the High Yield program, Baker himself wrote an email trivializing this issue in January 2011.

MYTH: The Office of Internal Affairs investigation into Baker's whistleblower claim should be discounted because it didn't verify facts.

FACT: The Office of Internal Affairs took testimony and reviewed slides, videos and documents presented to the Board of Retirement before reaching its conclusion that the information Baker claimed to disclose had already been provided to the Board in public session. The notion of being a whistleblower requires revealing previously undisclosed information: making statements about already public information fails to meet the test.

MYTH: The First Amendment right to freedom of speech allows Baker to release SDCERA information to the media and others.

FACT: When public employees are operating in their official capacity, they are not protected under the First Amendment. Baker's own testimony shows he was operating in his official capacity. In any event, the First Amendment does not prevent a public employer from disciplining employees who violate policies that further a legitimate interest, such as SDCERA's *Data and Information* policy.