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Litigation Update
Investments and Pension Oversight Committee
August 9, 2013

Bartlett, et al. v. Cameron et al. (COLA challenge)

Petitioners filed a Petition for a Writ of Mandamus, seeking an order from the New Mexico Supreme Court directing the trustees of the Educational Retirement Board (“ERB”) to pay a Cost of Living Adjustment (“COLA”) without giving effect to the modifications made by SB 115. In effect, the Petitioners challenged the constitutionality of the COLA modification that was enacted as part of SB 115. That legislation included a two stage reduction in the COLA when the Educational Retirement Fund (the “Fund”) is less than 100 percent funded.

In their response, the ERB trustees argued that mandamus was not appropriate because Article XX, Section 22 of the New Mexico Constitution does not unambiguously prohibit changes to the retirement plan, including the COLA. Rather, the Constitution grants a limited or qualified vested property right to members of a State retirement system who meet the minimum service requirements of that system while also stating that nothing in Section 22 shall be construed to prohibit modifications to retirement plans that enhance or preserve their actuarial soundness. The COLA modification was made for the purpose of enhancing, and thereby protecting, the actuarial soundness of the Fund. Balancing the interest of the State, and the members themselves, in maintaining the Fund’s actuarial soundness against the Petitioners’ property rights weighs in favor of the constitutionality of the COLA modification. The Response also argued that, fundamentally, the Petitioners were asking the Supreme Court to substitute its judgment for that of the Legislature in formulating public policy, a role that is properly left to the Legislature. The Supreme Court ordered the parties to present oral argument on the matter on Wednesday, September 4, 2013.

AFSCME, et al. v. State et al. (contribution shift)

Plaintiff filed a complaint in June 2009, challenging the constitutionality of the contribution shift that the Legislature made beginning July 1, 2009. All of plaintiffs’ claims other than that asking the court to find the contribution shift was a ‘taking’ were dismissed. The ERB produced documents responsive to the Plaintiff’s discovery requests in the summer of 2011. The parties are working on a scheduling order. The ERB understands that counsel for the parties are seeking to schedule a trial for early 2014.

State ex rel. Foy v. Austin Capital Management

Plaintiff filed a lawsuit under the Fraud Against Taxpayers Act, NMSA 1978. §§ 44-9-1 to -14 (“FATA”), in 2009 alleging that beginning in 2003 the defendants, which include investment management firms, investment advisors, placement agents, the former chair of the ERB and the former State Investment Officer, engaged in improper activity, including misrepresenting investment products and services and paying kickbacks and bribes, that resulted in the ERB and the State Investment Counsel (“SIC”) losing hundreds of millions of dollars. Plaintiffs also alleged that the two state defendants conspired with the other defendants to steer investment contracts to management firms that were willing to pay kickbacks. Plaintiffs sought to recover under FATA on behalf of the ERB and the SIC. The ERB is not a defendant in this case. Applying the reasoning of the district court in *State ex rel. Foy v. Vanderbilt Capital Advisors* (see below), the district court in *Austin Capital* found that the clause in FATA providing for its retroactive application prior to the July 1, 2007 effective date of the legislation violated the *ex post facto* clauses of the federal and New Mexico constitutions. The district court severed that clause from FATA and allowed the action to proceed as regards conduct that allegedly occurred on or after July 1, 2007. The Court of Appeals affirmed the district court’s action. The Plaintiff’s appealed to the New Mexico Supreme Court, which has granted *certiorari* and will consider the matter.

State ex rel. Foy v. Vanderbilt Capital Advisors

Plaintiff filed this lawsuit under FATA in 2008 alleging improper activity similar to that alleged in *State ex rel. Foy v. Austin Capital Management* in connection with \$40 million invested by the ERB and \$50 million invested by the SIC in Vanderbilt Financial Trust. A substantial portion of the \$90 million was invested in the unrated ‘equity strip’ portion of collateralized debt obligations (“CDOs”) that held securitized mortgages originated by other parties that were sold to Vanderbilt. The equity strips received the cash flows remaining after payments were made on ‘rated’ securities created from the mortgages. The ERB investment was made in 2006; it wrote the entire investment off in 2007. The district court found that retroactive application of FATA was unconstitutional under the *ex post facto* clauses of both the federal and state constitutions and dismissed the suit as to events that occurred prior to July 1, 2007. The Supreme Court’s decision in *State ex rel. Foy v. Austin Capital Management* will be determinative of whether FATA can be retroactively applied. There has been no further action in this suit to date.

Vanderbilt Settlement

On a related note, the SIC and the ERB reached a settlement with Vanderbilt Capital Advisors, LLC, in which Vanderbilt agreed to pay \$20 million to the SIC and \$4.5 million to the ERB in settlement of those agencies claims against it. A motion to approve the settlement was filed with the district court in *State ex rel. Foy v. Vanderbilt Capital Advisors*. The court determined that it will not address the motion pending the Supreme Court’s resolution of the appeal in *State ex rel. Foy v. Austin Capital Management*. Resolution of that appeal may have bearing on the settlement agreement with Vanderbilt Capital Advisors.

Hill v. Vanderbilt Capital Advisors

Plaintiff filed a class action suit, or alternatively, a derivative action, in January 2010 in state district court in Santa Fe regarding the investment in Vanderbilt Financial Trust described above, as well as investments allegedly influenced by Aldus Equity and Saul Meyer. The suit alleges that the investments were influenced by pay-to-play schemes orchestrated by the defendants and seeks damages allegedly resulting from these investments. For purposes of bringing a derivative action, the Educational Retirement Fund was named as a nominal defendant in the action. The Fund, however, would not be liable for damages allegedly sustained by the Fund itself because of the actions of the other defendants. The suit was removed to federal district court, which dismissed it for lack of jurisdiction and remanded it to state district court. The Tenth Circuit Court upheld the dismissal in late 2012. The plaintiffs have requested a scheduling order.

Hammes v. Vanderbilt Capital Advisors

This lawsuit was filed in state district court in Santa Fe by the same plaintiffs' counsel as the *Hill* action. The complaint contains many of the same allegations as in the former action; however, it was drafted so as to avoid removal of the case to federal district court. The case is currently stayed. Again, for purposes of bringing a derivative action, the Fund was named as a nominal defendant.

Foy v. New Mexico Educational Retirement Board, et al. (IPRA)

The plaintiff brought suit alleging that the ERB was not producing the voluminous materials that had been requested in an IPRA. At that time, the ERB was providing materials in response to a federal grand jury subpoena as well as in response to the IPRA. Responding to the subpoena was the priority matter. Following completion of the response to the subpoena, production of materials responsive to the IPRA was completed. Production of those materials was completed in 2011. The suit remains pending. The ERB's position is that it did not violate IPRA.

New Mexico Educational Retirement Board v. Renaissance Private Equity Partners, Aldus Equity Partners, et al.

The ERB filed suit in 2010 in state district court against its former private equity advisory firm, Saul Meyer, Mark Correra and others seeking damages resulting from the defendants' wrongful acts and breaches of contract. The case is currently in the discovery phase. The lawsuit arose in part because of Meyer's admission in the course of pleading guilty to an indictment secured by the New York Attorney General that on a number of occasions, Aldus had recommended investments to the State of New Mexico that were pushed on Meyer by politically-connected individuals in New Mexico.