Twisted Priorities

Putting Wall Street & Chicago money managers interests over Police Officers & Taxpayers. Preliminary Findings of Forensic Investigation, Police Benefit Annuity Fund of Chicago Commissioned by Chicago Police Pension Accountability Group

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I. Executive Summary

WORST FUNDED NON TRANSPARENT

The Chicago Policemen's Annuity and Benefit Fund (PABF) - commonly referred to as the "Chicago Police Pension Fund" is one of the worst funded public pension plans in the U.S. today and in U.S. history. Its funding ratio as of today is only 23%.

It is also so damaged by a total lack of transparency that it puts the interest of Wall Street & Chicago Investment Managers over its own current and retired officers. PABF has hidden $10s of millions in investment fees, while denying payment for a disabled officer's wheelchair.

Key Finding:

PABF has long abandoned transparency, choosing instead to collaborate with Wall Street firms and others to eviscerate Illinois public records laws and avoid accountability to stakeholders. Predictably, billions have been squandered over time as transparency has ceased to be a priority.

Retired Chicago Police Officer Rosemarie Giambalvo initiated the call for a complete forensic audit of the Chicago Police Pension fund in February 2020 seeking full transparency and accountability. Rosemarie also founded the CPD Pension Board Accountability Group consisting of over 2600 retired, widows, and active officers who signed two petitions calling for the audit. Rosemarie was told during the February 2020 Pension Board meeting that, *"whoever wants an audit must pay for it?"* One trustee then stated, *"it would cost $20,000"*. Rosemarie notified the group members and within two weeks raised the full $20,000 from the group to pay for the audit costing the pension board nothing. Justin Kugler stated, *"he didn't care how much money they raised, we will not consent to a forensic audit!"* After the elected trustees refused to address the concerns of their underfunded pensions (22% in 2020), the group agreed to hire myself Christopher Tobe, a Forensic Investigator to which I began the forensic audit report upon being hired by Rosemarie Giambalvo and the group.

The board and staff of the Chicago Policemen's Annuity and Benefit Fund (PABF) have gone out of their way to conceal and block information for this report. They illegally denied most of our Freedom of Information Act (FOIA) requests only providing small amounts of information which should have been previously disclosed on the web page.

Regardless, we have come up with a report that can have an impact by providing more transparency and accountability for the operations of the fund.

The current FBI investigation of the Pennsylvania teachers' pension has many similarities. My findings are very consistent with the 2014 SEC "pay to play" investigation initiated by the Chicago Board of

Alderman.[1] Also it has similar potential findings to those the SEC found exposing securities fraud around Illinois pension valuations in 2013. [2]

Alternative investments in public pensions which include hedge funds, private equity and real estate have been coming under increased scrutiny for their valuation, performance numbers and excessive management fees, as illustrated in an ongoing FBI investigation in Pennsylvania. Unfortunately, the PABF is loaded with these same high-risk, high fee alternative assets. Pulitzer winner and former New York Times writer Gary Rivlin wrote in his Illinois pension expose in 2018, *"Those with the highest exposure to high-fee alternatives are also the most vulnerable to pay-to-play."*[3]

Chicago Police is the only pension fund I know of in 30 years' experience that an unqualified trustee has inserted himself as Chief Investment Officer (CIO). The fund's board structure itself creates this endless cycle of underfunding and adds to the lack of transparency. This board structure facilitates excessive conflicts of interest with the mayor's immediate political goals of a city budget and political fundraising overshadowing long-term fiduciary goals. One of the nation's leading public pension experts Alicia Munnell described the pension situations in Illinois and Kentucky: *"Fiscal discipline simply appeared not to be part of the state's culture."*[4]

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[1] *https://www.bondbuyer.com/news/chicago-aldermen-want-sec-probe-of-mayors-campaign-contributions*

[2] *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171513202#.Up48l9JDtRs*

[3] *https://theintercept.com/2018/10/22/illinois-governor-bruce-rauner-pensions/*

[4] *http://www.bloomberg.com/news/2012-10-23/pension-funding-scare-won-t-frighten-all-states.html Peter Orszag*

FUNDING

The fund went from a mediocre 61% funding level in 2003 to a mere 22% in 2019, which ranks it as one of the worst in US Pension History. It is at by many counts the 3rd worst large public pension in US history after the smaller Chicago Firefighter's Pension Fund and the Kentucky Employees plan.

Defunding the Police Pension has been happening for the last 17 years. Chicago city government has used the PABF like a credit card, underfunding it by approximately $300 million a year, resulting in an $11 billion balance in unfunded liabilities.

City officials have lobbied the State of Illinois so that, while the Actuarial Required Contribution for 2019 was $1.037 billion, the State allowed them to "short" the pension borrowing around $300 million. This was accomplished by allowing the City to claim the statutory required contribution was only $737 million. The amount of annual contributions defined under P.A. 99-0506 does not even cover normal cost, let alone the interest on the unfunded liability for the next 11 years. This means the unfunded liability is projected to increase to a high of $12.2 billion in 2030, when contributions are finally sufficient to start reducing the unfunded liability.

To add insult to injury, the city even underfunds the pension more than the statutory amount, blatantly breaking the law, with no consequences. While the law has an intercept function that works for some cities, it seems deliberately rigged to let Chicago off the hook with intercepts so small they are immaterial.

Chicago is frequently considered as being the most likely major U.S. city to file bankruptcy following Detroit. Officers have already had retiree health benefits related to plan cut significantly. Retirees, disabled officers, and widows, along with currently active police officers, have valid concerns that their pension benefits could possibly be slashed by as much as half in a municipal bankruptcy.

LACK OF TRANSPARENCY

Transparency in government has long been acknowledged as essential to a healthy democracy in America. All 50 states also have public records laws which allow members of the public to obtain documents and other public records from state and local government bodies.

Absent full disclosure by investment firms to pension boards and staffs, these individuals cannot fulfill their fiduciary duty to diligently safeguard pension assets. Full disclosure of investment information to the public is necessary for the stakeholders to understand the investment program, as well as evaluate whether pension fiduciaries are prudently performing their duties.

The *overwhelming majority* of the most critical disclosure information we requested was *summarily* denied or redacted. Even the names of the underlying managers of fund of funds were denied. Regarding fee and contract information on investment managers, it appears that PABF repeatedly permitted the investment firms involved to unilaterally determine what to disclose under Illinois law.

The lack of cooperation by PABF is more surprising given that PABF is well aware that this forensic review of the pension was commissioned, as well as paid for, by hundreds of participants, and had the stated objective of improving management and oversight of the pension. Pension fiduciaries solely concerned with the interests of participants and beneficiaries should welcome, not oppose, a free independent review by nationally recognized experts in pensions.

Almost all Public pensions produce a Comprehensive Annual Financial Report (CAFR) which provides more transparency for the financials of the plan and is strongly recommended by the Government Finance Officers Association. PABF trustees decided that a CAFR was needed neither in 2019 nor 2020. It is not known why the trustees declined to provide financial transparency to the one of the worst funded plans in U.S. History.

Alarmingly, our investigation reveals that the Chicago Police Pension (PABF) has long abandoned transparency, choosing instead to collaborate with Wall Street firms and others to eviscerate Illinois public records laws and avoid accountability to stakeholders. Predictably, hundreds of millions have been squandered on excess fees and poor performing managers as transparency has ceased to be a priority.

HIDDEN FEES

PABF has failed to monitor and fully disclose investment fees and expenses. Fees and expenses could be 10 times more than they disclose ($7.425mm) on their own 2020 Mitchell Titus Audit. This so-called audit omits dozens of managers and their fees from its fee disclosure page. [5] The Wall Street Journal just highlighted deficiencies in audit firms like Mitchell Titus on similar issues. [6] The fees disclosed from the 2020 financials only account for around half the assets and are only those of the lower fee managers. Truth in Accounting only assuming fees of 200 basis points thought fees to be

[5] *https://chipabf.org/pdfs/audit/final_pabf_fs_2019.pdf*
[6] https://www.wsj.com/articles/weak-oversight-plagues-audits-of-billions-in-private-assets-11628847000

at least $30 million a year. Using a Oxford study I assume fees and expenses for alternative managers of 5% or 500 basis points, undisclosed fees could be as high as $70 million or more a year. [7]

It is well established that sponsors of retirement plans have a fiduciary duty to ensure that the fees their plans pay money managers for investment advisory services are reasonable.

PABF has hired several managers who have had SEC issues with fee disclosure. There is no evidence that PABF closely monitors these fees as the SEC found that more than half of about 400 private-equity firms it examined charged unjustified fees and expenses without notifying investors.

$2 TO $3 MILLION IN FEES PAID TO WALL STREET EVERY YEAR FOR DOING NOTHING

From the PABF Financial Statements ending 2020:

NOTE 6 UNFUNDED INVESTMENT COMMITMENTS The Fund had unfunded commitments of approximately $157 million and $108 million on December 31, 2020 and 2019, respectively, in connection with real estate, infrastructure, private equity and collective commingled fund investments.[8]

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[7] *https://www.hbs.edu/ris/Publication%20Files/20-073_32c98338-75e6-4174-947f-510b16236e6d.pdf*

https://www.institutionalinvestor.com/article/b1lxv2czrsv9y7/The-Inconvenient-Fact-Behind-Private-Equity-Outperformance

https://www.ft.com/content/377a8850-d72b-40a2-94d0-0abf1848bca2

[8] *Not https://chipabf.org/wp-content/uploads/2021/06/PABF_FS_2020.pdf*

Assuming PABF pays fees of 2 percent on total unfunded commitments, this amounts to an annual waste of approximately $3 million a year in 2020, and $2 million a year in 2019 essentially “Money for Nothing”. This is in stark contrast to their almost joy in denying benefits of a fraction of this amount to disabled officers.

GHOST MANAGERS

It is not uncommon for public pensions to have sometimes hundreds of hidden “Ghost managers” inside hedge funds and private equity funds of funds that are not named, and fees that are not disclosed. PABF may have over 100 ghost managers in funds of funds. In 2009 hundreds of plans in hedge fund of funds were shocked to find that one of their “ghost managers” was the Madoff fund.

What is uncommon is that PABF takes this lack of disclosure to the next level, “ghosting” dozens of other alternative managers in private equity, hedge funds and real estate from their financial statements and other disclosures.

On the last page of the official PABF 2019 Audit done by Mitchell Titus, it lists the mangers in the fund and how much they paid in fees. The list looked small to me, so I compared it to the 12/31/2019 NEPC report listing the performance of the managers. To my shock there were 32 managers on NEPC not on Financials with over $500 million in assets in the highest fee alternative assets.[9] On the 12/31/2019

e 6 page pg. 34 POLICEMEN’S ANNUITY AND BENEFIT FUND OF CHICAGO (A Component Unit of the City of Chicago) Notes to Financial Statements Years Ended December 31, 2020 and 2019 34 https://chipabf.org/wp-content/uploads/2021/06/PABF_FS_2020.pdf

[9] *https://chipabf.org/wp-content/uploads/2021/04/Investment-Performance-4th-Q-2019.pdf*

Northern Trust Custody report there are 45 managers not mentioned on the fee page of the 2019 Mitchell Titus Audit.

PAY TO PLAY

Pulitzer winner and former New York Times writer Gary Rivlin on his Illinois pension expose in 2018 wrote *"Those with the highest exposure to high-fee alternatives are also the most vulnerable to pay-to-play."*[10]

An inquiry into public records by a Chicago Alderman in 2014 disclosed that former Mayor Rahm Emanuel received campaign donations of over $600,000 from investment managers who manage accounts for the PABF and other city funds. This led to a SEC investigation initiated by a Chicago City Alderman. [11]

One manager, Madison & Dearborn, was not disclosed in public financial documents because it was in a Fund of Funds. It was only disclosed in a separate economic development document for Illinois related investments required by the state for each Illinois based pension plan. This document provides the names of all Illinois based "ghost managers" even those in funds of funds. We sent FOIA requests to both the Chicago Police and the state and they have redacted all these potential names from this report to avoid disclosure. The Illinois Municipal Plan treats this report as a public disclosure, and it is freely available unredacted on the web.

Public documents reveal that over $200,000 in donations have been made to Mayor Lightfoot by Madison Dearborn who has managed

[10] *https://theintercept.com/2018/10/22/illinois-governor-bruce-rauner-pensions/*

[11] *https://www.ibtimes.com/chicago-mayor-rahm-emanuel-accepted-campaign-contributions-financial-firms-managing-1723396*

investments for Chicago pensions and may still. Chicago Police continues to invest with Brinson partnerships, and Gary Brinson was a large doner to Mayor Emanual. Real Estate mogul John Grayken of Lone Star funds (a major Ghost Manager of PABF) has donated in the past to some officials. Under full transparency of "Ghost Managers" we expect that more conflicts with political donations will appear.

PERFORMANCE & VALUATION

Investment performance has been poor for the Chicago Police Pension over most recent time periods. If you compared performance for the 5 years ending 12/31/20 for PABF of 8.8% to a 70% S&P 500 index 30% Barclays Intermediate at 11.9% you have a significant shortfall. Approximating a $2.6 billion in assets, the shortfall over the last 5 years has been around $403 million dollars, or over $80 million a year. Only under more transparency will we be able to tell how much of this was from excessive fees versus bad investment performance.

Overall PABF investment performance has been poor for the 3 years ending 12/31/20 they ranked in near the bottom in the 90th percentile, for the 5 years ending 12/31/20 they ranked in the 81st percentile. This was mainly driven by their high allocation to high fee high risk alternatives.

While I believe that the NEPC performance numbers could be exaggerated, PABF seems to have wanted to enhance them more for 2020.

There are major performance discrepancies of the 2020 calendar year between the NEPC report presented at the board meeting of 10.64% in April 2021, and the Mitchell Titus Audit presented at the

June 2021 meeting of 12.9%.   That is an extra $45 million in return that miraculously appeared.[12]

Valuation is a major focus of the current FBI investigation in Pennsylvania.   In Chicago, the city has an incentive to overvalue the portfolio, to reduce immediate budget demands on the city, and to lower the costs of city bonds by keeping a higher credit rating.

The alternative investment managers have is an incentive to overvalue the portfolio since it increases their immediate performance bonuses. There are no effective controls on this potential overvaluation.

Alternative managers make up their own valuations as noted in the fine print in the financial statements for several years that we tested: *"Hedge fund, venture capital, private equity, infrastructure, and certain opportunistic investments are reported at estimated fair value as determined by the general partner of the investment vehicle."* The CPA firm admits that there are no controls on alternative mangers creating their own valuations.

It is likely performance is overstated due to omitting badly performing "ghost managers" and over valuation of alternatives.

Richard Ennis the actual former consultant for Chicago Police Pension writes underperformance in Public Pension plans is mostly caused by the excessive fees in alternative investments. [13]

[12] *$2.6 billion x 1.75%*

[13] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3883370

POOR MANAGEMENT & GOVERNANCE

The board structure itself creates this endless cycle of underfunding and adds to lack of transparency. The mayor and or the aldermen, should appoint independent members of the community to the board instead of city financial staff whose job is the day-to-day function of the government. These city financial officials are put into a difficult conflict of interest between short term budget needs of the city and the long-term needs of the police pension. This board structure inserts such excessive conflicts of interest as the mayor's immediate city budget policy and political fundraising both of which can overshadow the long-term fiduciary goals of running a pension.

Almost all pensions hire professionals for their two top positions, executive director or CEO and chief investment officer (CIO). The chair of the board of trustees, Thomas Beyna, an active-duty Chicago police officer, has served as CIO for the last 30 months. Beyna has no investment or any financial qualifications to be chief investment officer. We have been able to document erratic behavior moving in and out of funds and asset classes when non-professionals were CIO. This behavior is not consistent with fiduciary duty and helps explain the poor investment performance of recent years.
One of the Trustees running for reelection touted the following Fund accomplishments, I find his claims misleading at best

"12.29% vs. 6.75% actuarial return." This spin is very common by underperforming plans in bull markets as for FY 2021 the US Stock market as measured by the Russell 3000 was up 40% and Chicago Police only up 25%

"Market capital from $3.3 billion to $3.4 billion" Again most other plans would have done better in a bull market as this reflected underperformance.

“Reduced fund expenses by $800,000 and remained more than 12% under budget” I am not seeing this in financials as ……… Investment expenses are up in the $millions. The 12% budget savings may have something to do with not filling the Chief Investment Officer slot which has cost the fund $millions.

“Increased funding ratio from 22% to 23.2% with expected 24.1%” Again most other plans would have done better in a bull market.

“Improved the funds website and accountability” My findings are the opposite. PABF has dramatically reduced transparency and accountability more than any fund in the country by discontinuing the publication of a CAFR. Many investment managers are not even listed on the web page. Even more investment managers have been removed from NEPC performance reports.

These claims by the trustee are misleading at best.

The CPD Accountability group has received numerous complaints from retirees, disabled officers and widows concerned with the staff, trustee, and management mistreatment of retired and disabled police officers. We describe this in more detail in our subsection on disability.

Detail of the audited financial statements from 2019 shows poor expense control of the administration of the fund. Personnel salaries & benefits went from $1.827 mm in 2018 to $2.796 mm or 53% in 2019. We can find no explanation for this increase.

CONCLUSION

The toxic mix of the defunding of the police pension, conflicted and high-risk investments, and the poor management of the PABF demand the transparency and accountability this report will provide.

REPORT DETAIL

FUNDING

The fund is at a 23% funding level in 2020,[14] which ranks it as one of the worst in US Pension History. It is, by many counts, the third worst large public pension in US history after the smaller Chicago Firefighter's Pension Fund and the Kentucky Employees plan and not counting Puerto Rico.

The Police Pension has been defunded for the last 17 years, and the practice continues. Chicago city government has used the PABF like a credit card, underfunding it by approximately $300 million a year, resulting in an $11 billion balance in unfunded liabilities.

Municipal officials have lobbied the State of Illinois to not pay the actuarially required contribution. So that, while the actuarially required contribution to PABF for 2019 was $1.037 billion, the state allowed the city of Chicago to borrow around $300 million by allowing the city to claim the statutorily required contribution was only $737 million The *statutory amount of annual contributions defined under P.A. 99-0506 does not even cover normal cost, let alone the interest on the unfunded liability for the next 11 years.* This means the unfunded liability is actually projected to increase to a high of $12.2 billion in 2030, when contributions are finally sufficient to start reducing this unfunded liability. PABF's own actuary says this short statutory funding is harmful and dangerous to the plan. The SEC In 2013 charged the State of Illinois with securities fraud for

[14] *https://chipabf.org/wp-content/uploads/2021/06/PABF-Actuarial-Valuation-2020.pdf*

misleading municipal bond investors about the state's approach to funding its pension obligations; specifically, that its statutory plan significantly underfunded the state's pensions.

Chicago has consistently underfunded the plan more than the statutory amount, blatantly breaking the law, with no consequences. While the Illinois law has an intercept function that works for some cities, it seems deliberately rigged to let Chicago off the hook with intercepts so small they are immaterial.

Chicago is frequently considered as being the most likely major U.S. city to file bankruptcy following Detroit. The Detroit General fund was 75% funded and they still took a benefit cut of 5% in the bankruptcy order. This is triple the funding level of PABF. Retirees, disabled officers, and widows, along with currently active police officers, have valid concerns that their pension benefits could possibly be slashed as much as half in a municipal bankruptcy.

3 SETS OF BOOKS

The actuaries figure the funding ratio for Chicago Police three different ways, but in the case of PABF all three ways get you in the same ballpark of 22% to 24%.

Under federal pension law for corporate pensions, the department of labor classifies funding level like stoplights. Green is 80% and above, yellow is 65% to 80%, and below 65% is red where severe penalties kick in. Morningstar recently declared the fiscally sound threshold of a 70% funding ratio.

Under the current statutory funding policy, the funded ratio is projected to increase slowly over the next 10 years from 23.1% in 2020 to 32.7% in 2030. This theoretical funded ratio is projected to increase to 46.1% in 2040, 70.8% in 2050, and 90.0% in 2055.

So, this statutory policy, if it works perfectly, gets you out of the red zone around 2045. But these projections are optimistic, given Chicago's record of underfunding, poor governance, and poor returns. Current factors, like an increase in retiring officers and vacancies with current officers, all make this rosy scenario less likely.

PABF's actuary states: *Underfunding the Fund creates the risk that the long-term investment return cannot be supported, minimal investment income is available to pay benefits, or worse, that benefit obligations cannot be met from the trust. The In light of the current funded status of this Retirement Fund, we do not endorse this funding policy because the Statutory funding policy defers funding for benefits into the future and places a higher burden on future generations of taxpayers. We recommend a funding policy that contributes the net normal cost-plus amortization of the unfunded actuarial liability over a reasonable period.*[15]

For year ending 2020, assets went up $3.2 to $3.4 billion, but liabilities went up more; from $11.6 billion to $12.1 billion. [16]

Essentially, they took the actuarially required return which gets you to 100% funding in 30 years or 2050, and to squeeze out another $300 million of borrowing, they changed the formula for statutory funding to 90% funding over 35 years or 2055.

All four Chicago funds including PABF have filed claims with the state comptroller that the city's pension contributions have fallen short of the low statutory required payments. As of June 2019, approximately $24 million in claims had been filed by the four funds. The city of Chicago did attempt to obtain a restraining order to prevent the state comptroller

[15] https://chipabf.org/wp-content/uploads/2021/06/PABF-Actuarial-Valuation-2020.pdf

[16] https://chipabf.org/wp-content/uploads/2021/06/PABF-GASB6768-2020.pdf

from intercepting state grant funds, but was denied by a judge (Shields, 2019).

PABF has a 2020 assumed investment return of 6.75% the only fund lower funded the Kentucky plans has an assumption of only 5.25%. IF PABF adopted a more conservative investment assumption its funding ratio could drop to the teens.

NATIONAL & ILLINOIS TRENDS

In 2013, the Securities and Exchange Commission (SEC) charged the state of Illinois with securities fraud for misleading municipal bond investors about the state's approach to funding its pension obligations. Illinois failed to disclose that its statutory plan significantly underfunded the state's pension obligations and increased the risk to its overall financial condition. The state also misled investors about the effect of changes to its statutory plan.[17] *The state's misleading disclosures resulted from various institutional failures. As a result, Illinois lacked proper mechanisms to identify and evaluate relevant information about its pension systems into its disclosures. For example, Illinois had not adopted or implemented sufficient controls, policies, or procedures to ensure that material information about the state's pension plan was assembled and communicated to individuals responsible for bond disclosures.* [18] It appears Chicago plans are very similar.

Most state constitutions require a balanced budget, but the offending state and local officials have willfully and deliberately paid only a fraction of their ARC for many consecutive years. By underfunding their public pensions, they have taken on secret, illegal debt that must be paid to municipal bond holders. This makes these municipal bonds far

[17] https://www.sec.gov/news/press-release/2013-2013-37htm
[18] https://www.sec.gov/news/press-release/2013-2013-37htm

riskier than disclosed in SEC documents and reflected in their ratings by S&P and Moody's. [19]

Many feel that the SEC response in Illinois was weak and probably a case of "too little too late." Thomas Dolan's March 2016 article in Barron's comments on the SEC investigation into Illinois. [20] "*The SEC demanded no penalty, no fine, no exclusion of any bankers, lawyers, auditors and actuaries from new state business" With* this no-fine policy the SEC has basically stripped municipal bond holders from any protection from the whistleblower program, since it depends on a percentage of fines. The excuse that the SEC lacks authority in states is weak since state and federal finances are already intertwined with Medicaid and other programs.[21]

Dallas Police & Fire was touted as near insolvency and would force the city of Dallas into bankruptcy at a 45% funding ration-- twice that of PBAF. This was caused by bad real estate investments which is also an issue with PBAF [22]

PBAF remains one of the worst funded plans in US history, and without changes, will continue to be in severe risk of insolvency.

[19] *http://www.plansponsor.com/Ky_Retirement_Systems_Call_on_State_for_Higher_Contributions.aspx*

[20] *http://online.barrons.com/article/SB50001424052748704836204578360700155246458.html*

[21] *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2081150*

[22] *https://www.fraud-magazine.com/article.aspx?id=4295000920*

FEES – LACK OF TRANSPARENCY

Bill Bergman of Truth in Accounting wrote this specifically on the lack of fee transparency in the Chicago Police Pension Audit in July 2021?[23]

So, we should have good information about how much it costs to manage pension assets, right?[24] Wrong. Let's take a peek at another Illinois plan – the Policemen's Annuity & Benefit Fund of Chicago, the retirement plan for Chicago cops. At year-end 2020, the plan had more than $2.7 billion in investments, but the plan's "fiduciary net position" was only about one-fifth of the present value of its promised benefits. Here's what the latest audit report had to say about disclosure of investment fees:

> ***Investment management fees from equity and fixed-income managers, including one of the collective funds, one of the private equity managers, and the cash manager, are included in investment management fees on the statements of changes in fiduciary net position. Investment management fees from all other collective funds, short-term investments, infrastructure, hedge, real estate, venture capital and private equity are reflected in the net investment income from such investment products. Such investment management fees are not significant to the financial statements.***

At year-end 2020, this fund had about $800 million in "collective investment funds," $220 million in hedge funds, $140 million in real estate investments, $110 million in venture capital and private equity

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[23] https://www.truthinaccounting.org/news/detail/are-public-pensioners-and-taxpayers-paying-for-investment-performance

[24] https://www.truthinaccounting.org/news/detail/are-public-pensioners-and-taxpayers-paying-for-investment-performance

*investments, $100 million in short-term instruments, and $68 million in "infrastructure" investments. If experts were being paid two percent (annually) of the $1.4 billion in those investments, it would amount to about **$30 million** a year.*

But we don't know what the true compensation rate is because "such

Bergman of Truth and Accounting makes a very conservative estimate of PABF hiding fees of $30 million a year, but I think it is much higher closer to $70 million. The Mitchel & Titus claim that it is immaterial to their audit so they can cover it up is ridiculous

investment management fees are not significant to the financial statements."[25]

PABF has failed to monitor and fully disclose investment fees and expenses. Fees and expenses could be 10 times that which they disclose on their own 2020 Mitchell Titus Audit of $7.425 million. This so-called audit omits dozens of managers and their fees from its fee disclosure page. [26] The fees disclosed from the 2019 financials ($8.433m) only account for around half the assets and are for the lower fee managers. Assuming fees and expenses for alternative managers of 5% or 500 basis points, undisclosed fees could be as high as $70 million or more a year. [27]

[25] https://www.truthinaccounting.org/news/detail/are-public-pensioners-and-taxpayers-paying-for-investment-performance

[26] https://chipabf.org/pdfs/audit/final_pabf_fs_2019.pdf

[27] https://www.hbs.edu/ris/Publication%20Files/20-073_32c98338-75e6-4174-947f-510b16236e6d.pdf

The last page of the 2019 Mitchell Titus Audit it lists the mangers in the fund and how much they paid in fees. [28] The list look small, so I compared it to the 12/31/2019 NEPC report listing the performance of the managers and was shocked to find 32 managers on NEPC not on financials with over $500 million in assets in the highest fee alternative assets.[29] On the 12/31/2019 Northern Trust Custody report there are 45 managers not mentioned on the fee page of the 2019 Mitchell Titus Audit. The 2020 fee page in the audit is remarkably similar.

How could Mitchell Titus omit the highest fee managers used by pensions? They make the following ludicrous claim in Note 4 of the 2020 audit that is also featured in the Truth in Accounting story:

Investment Management Fees Investment management fees from equity and fixed-income managers, including one of the collective funds, one of the private equity managers, and the cash manager, are included in investment management fees on the statements of changes in fiduciary net position. Investment management fees from all other collective funds, short-term investments, infrastructure, hedge, real estate, venture capital and private equity are reflected in the net investment income from such investment products. Such investment management fees are ***not significant*** *to the financial statements.*

The SEC says that fees are always material. No one thinks that $70 million a year is immaterial to taxpayers and participants anywhere. Hiding fees

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https://www.institutionalinvestor.com/article/b1lxv2czrsv9y7/The-Inconvenient-Fact-Behind-Private-Equity-Outperformance

https://www.ft.com/content/377a8850-d72b-40a2-94d0-0abf1848bca2

[28] *https://chipabf.org/pdfs/audit/final_pabf_fs_2019.pdf*
[29] *https://chipabf.org/wp-content/uploads/2021/04/Investment-Performance-4th-Q-2019.pdf*

by just skimming them from returns has been exposed by the CFA Institute. [30]

Mitchell Titus admits to omitting managers in different parts of the audit. They admit there are four hedge fund of funds on December 31, 2020, and five funds at December 31, 2019. These are some of the highest fee vehicles with six layers of fees involved, with management fees, performance fees, and expenses at the hedge fund and fund of funds level. Their claim that these fees are immaterial is ridiculous.

In the notes Mitchell Titus say real estate investments consist of 25 and 23 real estate funds as of December 31, 2020, and 2019, respectively, but that none have enough fees to disclose. There are also many other undisclosed investments in private equity, private debt, and infrastructure.

Of the managers listed not on the 2019 audit, many have underreported fees primarily the alternative managers' multiple level fees. PAPF has illegally decided to withhold statements which would document these fees.

HIDDEN FEES PABF

Failure to Monitor and Fully Disclose Investment Fees and Expenses
It is well established that sponsors of retirement plans have a fiduciary duty to ensure that the fees paid to money managers for investment advisory services are reasonable.

The shift by public pensions into more complex, so-called "alternative" investment vehicles, such as hedge, private equity and venture funds,

[30] *https://blogs.cfainstitute.org/investor/2018/01/22/where-are-fees-and-expenses-not-costs/*

real estate, private debt, infrastructure as well as fund of funds, resulted in dramatically higher investment fees. These fees are much more difficult for pensions to monitor.

Most disturbing, a recent internal review by the SEC found that more than half of about 400 private-equity firms it examined charged unjustified fees and expenses without notifying investors.

Thus, pensions which choose to gamble in asset classes—such as private equity funds, specifically cited by regulators for frequently charging bogus fees in violation of the federal securities laws—must establish *heightened safeguards.* They must ensure that all fees paid to, or collected by, such managers are properly reviewed and determined to be legitimate, as well as fully disclosed to participants. PABF has done the opposite actually hiding 100% of the fees.

Many investment managers are known for taking excessive fees especially when dealing with public pensions whose managers are not actively monitoring, and reconciling fee bills quarterly. Even if a plan does not monitor funds, it should avoid those plans who have been fined by the SEC for taking excessive fees. PABF is so negligent in tracking fees and in selecting managers with SEC issues, that it looks as if they do not mind paying the high fees. The understating and hiding of excessive fees on the financial statements is even more troubling.

$2 TO $3 MILLION IN FEES PAID TO WALL STREET EVERY YEAR FOR DOING NOTHING

From the PABF Financial Statements ending 2020:[31]

[31] *https://chipabf.org/wp-content/uploads/2021/06/PABF_FS_2020.pdf*

NOTE 6 UNFUNDED INVESTMENT COMMITMENTS The Fund had unfunded commitments of approximately $157 million and $108 million at December 31, 2020 and 2019, respectively, in connection with real estate, infrastructure, private equity and collective commingled fund investments.[32]

Assuming PABF pays fees of 2 percent on total unfunded commitments, this amounts to an annual waste of approximately $3 million in 2020, and $2 million in 2019 essentially "Money for Nothing".

It is common practice for private equity and other alternative investment funds to seek to charge investment management fees on "committed capital." In other words, after the investor makes a capital commitment to a fund, management fees are charged on the entire commitment amount, regardless of whether the capital is actually drawn or invested. Paying fees on committed, uninvested capital results in exponentially greater fees on assets under management on a percentage basis.

While an increasing number of institutional investors resist paying fees to investment managers for *doing nothing*, the overwhelming majority willingly pay fees based upon their capital commitments.

As mentioned earlier, it is unclear whether PABF knows the full fees—including fees on committed, uninvested capital—it pays investment managers and whether those fees are fully disclosed.

[32] *https://chipabf.org/wp-content/uploads/2021/06/PABF_FS_2020.pdf*

e 6 page pg. 34 POLICEMEN'S ANNUITY AND BENEFIT FUND OF CHICAGO (A Component Unit of the City of Chicago) Notes to Financial Statements Years Ended December 31, 2020 and 2019 34 https://chipabf.org/wp-content/uploads/2021/06/PABF_FS_2020.pdf

PABF MANAGERS ON FEE DISCLOSURE

PABF has hired several managers who have had SEC issues with fee disclosure. In 2014 the SEC surveyed 400 investment limited partnerships and found that over 200 of them overcharged fees to their limited partners. [33] Morgan Stanley was fined $150 million for damages to California Public Pensions by the California attorney general[34] Invesco's wholly owned subsidiary WL Ross was fined over $11 million for excessive fees in private equity by the SEC.[35] BMO was fined over $37 million for excessive fees by the SEC.[36] Voya was fined over $22 million for excessive fees by the SEC.[37] UBS was fined over $3.5 million for excessive fees by the SEC.[38]

Apollo was Fined $53 Million by the SEC in 2016 following charges that it misled investors regarding fee practices. [39] In early 2021 Apollo CEO Leon Black resigned after paying $158 million in excessive fees to Jeffrey Epstein.[40]

Toward the end of 2014, under SEC pressure, Blackstone admitted to hiding fees.[41] In 2015 the SEC fined Blackstone [42] The SEC found a

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33 *SEC finds Bogus Privatge Equity Fees" Bloomberg April 7, 2014 http://www.bloomberg.com/news/2014-04-07/bogus-private-equity-fees-said-found-at-200-firms-by-sec.html*

34 *California Attorney General April 25, 2019*

35 *August 24, 2016 SEC Administrative Hearings*

36 *September 27, 2019 SEC Administrative Hearings*

37 *December 21, 2020 SEC Administrative Hearings*

38 *October 27, 2017 SEC Administrative Hearings*

39 *https://www.ai-cio.com/news/apollo-fined-53-million-over-fees/*

40 *https://www.nytimes.com/2021/01/26/business/jeffrey-epstein-leon-black-apollo.html*

41 *Blackstone admits hidden PE fees" Bloomberg http://www.bloomberg.com/news/2014-12-31/blackstone-opens-up-about-hidden-fees-as-sec-pushes-transparency.html*

42 *Center for Economic and Policy Research (CEPR) http://cepr.net/publications/reports/private-equity-fees-2016-05 published a paper Fees, Fees and More Fees: How Private Equity Abuses Its Limited Partners and U.S. Taxpayers May 2016, by Eileen Appelbaum and Rosemary Batt.*

number of ways that general partners at Blackstone shifted or overcharged expenses to limited partnerships on broken deal expenses, [43] [44] Specifically, Blackstone had two distinct breaches of fiduciary duty when they accelerated the payment of future monitoring fees and charged legal fees to the funds at a much higher rate than Blackstone actually paid. [45]

REAL ESTATE & ALTERNATIVE FEES

Many public plans pay more than 4% a year in Real Estate fees. [46] There are many levels of fees. There are management and performance fees and expenses at the fund level and management and performance fees and expenses at the property level. In addition, there are commissions and transactions costs in obtaining and selling the real estate holdings.

Real estate investment consulting services consistent with ERISA fiduciary standards should include details regarding all the various opaque fees and expenses related to each fund, the nature of the services provided for such fees, the all-in actual costs (on a percentage and dollar amount basis). In addition, it should include an in-depth analysis of the reasonableness of such fees and expenses, weighing the costs against the expected rate of return. Any conflicts of interest related to fees paid to affiliated parties should be scrutinized.

Without a comprehensive all-in fee analysis prepared by the investment consultant, the PABF cannot fulfill its fiduciary duty to monitor the fees

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[43] *http://www.sec.gov/news/pressrelease/2015-131.html*

[44] [44] *"Blackstone admits hidden PE fees" Bloomberg http://www.bloomberg.com/news/2014-12-31/blackstone-opens-up-about-hidden-fees-as-sec-pushes-transparency.html*

[45] *http://www.sec.gov/litigation/admin/2015/ia-4219.pdf*

[46] *http://siedlewhistleblowerforensics.com/RhodeIslandRealEstateInvestigation.pdf*

paid s investment managers, and decades of profiting by PABF's real estate investment managers at the expense of the pension will continue.

In a Rhode Island investigation it was found that undisclosed real estate investment-related expenses may amount to an additional 3 percent, above and beyond the limited fees disclosed by the pension at that time. [47] Study revealed multiple potential undisclosed fees—such as fees for acquisitions, disposition, financing, performance, development supervision, property management, underlying partnership and performance, fund operating expenses, custody, administrative, brokerage—many of which may exceed 1 percent. This 3 percent undisclosed fee estimate may have been too conservative. We were provided with no documents indicating PABF is aware of the all-in fees and expenses related to the pension's real estate investments.

Hedge fund private equity and other alternative fees private debt infrastructure are excessive but hidden.

LACK OF TRANSPARENCY

Transparency in government has long been acknowledged in America as essential to a healthy democracy. On the federal level, the Freedom of Information Act opens the workings of government to public scrutiny, giving citizens information they need to evaluate and criticize government decision-making.

All 50 states also have public records laws which allow members of the public to obtain documents and other public records from state and local government bodies. The Illinois Public Records Act is built on the

[47] *http://siedlewhistleblowerforensics.com/RhodeIslandRealEstateInvestigation.pdf*

United States' historical position that the records of government are "the people's records."

Transparency is also critical to the prudent management of trillions of dollars invested in America's state and local government pensions. Indeed, the single most fundamental defining characteristic of our nation's public pensions is *transparency*. Of all pensions globally, our public pensions—securing the retirement security of nearly 15 million state and local government workers, funded by workers and taxpayers—are required under our public records laws to be the most transparent. Transparency of fees paid by taxpayers are key.

Public pensions primarily invest government workers' retirement savings in securities and funds which are regulated on the federal and state level. Our nation's securities laws require that securities issuers and fund managers register with regulators, disclose financial and other significant information to *all* investors, including public pensions, as well as prohibit deceit, misrepresentations, and other fraud. Such information is commonly provided in the form of prospectuses, offering memoranda, annual reports, performance reviews and other documents.

Absent full disclosure by investment firms to pension boards and staffs, these individuals cannot fulfill their fiduciary duty to diligently safeguard pension assets. Full disclosure of investment information to the public is necessary for the stakeholders to understand the investment program, as well as evaluate whether pension fiduciaries are prudently performing their duties.

Thus, in public pension matters, we are concerned with two levels of transparency:

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First, under state public records laws, all of the workings of the pension must be open to full public scrutiny, including, but not limited to, investments.

Second, under the securities laws, issuers and investment advisers must fully disclose material information to pensions, boards and staffs regarding pension investments.

Alarmingly, our investigation reveals that the Police Retirement System of Chicago (PABF) has long abandoned transparency of hiring practices of managers and fees paid, choosing instead to collaborate with Wall Street firms and others to eviscerate Illinois public records laws and avoid accountability to stakeholders. Predictably, billions have been squandered over time as transparency has ceased to be a priority.

EXCESSIVE FEES NATIONALLY

Governing magazine in May 2016 estimated that disclosed and undisclosed fees cost public plans upwards of $20 billion annually. [48] Jeff Hooke of the right- leaning Maryland Policy Institute has written about public pensions and fees. [49] Hooke's study concludes that pension funds with the highest fees, as a percent of assets, recorded inferior investment returns, on average, versus those in states with the lowest fees. [50]

[48] *http://www.governing.com/topics/finance/gov-pensions-come-terms-with-hidden-fees-some-say-annual-exceeds-20-billion.html*

[49] *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2653942*
[50] *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2653942*

In 2014 the SEC surveyed 400 investment limited partnerships and found that over 200 of them overcharged fees to their limited partners. [51] This suggests a breakdown of controls and a material weakness in these industries widely held in public pensions.

In 2014, former SEC Attorney Edward Siedle put out a scathing review of the North Carolina Public Pension system which was covered widely in North Carolina and the U.S.

Cowell has taken this quid pro quo to a new level as the Teachers' and State Employees' Retirement System of the State of North Carolina ("TSERS") has grown to $87 billion and disclosed fees paid to Wall Street have skyrocketed 1,000 percent. Cowell's political manipulation of the state pension fund has cost North Carolina $6.8 billion in fees and lost investment opportunities during her tenure. [52] North Carolina Republican Treasurer Dale Folwell ran for election on decreasing fees caused by Cowell.

New Jersey and South Carolina revamped their fee reporting. Since 2007, fees in South Carolina have gone from $39 million to $468 million, an increase the system attributes to better reporting based on a CEM recommendation. New Jersey's pension system recently announced it paid outside fund managers $328.4 million in performance bonuses last fiscal year, on top of nearly $400 million in management

[51] *SEC finds Bogus Private Equity Fees" Bloomberg April 7, 2014 http://www.bloomberg.com/news/2014-04-07/bogus-private-equity-fees-said-found-at-200-firms-by-sec.html*

[52] *North Carolina Pension's Secretive Alternative Investment Gamble: A Sole Fiduciary's Failed "Experiment" By Edward Siedle http://nebula.wsimg.com/2c61c80993914081e45d8ee4ad97e4d2?AccessKeyId=706D4353590FAA6ED8CE&disposition=0&alloworigin=1*

fees. South Carolina Republican Treasurer Curtis Loftis has been one of the biggest critics of fees. [53] Under Chris Christie, hedge fund and private equity fees totaled over $725 million in 2015 alone.[54] [55]

Many of these high fees were paid out of secret no-bid contracts for alternative assets. The American Federation of Teachers (AFT) commented in their May 2017 report that *"Attempts to pass legislation requiring fee transparency have foundered in states like… Kentucky"*[56] A2017 Pew report states that no-bid contracts for alternative assets have exploded in State Pension Plans, and with them, higher fees. [57] The Center for Economic and Policy Research (CEPR) in 2016 published a paper on the excessive hidden fees in private equity. [58] In 2015 IBT/Newsweek[59] and The New York Times[60] reported on hundreds of millions in secret fees in public pensions. The 2017 AFT report said "*Cutting fees to hedge fund, private equity and co-mingled real assets managers by half would have saved the 12 pension funds in our study*

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http://www.scstatehouse.gov/CommitteeInfo/HouseLegislativeOversightCommittee/CommitteeMeetingHandouts/ExecutiveSub/Sept102015ExecutiveSubcommitteeMeeting/TreasurersOfficeInformationProvidedAboutSCRetirementSystemInvestmentCommission.pdf

54 http://hedgeclippers.org/hedgepapers-no-31-christies-cronies/

55 http://wp.me/p5NdLG-sd

56 http://www.aft.org/sites/default/files/bigsqueeze_may2017.pdf

57

http://www.pewtrusts.org/~/media/assets/2017/04/psrs_state_public_pension_funds_increase_use_of_complex_investments.pdf

58 The Center for Economic and Policy Research (CEPR) http://cepr.net/publications/reports/private-equity-fees-2016-05 published a paper Fees, Fees and More Fees: How Private Equity Abuses Its Limited Partners and U.S. Taxpayers May 2016, by Eileen Appelbaum and Rosemary Batt

59 http://www.ibtimes.com/cities-states-paying-massive-secret-fees-wall-street-report-1887034
60 https://www.nytimes.com/2015/05/03/business/pension-funds-can-only-guess-at-private-equitys-cost.html?_r=0

$3.8 billion per year in alternatives fees, for a total of $19 billion over the last five fiscal years."[61]

Former consultant Richard Ennis discussed the high fees of alternatives in public pensions in his July 7, 2021 paper.[62] His fee estimates of 5.7% to 6% total for private equity.[63] For hedge funds, he used what he thought was low end of the range at 3.4%.[64] For private debt he cited a 2019 book with 3.0% in annual fees.[65] Ennis findings of other public plans with similar high fee alternative investments and similar poor performance are consistent with the finding in Chicago PABF.

Historically it was common to disclose management fees, but to not disclose performance fees. However, recently CALPERS South Carolina and New Jersey have started disclosing both management fees and performance fees. The major independent fee measuring service CEM went on record in 2014 recommending disclosure of both management and performance fees.[66] PABF does not disclose any performance fees and many management fees.

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[61] *http://hedgeclippers.org/partner-report-no-6-with-aft-the-big-squeeze-how-money-managers-fees-crush-state-budgets-and-workers-retirement-hopes/*
[62] *https://lnkd.in/ejW6RCa https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3883370*

[63] *The private equity cost estimate of 5.7% is that of CEM Benchmarking, as cited by McKinsey (2017 24); Phalippou and Gottschalg (2009) estimated the cost of private equity at 6% of invested capital*

[64] *The 3.4% figure is the low end of the range of estimates by French (2008), Ibbotson et al. (2010), Jurek and Stafford (2015), and Ben-David et al. (2020). Ben-David, I., J. Birru and A. Rossi. 2020. "The Performance of Hedge Fund Performance Fees." Fisher College of Business Working Paper No. 2020-03-014, Charles A. Dice Working Paper No. 2020-14. SSRN: https://ssrn.com/abstract=3630723 or http://dx.doi.org/10.2139/ssrn.3630723.*

[65] *Nesbitt, S. L. 2019. Private Debt. John Wiley & Sons, Inc.*

[66] *http://www.cembenchmarking.com/Files/Documents/CEM_article_-_The_time_has_come_for_standardized_total_cost_disclosure_for_private_equity.pdf*

SECRET NO-BID CONTRACTS

Hundreds of contacts for the investment managers at PABF are claimed to be secret and have not been provided under FOIA (Freedom of Information Act) requests. While PABF puts traditional investment managers through a competitive bidding or RFP process, they let the high-risk high fee alternative managers bypass this basic control for transparency and accountability.

A 2014 expose by David Sirota had this to say about Blackstone secret contracts. *Blackstone's payment structure is outlined, with language guaranteeing that Blackstone will receive its hefty annual management fees from the taxpayer - regardless of the fund's performance. In other documents, public pension money is exempted from some of the most basic protections usually guaranteed under federal law. Other contract language appears to license Blackstone to engage in financial conflicts of interests that could harm investors*[67]*.* Language like *"Blackstone may have conflicting loyalties"* between the different funds it operates, and that *"actions may be taken for the Other Blackstone Funds that are adverse" to investors* [68]

These Blackstone contracts have a troubling section entitled *"absence of regulatory oversight,"* The section includes clauses like investors *"are not afforded the protections of the 1940 (Investment Advisers) Act*." It also says that in the event of litigation brought against the managers of the fund, those costs *"would be payable from the assets"* of the

[67] *https://pando.com/2014/05/05/leaked-docs-obtained-by-pando-show-how-a-wall-street-giant-is-guaranteed-huge-fees-from-taxpayers-on-risky-pension-investments/*

[68] *https://pando.com/2014/05/05/leaked-docs-obtained-by-pando-show-how-a-wall-street-giant-is-guaranteed-huge-fees-from-taxpayers-on-risky-pension-investments/*

investors.[69] Sirota quoting former SEC investigator Ted Siedle, the conflict-of-interest section marked *"Fees for Services"* is particularly problematic. Siedle says it permits private equity managers to assess fees on companies the private equity fund owns, but then not compensate the fund investors (like public pensions) for those fees. This stealth fee-inflating practice, which is attracting SEC scrutiny, has been called the *"crack cocaine of the private equity industry*."[70]

What is in these secret contracts? Siedle in his North Carolina report make a mockery out of the industry claim that they are protecting "trade secrets" like the Colonel Sanders secret recipe for chicken. *Perhaps most disturbing, in response to our specific requests the Treasurer refused to disclose offering memorandum and other key documents (including information regarding millions in placement agent fees) related to TSERS' costly, high-risk alternative investments, citing supposed "trade secret" concerns raised by the alternative managers. Viewed from a regulatory and public policy perspective, the Treasurer's practice of withholding relevant information and intentionally providing incomplete or inaccurate disclosures regarding TSERS investments results in: (1) concealing potential violations of state and federal laws, such as those detailed throughout this report; (2) misleading the public as to fundamental investment matters, such as the true costs, risks, practices and investment performance related to hedge, private equity, venture and real estate alternative investment funds; (3) understating the costs and risks related to TSERS investments specifically; (4) misrepresenting the investment performance and*

[69] *https://pando.com/2014/05/05/leaked-docs-obtained-by-pando-show-how-a-wall-street-giant-is-guaranteed-huge-fees-from-taxpayers-on-risky-pension-investments/*

[70] *https://pando.com/2014/05/05/leaked-docs-obtained-by-pando-show-how-a-wall-street-giant-is-guaranteed-huge-fees-from-taxpayers-on-risky-pension-investments/*

financial condition of the state pension to investors in state obligations. [71]

Former SEC Attorney Edward Siedle dug into the documents further.

The documents we reviewed indicate the alternatives are high-risk, speculative investments; the funds' investments are highly illiquid subject to enormous valuation uncertainty; the offerings involve serious conflicts of interest regarding valuation of portfolios by the managers themselves and calculations of fees, as well as opportunities for self-dealing between the funds, the managing partners and their affiliates that may, in our opinion, violate state and federal law. For example, a manager may make investments for his own account in the very same assets in which the fund he manages invests, on more favorable terms and at the expense of investors in the fund, including TSERS. Alternatively, in the event that an investment opportunity is available in limited amounts, the manager may simply seize the entire investment opportunity for himself — robbing investors in the fund he manages, in breach of applicable fiduciary duties. Accordingly, we recommend further investigation by the SEC of such potential fiduciary breaches and violations of law. [72]

The alternative fund offering documents also generally provide that the funds will invest in portfolio companies that will not be identified to the investors prior to their investment in the fund. As a result, TSERS will not

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[71] *North Carolina Pension's Secretive Alternative Investment Gamble: A Sole Fiduciary's Failed "Experiment" By Edward Siedle* *http://nebula.wsimg.com/2c61c80993914081e45d8ee4ad97e4d2?AccessKeyId=706D4353590FAA6ED8CE&disposition=0&alloworigin=1*

[72] *North Carolina Pension's Secretive Alternative Investment Gamble: A Sole Fiduciary's Failed "Experiment" By Edward Siedle* *http://nebula.wsimg.com/2c61c80993914081e45d8ee4ad97e4d2?AccessKeyId=706D4353590FAA6ED8CE&disposition=0&alloworigin=1*

have any opportunity to evaluate for itself information regarding the investments in which the funds will invest. Since pension fiduciaries are required to know, as well as evaluate the assets in which they invest, in our opinion, such provisions render these investments unsuitable for fiduciary accounts.

TSERS alternative funds generally disclose a litany of risky investment strategies they may pursue such as short selling; investing in restricted or illiquid securities in which valuation uncertainties may exist; unlimited leverage, as well as margin borrowing; options; derivatives; distressed and defaulted securities and structured finance securities. Further, TSERS alternative investment documents reveal that managers may engage in potentially illegal investment practices, such as investing in loans that may violate the anti-predatory lending laws of "some states" and life settlement policies which give rise to lawsuits alleging fraud, misrepresentation and misconduct in connection with the origination of the loan or policy. In our opinion, an investigation should be undertaken by the SEC into the investment strategies of the alternative funds, as well as any underlying funds, to determine whether any violations of law exist. Unlike traditional investments, the alternative funds in which TSERS may invest may be managed by investment advisers not registered with the SEC under the Investment Advisers Act of 1940. Further, the funds themselves are not registered as "investment companies" under the Investment Company Act of 1940. As a result, the limited partners lack many meaningful protections of those statutes.

It is obvious that keeping contracts secret only helps hedge fund managers and private equity conceal their fiduciary breaches and excessive fees.

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FEE CONCLUSION

PABF Fees are severely underreported, if reported at all. Real Estate partnerships have at least three layers of fees for the partnership manager, managers of each property, and commissions and other transaction costs. Hedge fund of funds (FOF) have at least 6 layers of fees, AUM fees for the FOF and individual managers, Performance fees for the FOF and individual managers internal expenses and charges for the FOF and individual managers. Private Equity partnerships have at least 3 layers of AUM fees for the partnership manager, performance fees, and costs.

In examining PABF investments over the past 5 years, there seem to be at least 60 named investment managers and, if looking at fund of funds, well over 100. Not one of these managers was hired in the traditional competitive bidding or RFP process. They were hired in secret no-bid contracts. The Government Finance Officers Association officially recommends a RFP process for public pension managers to hire investment managers. [73]

Many public plans, if they bypass the RFP process, provide written analysis from consultants and/or staff to back up the purchase and the fees paid. We have asked for this analysis from PABF, and they have illegally denied our FOIA requests. While it is probable that NEPC provided some documentation for some of these no-bid managers, it is highly likely it did not cover all managers and/or was not very thorough.

[73] *https://www.gfoa.org/materials/procurement-of-financial-services*
https://www.gfoa.org/materials/selection-and-review-of-investment-advisors

GHOST MANAGERS & PAY TO PLAY

GHOST MANAGERS

PABF may have over 100 "ghost managers" in funds of funds. PABF takes this lack of disclosure to the next level, "ghosting" dozens of other alternative managers in private equity, hedge funds and real estate from their financial statements and other disclosures. Ghosting managers makes it impossible to determine pay for play or the amount of fees. This is clearly a breach of fiduciary duty.

The last page of the official PABF 2019 audit by Mitchell Titus lists the mangers in the fund and how much they paid in fees. [74] The list looked small, so I compared it to the 12/31/2019 NEPC report listing the performance of the managers. To my shock there were 32 managers on NEPC not on financials with over $500 million in assets in the highest fee alternative assets.[75] On the 12/31/2019 Northern Trust Custody report there are 45 managers not mentioned on the fee page of the 2019 Mitchell Titus Audit. The fees omitted from the 2019 financials could be as high as $20 million or more. Mitchell Titus hints that the omissions of real estate, hedge funds, private equity "Ghost managers" are immaterial, but this is a blatant fiduciary breach since fees are never immaterial. [76]

The key to the 2014 SEC investigation was the un-ghosting of manager Madison & Dearborn which was not disclosed in public financial documents because it was in a fund of funds. It was only disclosed in a separate economic development document for Illinois-related

[74] *https://chipabf.org/pdfs/audit/final_pabf_fs_2019.pdf*
[75] *https://chipabf.org/wp-content/uploads/2021/04/Investment-Performance-4th-Q-2019.pdf*
[76] *Pg 46. https://chipabf.org/pdfs/cafr/cafr_2015_final.pdf*

investments that is not widely published. It provides the names of all Illinois based "ghost managers" even those in funds of funds as well as addresses of real estate owned in Illinois as well as private companies. Chicago Police and the state in violation of FOIA redacted all of these names from this Illinois Economic Development report their open records requests. The Illinois Municipal Retirement fund on its website disclosed this entire report unredacted. This redaction by PABF appears to me a deliberate attempt to not disclose potential pay to play.

LOST MANAGERs

This is a small sample of those managers showing up on the Northern Trust lists, but do not show up on the financial statement fee disclosures.

2019

Adams Street, Brinson etc. AG Core Plus Realty II
PIMCO All Asset ,Entrust PERMAL,UBS Bucktown FOF
Blackstone Property,BeachPoint Select PD
Blackrock EM, MS Prime Property
Global Infrastructure Partners III, Clareant Euro DIR
Eagle Point, Soundmark Partners Horizons
Crestline Opportunity, Dorchester, TerraCap IV
Lonestar X, Lonestar Fund VI, Lonestar XI, Lonestar Global

Monroe Capital, Monroe Capital Private
Mesirow Capital Partners Fin RE Val III
Brookfield RE fund B,Clareant Euro DIR III
Global Infrastructure Partners I,Global Infrastructure Partners IV
DRA Advisors,Apollo Real Estate Advisors
Mesirow Capital Partners RE val,Morgan Stanley RE IV
ABR Chesapeake III

2017

ADAMS STREET PARTNERS AIM(INVESCO) PRIVATECAPITAL
MESIROW FINANCIAL PRIVATE EQUITY
MULLER & MONROE ASSET MANAGEMENT, LLC

INVESCO VENTURE ALPHA FUND, L.P. BEACH POINT SELECT FUND LP.
CRESTLINE OPPORTUNTY FUND III, LLC DORCHESTER CAPITAL
SECONDARIES OFFSHORE IV, L.P. (DORCHESTER)
MONROE CAPITAL PRIVATE CREDIT FUND II, L.P. (MONROE)
VOYA CREDIT OPPORTUNTIES FUND, TACTICAL AND ALPHA STRATEGIES
ENTRUSTPERMAL PABF FUND LLC (ENTRUSTPERMAL)
PLUSCIOS FUND LLC (PLUSCIOS)
GMO Global Asset Allocation PIMCO All Asset Collective Trust (
CARLYLE INFRASTRUCTURE PARTNERS, L.P.
GLOBAL INFRASTRUCTURE PARTNERS, L.P GLOBAL INFRASTRUCTURE
PARTNERS III A/B, L.P.
ULLICO INFRASTRUCTURE TAXABLE FUND,

ANGELO GORDON CORE-PLUS REAL ESTATE FUND II
APOLLO EUROPE III , BLACKROCK ASIA FUND III (AF III)
BROOKFIELD REAL ESTATE FUND V, L.P. (BREF V)
CBRE CLARION SECURITIES GLOBAL REAL ESTATE SECURITIES STRATEGY
LONE STAR REAL ESTATE FUND, LONE STAR FUND VI.
MESIROW FINANCIAL REAL ESTATE VALUE FUND, L.P. ...
MORGAN STANLEY PRIME FUND,MSREF VI INTERNATIONAL
NEWPORT CAPITAL, QUADRANT FUND50
SOUND MARK HORIZONS FUND, UBS TRUMBULL PROPERTY FUND

PAY TO PLAY

Pay for Play is not always illegal, but it is a bad fiduciary practice in all cases. This report's job is to shed transparency on the excessive fees paid by managers. Most importantly we need the transparency of the names of the secret investment managers in fund of funds for anyone to even know who may be paying whom. We focus on the harm to the fund via the underperformance which is connected to the excessive fees. We will let others in media and government connect the dots of these excessive fees to various types of payments.

The Chicago Ethics Commission has pretty much looked the other way at pay for play in this 18-page report after the IBT story and 2014 SEC investigation initiated by several Aldermen.[77]

This report does not delve into the political side of this. That is for others to do. However, this report demands the minimum transparency of public disclosure of all the Investment managers for the PABF, including those in funds of funds. Only with this level of transparency can you even see if pay to play exists.

Pulitzer winner and former New York Times writer Gary Rivlin on his Illinois pension expose in 2018 wrote "Those with the highest exposure to high-fee alternatives are also the most vulnerable to pay-to-play."[78] Chicago Police clearly have a high exposure to alternatives.

An inquiry into public records by a Chicago Alderman in 2014 disclosed that former Mayor Rahm Emanuel received campaign donations of over $600,000 from investment managers who manage accounts for the PABF

[77] https://www.chicago.gov/content/dam/city/depts/ethics/general/AO_CampFinanacing/141280.A.pdf

[78] https://theintercept.com/2018/10/22/illinois-governor-bruce-rauner-pensions/

and other city funds. This led to a SEC investigation initiated by a Chicago City Alderman. [79]

A cursory examination of public documents reveals that over $200,000 in donations have been made to Mayor Lightfoot by firms that have managed investments for Chicago pensions.
One particular investment firm was Madison Dearborn buried in a fund of funds run by a manager Adams Street that was uncovered in the Emanual SEC investigation in 2014. The Chicago Municipal Employees Annuity and Benefit Fund, invested in an Adams Street Partners fund of funds in which Madison Dearborn entities comprise 9 of the 16 total funds.[80] The Brinson Partnerships were also hidden under Adams Street with the Chicago Police Fund.

We found this same firm Madison Dearborn has made over $200,000 in donations to Mayor Lightfoot.[81] Because of the lack of transparency we do not know if Madison Dearborn manages money for PABF or other Chicago pensions currently via Adams St. or another fund of funds. We do know that while Adams St was left off of the 2019 PABF financial statement, NEPC reported a $2.9 million balance as of 12/31/19. The Northern Trust 12/31/19 statements do not list Adams Street specifically, but list seven different private equity funds under the name Brinson which are owned by Adams Street. Adams Street has been disclosed sporadically in PABF documents over the years. Gary Brinson was a large donor to Mayor Emanuel. The Chicago Teachers Union pointed out the Madison Dearborn contribution to Lightfoot as troubling. [82]

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[79] *https://www.ibtimes.com/chicago-mayor-rahm-emanuel-accepted-campaign-contributions-financial-firms-managing-1723396*

[80] *https://www.ibtimes.com/chicago-pension-investments-rahm-emanuels-proposed-merger-could-benefit-campaign-1993137*

[81] *https://illinoissunshine.org/committees/lightfoot-for-chicago-34589/*

[82] *https://www.ctulocal1.org/posts/we-dont-need-another-rahm-or-his-donors-lining-up-behind-lori-lightfoot/*

HISTORY OF MAYOR EMANUAL ADMINISTRATION

Former Chicago Mayor Rahm Emanuel has a long history of ties to Wall Street Firms from the time he worked for Bill Clinton, and his days in Congress.[83][84] The firms include Madison Dearborn, Goldman Sachs, JP Morgan, Citigroup, Blackstone, Citadel, Lazard Freres, Morgan Stanley. [85]

Rahm Emanuel had a long relationship with Private Equity GCTR head then Governor Bruce Rauner. Rauner made much of his fortune off excessive fees on Public Pensions. In Pulitzer winner Gary Rivlin's profile of Illinois pensions he wrote *in the late 1990s, shortly after Emanuel left the Clinton White House and around the time Emanuel was brought on as a partner at the investment bank Wasserstein Perella & Co. The young politico famously earned $18.5 million during his two-and-one-half years there — much of it courtesy of his business relationship with Rauner. The two did five deals together, including SecurityLink, an alarm company Emanuel brought to Rauner for acquisition. Rauner's private equity firm GTCR bought the company from SBC Communications for $479 million, then sold it six months later for $1 billion. Shortly after he was elected mayor, Emanuel put Rauner and his wife into what the Chicago Tribune called "unpaid but prominent advisory roles." Rauner left GTCR in October 2012 and announced that he was running for governor in June 2013.*[86]

Chicago political and media figure Bill Kelly wrote in 2014
It is no secret that Chicago Mayor Rahm Emanuel and Illinois Governor-elect Bruce Rauner are bosom friends and business partners. However, according to an investigation by reporter David Sirota at IBTimes.com,

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[83] https://www.nakedcapitalism.com/2010/04/rahm-emanuel-and-magnetar-capital-the-definition-of-compromised.html

[84] https://dailyantikos.blogspot.com/2008/11/rahm-emanuel-bought-and-paid-for.html

[85] http://www.opensecrets.org/members-of-congress/contributors?cycle=Career&cid=N00024813

[86] https://theintercept.com/2018/10/22/illinois-governor-bruce-rauner-pensions/

the two also appear to have something else in common: serious violations of SEC law involving pension fund-tainted political donations. The IBTimes.com reports that since 2011, Mayor Emanuel and his political action committees have accepted more than $600,000 in contributions from executives at firms that manage city pension funds – if true, these contributions constitute a serious violation of federal law.[87]

After these stories were published, a Chicago Alderman requested the SEC to look into Rahm Emanual for pay to play in 2014.[88]

A big chunk of this $600,000 came from Madison Dearborn a Chicago based investment manager. Madison Dearborn claimed some loophole, asserting that because they are buried in a fund of funds they can remain secret, but the SEC does not buy this.

The SEC has explicitly decreed that manager of a fund of funds are governed by its pay-to-play rules. *"It is not appropriate to exclude subadvisors from the rule,"* the commission said, otherwise the rule would be compromised by a gaping loophole: Firms *"that sought to avoid compliance"* with the rule's strictures could make campaign contributions freely while handling their public pension business exclusively through fund of fund relationships. The agency included provisions barring financial firms from doing *"indirectly what [they] could not do directly under the rule."*[89] We need full disclosure of all the managers even in fund of funds to determine whether or not pay to play is going on.

Emanuel was tied to several funds. A story on Chicago Teachers Pension pay to play mentions ties linking Emanual to hedge fund operator

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[87] *https://www.chicagonow.com/kelly-truth-squad/2014/11/rahm-emanuel-bruce-rauner-violate-sec-pay-to-play-rules-with-pension-cash/*

[88] *https://www.ibtimes.com/chicago-lawmakers-call-sec-investigation-mayor-rahm-emanuel-1725673*

[89] *https://www.ibtimes.com/chicago-mayor-rahm-emanuel-accepted-campaign-contributions-financial-firms-managing-1723396*

Grosvenor. This relationship was buried in a hedge fund of funds that Chicago Teachers refused to disclose [90] Chicago Teachers continue to monitor issues with private equity and hedge funds. [91] Mayor Emanual was involved in a big charitable initiative with Blackstone while the firm was a PABF manager. [92]

An Apollo Cayman Islands partnership was purchased by PABF during the Emanuel administration. In early 2021 Apollo CEO Leon Black resigned after paying $158 million for services to Jeffrey Epstein.[93] Soon after the resignation a major Pennsylvania fund halted business with Apollo due to an investigation over Chairman and CEO Leon Black's professional relationship with financier and registered sex offender Jeffrey Epstein.[94] Apollo was involved in a massive pay to play scheme involving a trustee and CEO of CALPERS the US largest public pension. The CALPERS CEO Buenrostro was sent to prison and the trustee Villalobos committed suicide before serving his term.[95] Christian Moree the former Director of Advance for the Chicago for Rahm Emanuel Mayoral campaign was recently named Chief of Staff for Apollo. [96]

According to the December 31, 2019 Northern Trust portfolio statements there were 7 different Private Equity Partnerships under the name "Brinson Partnership Fund Trust" with total unrealized losses of around -$17 million. Gary Brinson is a well-known Chicago money manager who has been a Rahm Emanuel doner of at least $50,000. [97]

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[90] *https://www.ibtimes.com/chicago-teacher-pension-money-invested-rahm-emanuels-friends-donors-1843104*

[91] *https://theintercept.com/2019/10/25/chicago-teachers-strike-wall-street/*

[92] *https://www.blackstone.com/press-releases/article/mayor-emanuel-blackstone-charitable-foundation-and-world-business-chicago-launch-blackstone-inclusive-entrepreneurship-challenge/*

[93] *https://www.nytimes.com/2021/01/26/business/jeffrey-epstein-leon-black-apollo.html*

[94] *https://www.pionline.com/pension-funds/pennsylvania-fund-halting-business-apollo*

[95] *https://www.latimes.com/business/la-fi-villalobos-suicide-20150115-story.html*

[96] *https://www.linkedin.com/in/christian-moree/*

[97] *https://www.factcheck.org/2015/03/chicago-school-fight/*

Amer Ahmad was a PABF trustee for 2 years in 2011 and 2012 during the Emanuel administration. Months later with the Ohio Treasurers office in 2013 "*Ahmad pleaded guilty to bribery, money laundering and conspiracy, admitting that he steered more than $3 million dollars in state investment business to a high school classmate, who then kicked back $500,000 to Ahmad. While awaiting sentencing he escaped the U.S. to Pakistan using falsified documents. He avoided punishment for nine months but was eventually caught and sent back to Chicago, where his wife and children have since disowned him.*[98] "He was sentenced to 15 years. Mayor Emanuel spent $800,000 looking into Ahmad's Chicago career, but the investigators claimed they did not to find anything, it is unclear whether they looked at his PABF Trustee role.

Perhaps the most infamous investment last showed up on the Northern Trust December 31, 2017 custodial report in which a -$12.2 million loss appeared which had already been "ghosted" off the NEPC reports and audits. DV Urban Realty Partners was noteworthy for its massive losses and because one of its main partners was the nephew of former Mayor Daly. [99]

ILLINOIS HISTORY OF PAY TO PLAY

Many people do not know that the FBI got the tape of Illinois Governor Rob Blagojevich selling Barack Obama's vacated Senate seat, because of, the investigation of placement agents who were deeply involved in pay to play in public pensions. Placement agents have all but disappeared after the Supreme Court Citizens United decision which allows pay to

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[98] https://abc7chicago.com/illinois-coronavirus-covid-chicago-amer-ahmad/6317623/
[99] https://www.illinoispolicy.org/high-risk-real-estate-investments-cost-chicago-pension-funds-54m-win-fund-managers-9m/

play money to be contributed secretly via SuperPacs and other dark money vehicles. This negates the need for middlemen the placement agents.

The pay to play abuses first unraveled in Illinois, are related to the current insolvency issues plaguing the state. The shady dealings of Stuart Levine, a trustee of the Illinois Teachers' Retirement System (TRS), caused the system to ban placement agents in 2005, and led to his federal indictment in 2006, and finally a prison sentence in 2012.

Levine received a significantly reduced, five and a half year prison sentence because he provided information that helped unravel the corrupt Blagojevich administration.[100] The 2006 indictment he shared with placement agent and political fundraiser Antoin Rezko stated that the "two men agreed to divert to Rezko and his associate $250,000 out of a $375,000 finder's fee paid by an investment firm that received $50 million in investment funds from the Teachers Retirement System (TRS), on whose board of trustees Levine served."[101]. In a true show of bipartisanship, Rezko used his relationship with Democratic Governor Blagojevich to facilitate Republican Levine's reappointment to the TRS board in the spring of 2004.

During April and May of 2004, according to the indictment, Rezko and Levine arranged to split among themselves and others nearly $5 million in kickbacks from six different investment firms that were then seeking funds from TRS and another state pension fund. Rezko and Levine also allegedly agreed to tell a seventh firm that it would only receive a $220

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[100] http://articles.chicagotribune.com/2012-07-20/news/ct-met-stuart-levine-sentencing-0720-20120720_1_political-insider-stuart-levine-purple-hotel-attorney-christopher-niewoehner

[101] http://www.justice.gov/usao/iln/pr/chicago/2006/pr1011_01.pdf

million allocation from TRS if it either paid $2 million to a consultant who would funnel the money evenly to Rezko and Levine or made a $1.5 million political contribution to a certain public official."[102]

In another attempt to perpetuate the scheme, Levine asked Rezko "to use their relationships and influence with high-ranking state officials to oppose the proposed consolidation of TRS, the Illinois State Board of Investment (ISBI), and the State University Retirement System (SURS), into a single pension fund.[103]

In another somewhat related incident, Hopewell Ventures, founded by David Wilhelm, Governor Blagojevich's former campaign chief and Bill Clinton's 1992 campaign manager, secured a $10 million investment from the state Teachers' Retirement System in December 2003.[104] One of those charged in the Levine matter had demanded a $850,000 kickback the prior year from a Virginia investment firm, declaring, "This is how things are done in Illinois," according to the charges.[105]

In 2005 the Illinois Teachers' Retirement System barred money managers from paying finders' fees to middlemen after Carlyle Group, a Washington private-equity firm, paid $5 million in fees to lobbyist Robert Kjellander. [106] Kjellander was nicknamed the Pension Pirate [107]

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[102] *http://www.justice.gov/usao/iln/pr/chicago/2006/pr1011_01.pdf*

[103] *http://www.justice.gov/usao/iln/pr/chicago/2006/pr1011_01.pdf*

[104] *Chicago Sun-Times Feds probe gov aide's pension role August 11, 2005BY CHRIS FUSCO AND DAVE MCKINNEY*

[105] *Pension kickbacks alleged GOP insider Levine called brains of extortion scheme Chicago Tribune By Matt O'Connor and Ray Gibson August 4, 2005*

[106] *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aq9imGMCP8Qk*

[107] *http://inthesetimes.com/article/2754/*

and, while escaping indictment himself, was mentioned repeatedly in the Blagojevich charges[108] as individual K. [109]

Bill Atwood, executive director of the Illinois State Board of Investments, predicted in May 2009 after the Illinois fiasco that "Placement Agents Are Likely to 'Go Away." [110] Carlyle Group was soon embroiled in scandals in New York and New Mexico.[111]

PERFORMANCE VALUATION

POOR PERFORMANCE

A comparison of the five years ending 12/31/20 for PABF of 8.8% (according to NEPC) with a 70%S&P 500 index 30% Barclays Intermediate at 11.9%, shows approximately $2.6 billion in assets. The shortfall over the last five years has been around $403 million dollars, or over $80 million a year. Only more transparency will reveal how much of this was from excessive fees or how much was from bad underlying investments-- many a result of conflicts of interest. For the most part, the traditional stock and bond managers were OK, but the real estate, private equity and hedge fund managers severely underperformed.

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[108] *http://www.bondbuyer.com/issues/118_64/-302104-1.html*

[109] *http://www.prairiestatereport.us/2013/01/25/senator-oberweis-responds-to-nbc-chicago-attack/*

[110] *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aq9imGMCP8Qk*

[111] *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=atwTqj6OjY7U How Pension Placement Agent Exploited Political Ties ,Martin Braun & Gillian Wee May 18, 2009*

Overall PABF investment performance has been poor for the 3 years ending 12/31/20. They ranked in near the bottom in the 90th percentile according to NEPC. For the 5 years ending 12/31/20, they ranked in the 81st percentile. This change was mainly driven by their high allocation to high fee, high risk alternatives.

Alternative performance has been a disaster for PABF for the 3 years ending 12/31/20. The Russell 1000 Stock index which PABF invests in via Northern Trust averaged 14.02%. Higher risk high fee alternatives performed poorly. Private equity reported at 9.9%, infrastructure at 4.5%, real estate at 1.97% and hedge funds at 1.82%.

This poor alternative performance clearly puts them in violation of their Investment Policy Statement (IPS pg.7) which clearly states:

Relatively illiquid investments, such as venture capital partnerships, real estate holdings, and private capital investments may be made within prescribed limits, with due consideration regarding their impact on overall liquidity requirements, and when the ***excess expected return is sufficient to compensate the Fund for reduced liquidity.***

All the numbers point to the opposite as returns have been negative, especially compared to US public markets.

PERFORMANCE BENCHMARKS

Richard Ennis was the actual consultant for the Chicago Police Pension plan prior to NEPC with his firm Ennis Knupp. He says custom benchmarks like Chicago Police uses are seriously flawed "chasing slow rabbits."

I estimate that statewide pension funds in the United States incur annual investment expenses averaging 1.3% of asset value. A sample of 24 of them underperformed passive investment during the past decade by an average of 1.4% a year. And yet, those same funds report that they outperformed benchmarks of their own devising by an average of +0.3%

a year for the same period. This sharp disconnect raises questions about the usefulness of the funds' performance reporting, as well as their heavy reliance on expensive active management.[112]

A passively investable benchmark (PB) *typically comprises several broad market-cap-weighted indexes. These might include the Russell 3000 stocks, ACWI ex-US stocks, and Bloomberg Barclays Aggregate bonds. These indexes don't tend to overlap and pretty much cover the waterfront. Sometimes the PB is described as a policy portfolio. As the name implies, the benchmark is investable and passively so: It is feasible rather than hypothetical. It provides a baseline to determine whether portfolio management adds value in excess of purely passive implementation. Finance scholars and serious practitioner researchers invariably use PBs to evaluate investment performance. Indeed, the PB is the* essential *benchmark for performance evaluation.*[113]

Compared to a 80/20 Russell 3000/Barclays Ag or a 70/30 Chicago Police comes up way short which is why they have created custom benchmarks.

The custom benchmark (CB) generally consists of additional asset class components that describe how the portfolio manager intends to depart from the PB at the asset class level to achieve a strategically superior, better-performing portfolio. ……….

In practice, the PB — the essential benchmark — has gone by the wayside. Among most institutional funds, the CB has become the sole benchmark in use — or at least the sole visible benchmark in public performance reporting. As a result, insight into the merit of strategic decision-making versus the policy baseline is lost. As we shall see,

[112] *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3883370*

[113] *https://blogs.cfainstitute.org/investor/2021/06/07/institutional-portfolio-benchmarks-slow-rabbits/*

exclusive use of the CB has another, even more perverse effect: It tends to present a rosy, rather than accurate, reading of performance. [114]

What we observe with CalPERS is not an isolated problem but a chronic one: CB returns tend to lag I-PBs by a wide margin. The funds are chasing slow rabbits. ……

To make matters worse, some public funds pay staff bonuses based on performance relative to the CB. Fund trustees should direct their staff and consultant to incorporate a PB in all performance reporting.

The management of public pension funds is bedeviled by agency problems. Here is an opportunity to ameliorate an important one of them. Public pension funds need to find faster rabbits to chase. [115]

Chicago Police custom benchmarks are misleading as they attempt to cover up the underperformance of the more accurate passive benchmarks.

COOKING PERFORMANCE IN 2020

While the NEPC performance numbers could be exaggerated, PABF seems to have wanted to enhance them more for 2020

Major performance discrepancies were discovered in the 2020 calendar year between the NEPC report presented at the board meeting of 10.64% in April 2021, and the Mitchell Titus Audit presented at the June

[114] *https://blogs.cfainstitute.org/investor/2021/06/07/institutional-portfolio-benchmarks-slow-rabbits/*

[115] *https://blogs.cfainstitute.org/investor/2021/06/07/institutional-portfolio-benchmarks-slow-rabbits/*

2021 meeting of 12.9%. ($2.6 billion x 1.75%). That's an extra $45 million in return that miraculously appeared.

The equities and fixed income are kept with the custodian and their performance is exceedingly difficult to manipulate due to the transparency; thus, performance was identical between Mitchell Titus and NEPC. The global asset allocation funds and hedge funds still have some transparency and stayed close to the same.

However, many other alternative assets performances are easy to manipulate since the managers basically make up their own performance. The real estate losses went down from -2.8% to -0.21%: the infrastructure losses went down from -9.2% to a -7.28%: the private equity losses went down from -2.5% to a -1.82%. Private equity gains went up from 14.4% to 16.9%, and opportunistic debt from 12.8% to 15.30%. These manipulations make these numbers more suspect than they were before and taint the entire financials.

REAL ESTATE PERFORMANCE

The biggest headlines on real estate losses in recent years came from Dallas. Real estate losses over the years at Chicago Police may even be worse. Real Estate holdings lack transparency, but it is apparent that many holdings may be in Chicago, and local real estate has a poor record in many public pensions. One DV Urban Realty Partners run by former Mayor Daly's nephew, is so bad it does not show up in any NEPC reports but showed a $12.2 million loss in the 2017 custodial statements. [116]

Since 1995 through year end 2020 PABF have averaged only 5.35% compared to their benchmark the NCREIF Property Index 9.08%.[117]

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[116] https://www.illinoispolicy.org/high-risk-real-estate-investments-cost-chicago-pension-funds-54m-win-fund-managers-9m/

[117] *Rhode Island used the benchmark NCREIF Property Index+100.*

Assuming an average $100 million in real estate assets underperforming -3.73% over 25 years is $93.25 million. Losses over the last 10 years $35.5 million. [118] Hiding real estate performance and valuation seems to be an ongoing practice.

The NEPC year end 2020 performance has omitted individual real estate managers which appears to be a way to hide underperforming managers.

The NEPC year end 2019 performance for individual real estate managers show some incredible losses. The Lone Star X (Lone Star CEO Grayken active in Chicago Politics) has a negative return of -25.53% since December 2017.The Lone Star XI since June 2019 has negative return of -31.22%. The Lone Star Global lost -36.83% in 2019 alone. The Apollo Real Estate Advisors (CEO tied to Jeffrey Epstein) had 3-year losses of -33.56% and 5-year losses of -23.35% as of December 2019.

The NEPC year end 2017 performance for individual real estate managers shows more incredible losses. The BlackRock Asia fund, from its inception in May 2008, lost -50.95%. Newport Capital Partners, from its inception in December 2012, lost -14.97%. Morgan Stanley RE VI, from its inception in July 2007, has lost -14.19%.

While NEPC numbers suggest real estate losses over 25 years is $93.25 million, it could be much higher.

HEDGE FUND PERFORMANCE

Hedge fund losses at Chicago Police are significant. While the real estate and Private Equity composites go back to 1995, it looks like they started a new performance composite for hedge funds starting August 2016. In the short composite through year end 2020 they averaged

[118] *https://chipabf.org/wp-content/uploads/2021/02/2020-q4-performance.pdf*

only 3.29% compared to their benchmark the HFRI Fund of Fund Composite 5.40%.[119]

Assuming an average $150 million in hedge fund assets underperforming -2.11% over 5 years ending December 2020 is a loss of $15.825 million. [120] Hiding hedge fund performance and valuation seems to be an ongoing practice.

The NEPC year end 2020 performance has omitted individual hedge fund managers which appears to be a way to hide underperforming managers.

The NEPC year end 2019 performance for hedge funds before 2020 were close to benchmarks as were the disclosed managers.

PRIVATE EQUITY PERFORMANCE

Private equity losses at Chicago Police are significant. Since 1995 through year end 2020 they have averaged only 8.16% compared to their benchmark the CIA US ALL PE Index 14.13%.[121] Assuming an average $50 million in private equity assets underperforming -5.97% over 25 years the loss is $74.625 million. Losses over last 10 years $15 million. [122] Hiding private equity performance and valuation seems to be an ongoing practice.

The NEPC year end 2020 performance has omitted individual private equity managers. This omission appears to be a way to hide underperforming managers. The practice seems to be growing as more

[119] *Rhode Island used the benchmark NCREIF Property Index+100.*

[120] *https://chipabf.org/wp-content/uploads/2021/02/2020-q4-performance.pdf*

[121] *Rhode Island used the benchmark NCREIF Property Index+100.*

[122] *https://chipabf.org/wp-content/uploads/2021/02/2020-q4-performance.pdf*

public pensions start receiving heat for poor private equity performance. [123]

The NEPC year end 2019 performance reporting has only two individual private equity managers. The Northern Trust 2019 reports 22 “Ghost” private equity managers omitted from performance report.

The NEPC year end 2017 performance in which they had a fire sale of private equity has produced 1-year losses as of 12/31/17 of -9.85% for private equity, including -23.01% Adams Street Partners Direct, -17.36% for Mesirow Fund III, -12.74% for Muller Monroe, -67.75% for Invesco Fund IV Intl, -36.35% for Invesco Fund IV US, -75.73% for Invesco Fund IV Venture, -84.48% for Muller Monroe 2.

The Northern Trust 2017 reports 15 “Ghost” private equity managers omitted from performance report.

LOSSES UNREALIZED

Performance could be much worse than reported. Many of the “ghost managers” that disappear off NEPC reports and are ignored in the Mitchell Titus audit, happen to have poor performance and huge unrealized losses. While these particular losses are most likely counted in the market value of assets and the funding ratio, it is not clear how these losses were accounted for in performance calculations

Several partnerships with huge unrealized losses show up on the Northern Trust 12/31/20 custodial report but are “ghosted” off the NEPC reports and audits. Apollo European Real Estate Cayman Feeder Fund III shows a $2.9mm loss. The fund’s CEO Leon Black has been all over the news with his connections to Jeffrey Epstein. Morgan Stanley - $8.5 mm is a firm that has been fined numerous times. Shamrock Hostmark Hotel Fund, headquartered in Schaumburg, IL., had a $4.3mm

[123] *https://pitchbook.com/news/articles/pensions-under-fire-after-pe-underperforms June 2021*

loss.   Carlyle Infrastructure Fund had, a company that got in trouble in NY for pay to play showed a -$3.5 million loss. Others include: AG Core Plus Realty Fund II -$3mm, DRA Growth and Income fund VI -$1mm, Sound Mark Horizons Fund -$2.6mm loss, Global Infrastructures Partners III -$1.8 mm loss on NT 2020 year end.

Perhaps the worst losses on the Northern Trust 12/31/20 Custodial Report come from six Brinson Partners Private Equity Partnerships totaling -$19.6mm in unrealized losses. [124] Not only was Brinson himself a major Chicago political donor, but the firm that currently managers the Brinson partnership, Adam Street, is detailed in the pay for play sections of this report.

A few partnerships with huge unrealized losses have shown up on recent Northern Trust Custodial Reports and were "ghosted" off the NEPC reports and audits.   The Illinois Private Equity Funds of Funds LP showed a -$6.9 mm loss on the NT 2015 statement, but disappears, perhaps under the Muller & Monroe or M2 names for a private equity fund of fund manager.

Perhaps the most infamous investment last shows up on the Northern Trust 12/31/17 Custodial Report with a -$12.2 million loss and was already "ghosted" off the NEPC reports and audits.   DV Urban Realty Partners was noteworthy because one of main partners was the nephew of former Mayor Daly. [125]

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[124] *Brinson Pship Fund Tr-2002 Secondary $0.6 mm loss on NT 2020 year end Brinson Pship Fund Tr-2003 Primary $1.9 mm loss on NT 2020 year end   Brinson Pship Fund Tr-2001 Primary $2.1 mm loss on NT 2020 year end Brinson Pship Fund Tr-1998 Primary $3.7 mm loss on NT 2020 year end Brinson Pship Fund Tr-1999 Primary $2.5 mm loss on NT 2020 year end Brinson Pship Fund Tr-2000 Primary $8.1 mm loss on NT 2020 year end*

[125] *https://www.illinoispolicy.org/high-risk-real-estate-investments-cost-chicago-pension-funds-54m-win-fund-managers-9m/*

Performance numbers are incomplete with all the secret managers. The mainstream stock and bond managers for the most part seem to have average performance.

COOKING THE BOOKS

Performance of these alternatives may be worse. Public pension plans usually have two sets of books for investment performance, but we may have three with PABF. PABF seems to have a clean set of performance books of traditional stock and bond managers which comply with Global Investment Performance Standards (GIPS). Most likely they have a cooked set of performance books of private equity, hedge funds & real estate managers, all of whom refuse to comply with GIPS standards. These alternative managers make up their own valuations and thus performance.

Since most receive additional excessive fees from higher performance, they have every incentive to provide exaggerated valuations and performance. PABF has a 3rd set of performance books with their "Ghost Managers".

VALUATION

Valuation is troublesome for most alternative investments. Valuation is a major focus of the current FBI investigation in Pennsylvania. There is political motivation for over valuation in Pennsylvania. In Pennsylvania it appears that overvaluation was manipulated to prevent triggers to force teachers to make substantially more contributions which would draw unwanted attention.

Chicago the city which many feel has effective control of the eight-member board (four city officials report directly to the mayor and two active police officers are indirectly under mayor) has an incentive to overvalue the portfolio. The overvaluation reduces immediate budget demands on the city and lowers the costs of bonds. In 2013, the SEC charged the state of Illinois with securities fraud for misleading municipal bond investors by overvaluing the pensions and undervaluing liabilities. [126]

The alternative investment managers have an incentive to overvalue the portfolio since it increases their immediate performance bonuses. There are no effective controls on this potential overvaluation.

Alternative managers make up their own valuations as noted in the fine print in the Mitchell Titus financial statements in several years tested *"Hedge fund, venture capital, private equity, infrastructure, and certain opportunistic investments are reported at estimated fair value as determined by the general partner of the investment vehicle."* The CPA firm admits that there are no controls on alternative mangers making up their own valuations.

Since most receive additional excessive fees from higher performance, managers have every incentive to provide exaggerated valuations and performance.

PABF has refused to provide many documents that disclose fees and even names of underlying documents.

Stated Performance was not good, but it could be worse if the current valuations are exaggerated. The valuations on the traditional stocks and bond managers with the securities held at Northern Trust seem to be solid and they comprise around 70% of the portfolio. It is the other 30% of the portfolio of alternatives that is very prone to valuation risk.

[126] *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171513202#.Up48l9JDtRs*

Alternative managers in liquidation could be worth 70 cents on the dollar in valuation which means PABF could even be worse funded than reported.

Other experts have warned that because firms' alternative investments are not independently valued by third-parties, managers can use their own valuation process to fleece investors. [127]

REAL ESTATE VALUATION

The biggest headlines on national real estate losses in recent years came from Dallas. Real estate losses over the years at Chicago Police may be even worse. Since 1995 through year end 2020 they have averaged only 5.35% compared to their benchmark the NCREIF Property Index 9.08%.[128] Assuming an average $100 million in real estate assets underperforming -3.73% over 25 years is $93.25 million, losses over the last 10 years come to $35.5 million. [129] Hiding real estate performance and valuation seems to be an ongoing practice. *Fraud Magazine* said the following:

The rise and fall of the Dallas Police and Fire Pension System because of these non-traditional investments provides a cautionary tale Heavy investment loss left the fund only 45 percent funded, and the fund's consultant projected it would be insolvent in 15 years. News of the losses caused police and firefighters to retire in droves and withdraw their Deferred Retirement Option Plan accounts in lump sums. The fund's trustees had asked the city of Dallas for an immediate contribution of

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[127] *http://www.ibtimes.com/political-capital/paradise-papers-your-retirement-cash-may-be-caymans-can-you-get-it-back-2615694 November 2017*

[128] *Rhode Island used the benchmark NCREIF Property Index+100.*

[129] *https://chipabf.org/wp-content/uploads/2021/02/2020-q4-performance.pdf*

more than $1.1 billion, which Dallas Mayor Michael S. Rawlings and City Council member Lee Kleinman said threatened to bankrupt the ninth-largest city in America. (See Dallas Stares Down a Texas-Size Threat of Bankruptcy, by Mary Williams Walsh, The New York Times, Nov. 20, 2016.) 130

Dallas Police & Fire has double the funding ratio of PABF and the likelihood of Dallas going bankrupt is far less than that of Chicago, but this fact does not seem to have registered with the public or police in Chicago. Dallas Police & Fire used consultant NEPC from 2006 to 2018 when they were not rehired.

Dallas has filed some lawsuits against real estate managers to recover losses. It is unclear if PABF has, but a sister Chicago teachers' pension did recover money from the before-mentioned Daly nephew's real estate fund. [131]

Local real estate valuation is a major focus of the FBI investigation in Pennsylvania. There is political motivation for over-valuation in Pennsylvania Chicago Mayor is reputed to have effective control of the eight-member board (four city officials who report directly to Mayor and two2 active police officers indirectly under mayor). In fact, Chicago has an incentive to overvalue the portfolio and reduce immediate budget demands on the city.

The alternative investment managers have an incentive to overvalue the portfolio since it increases their immediate performance bonuses.

There are no effective controls on this potential overvaluation of real estate.

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[130] https://www.fraud-magazine.com/article.aspx?id=4295000920

[131] https://www.ctpf.org/news/ctpf-statement-dv-urban-realty-partners

DENIAL OF PUBLIC RECORDS REQUEST

During May and June 2021, we filed six requests for an opportunity to inspect or obtain copies of public records related to primarily the pension's investment managers.

The *overwhelming majority* of the most critical disclosure information we requested was *summarily* denied or redacted.

Open Records request 1 on May 25, 2021, to the Chicago Police Pension Fund was for basic documents that appear on many public pension websites. Even this basic request which should have taken minutes they played games. At the last minute of legal deadline on June 2 they asked for another 5 days. was delayed and was somewhat delivered on June 9 with more documents June 14.

Open Records Request A was to the State Government, Governor's office for Economic Opportunity, on May 31st asking for a report that Chicago Police Pension provides to the state. There were numerous delays, and when finally received On June 14th 100s of names of investment managers and investments were (in our opinion illegally) redacted.

Open Records request 2 on June 7, 2021, to the Chicago Police Pension Fund was for annual reports that came directly from each manager for year ending 2015,2016,2017, 2018,2019,2020, 1q2021 that include valuation, performance, and fees. These include all alternative managers. On June 14 playing games they asked for 10 more days. On July 6 they ask for another day. On July 7 they provide a coded response in which they deny all the useful information.

Open Records request 3 on June 7, 2021, to the Chicago Police Pension Fund was for names of the underlying funds in all of the funds of funds invested in since 2015, by fund of fund. This includes private equity, hedge fund and other funds of funds. On June 14 they rejected the request entirely.

Open Records request 4 on June 14, 2021, to the Chicago Police Pension Fund was for Investment Manager Contracts All contracts, including any offering documents and subscription agreements, between the fund and its investment managers from managers held since 2015 including those hired before 2015, but held into 2015 forward. Please list all investments in limited partnerships and provide those partnership agreements and documents. This includes private equity, hedge funds and real estate. On or around July 7 they rejected the request entirely.

Open Records Request 5 on June 21 asking for a report that Chicago Police Pension provides to the state. There were numerous delays, and when finally received, on July 7th 100s of names of investment managers and investments were (in our opinion illegally) redacted.

It appears that PABF repeatedly simply permitted the investment firms involved to unilaterally determine whether the information we sought on behalf of stakeholders had to be disclosed under Illinois law. Not surprising, most firms granted the opportunity to oppose public scrutiny of their dealings especially fees with PABF, chose to do so.

Very disturbing is that, *not a single* prospectus or offering document required to be provided to *all investors* under the nation's securities laws was provided to us in response to our public records request.

As a result of the extensive denials of important public records requests, it is impossible for PABF stakeholders to evaluate the investment strategies, performance, fees, risks, and conflicts of interest related to the pension's investment portfolio.

The lack of cooperation by PABF is all-the-more surprising given that PABF is well-aware that this forensic review of the pension was commissioned, as well as paid for, by hundreds of participants, with the stated objective of improving management and oversight of the pension. Pension fiduciaries solely concerned with the interests of participants and beneficiaries should welcome, not oppose, a free independent review by nationally recognized experts in pensions.

In our opinion, transparency, which would add not a single dollar of additional cost to the pension but would swiftly move to reduce a number of problems—excessive fees, reckless risk-taking, unaddressed conflicts of interest, gross mismanagement and potential malfeasance.

POOR MANAGEMENT & GOVERNANCE

BOARD STRUCTURE

Board structure guides the long-term results of the Chicago Police Pension plan, and this poor structure is key in driving one of the worst pensions in US History.

The Board structure itself creates this endless cycle of underfunding and adds to the lack of transparency. The mayor and or maybe the Aldermen, should appoint independent members of the community instead of financial staff of the City in charge of the day to day function of the government. These city financial officials are put into a horrible conflict of interest between short term budget needs of the city and the long-term needs of the Police Pension.

A prudent fiduciary structure for public pensions is to have a combination of elected and appointed independent trustees and a professional staff. The Chicago Police Pension governance structure makes a mockery of this. 4 of the 8 trustees are direct employees of the mayor with another 2 elected active police officers report indirectly to the mayor via the police chief. This board structure inserts excessive conflicts of interest as the mayor's immediate political goals of a city budget and political fundraising can overshadow the long-term fiduciary goals of running a pension.

STAFF STRUCTURE

Almost all pensions hire professionals for their 2 top positions, Executive Director or CEO and Chief Investment Officer (CIO). Chicago Police is the only pension I know of in 30 years' experience that an unqualified Trustee has inserted himself as Chief Investment Officer (CIO). It is widely seen as a conflict of interest for a board member to become a Executive Director or Chief Investment Officer, much less hold both positions simultaneously which is unheard of nationally except for PABF.

The Chair of the Board of Trustees Thomas Beyna an active-duty Chicago Policemen has simultaneously served as Chief Investment Officer (CIO) for the last 30 months. Beyna has no investment or even financial qualifications to be Chief Investment Officer but has had 22 allegations of misconduct as a police officer including one for bribery/official corruption. [132]

One of the main qualifications for public pension investment staff and investment consultants is the CFA charter. While PAPF has had CFA charter holders on staff and as consultants in the past currently no staff or consultants hold a CFA charter. With the deliberate vacancy of an investment professional there seems to be no plans to hire qualified professionals.

This is not a first for PABF. In November 2014 after the CIO resignation Trustee and Lieutenant James Maloney was named CIO and he served 17 months until a CIO was hired

The Kentucky plan the all-time worst funded in history at 14% did transform a board trustee into the Executive Director position in 2016. Several months ago, in 2021 the Illinois legislature voted 114 to 0 that they would impose a 12 month ban on any board member to work for that system or a vendor. This seems to be in response to the Chicago Teachers Board member moving to the Executive Director spot. [133] While Beyna's move would probably be illegal today there does not seem to be

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[132] *https://m.cpdp.co/officer/1950/thomas-beyna/*

[133] *https://capitolfax.com/2021/05/11/its-just-a-bill-273/*

any movement to correct this breach with the hiring of a professional CIO as he hides behind a grandfathering defense.

Erin Keane the Current Executive Director of Chicago Police pension while not violating this rule specifically, could be said to be violating it in spirit. Chicago Police has sister plans which are very similar in funding and even investments. Keane served on the board of 3 of these plans (Chicago Municipal Employees, Fire & Laborers) as Ex-Officio board member and 2 of the plans as Vice President of the board.

PABF has major conflicts of interest with both of their top staff positions. The nearly 3 year move by an active police officer to weaken oversight by taking dual roles as trustee and chief investment officer is a major conflict.

INVESTMENT OVERSIGHT WEAKNESS

The investment decision-making at the Chicago Police Pension Fund (PABF) is erratic and unprofessional at best. Having a police officer with no financial management training or experience assume the duties of Chief Investment Officer (CIO) is a breach of fiduciary duty.   The minutes and other documents available on the website show no evidence of prudent decision making. The PABF has not provided sufficient information or explanation via the Freedom of Information Act (FOIA).

In 2014-2015, with a police officer as CIO, the hedge fund of funds portfolio was 90% liquidated going from $100 mm to $9 mm over several months.[134] There is no explanation for this erratic behavior.

The primary source of information has been the trade press, specifically *Pensions & Investments (P&I)* for information on the PABF investment process since minutes are vague at best.   *P&I* of April 5, 2017, reported

[134] *https://chipabf.org/pdfs/cafr/cafr_2015_final.pdf Pg. 8*

that PABF was going to dump their entire private equity portfolio because, as a low funded plan, they need to get rid of illiquid assets like Private equity.   P&I reports the sale of the PABF private equity portfolio February 26, 2018. These types of sales usually result in large losses, but it is uncertain if this was measured in the investment performance.

From NEPC total   private equity investments as of yearend 2015 was $240mm, yearend 2016 $121mm, yearend 2017 $83mm and by March 2018, only $12mm. Sales produced one-year losses as of December 31, 20177 of -9.85% for private equity, including -23.01% Adams Street Partners Direct, -17.36% for Mesirow Fund III, -12.74% for Muller Monroe, -67.75% for Invesco Fund IV Intl, -36.35% for Invesco Fund IV US, -75.73% for Invesco Fund IV Venture, -84.48% for Muller Monroe 2.

According to P&I, on December 1, 2017, PABF hired two somewhat illiquid hedge funds. Despite claiming they needed more liquidity due to the low funding ratio, they continued to do the opposite adding four illiquid real estate managers in 2018.   Then in the next year, October 9, 2019, the PABF decided to invest again in illiquid private equity and selected a manager in February 2020.   This appears to be a strategy to maximize fees for Wall Street—not returns for the plan.

Hedge funds seem to appear and disappear off of the financials and NEPC reports. At yearend 2015 Aetos Capital and K2 Advisors Hedge fund of funds each have around $50 million. By end of 2015, both are down to around $9mm. By August 16, both are gone and Plusious Fund of Fund comes in with $20mm.   EnTrust Permal shows up with $50mm in February 2017.   Neither hedge fund appears on the audited financials fee page in December 2017. Blueprint shows up as private equity in August 2017 but is then classified as a hedge fund of fund in 2018. All are on NEPC December 19, Blueprint and Pluscios make the 2019 financials: EnTrust Permal does not.

In the fine print of their contracts, most alternative (ie hedge funds private equity, real estate) investment managers say they are not a fiduciary to the plan which is a violation of the PABF Investment Policy Statement. This is evidently the reason for PABF to refuse FOIA requests for the manager contracts. The contracts would if disclosed document violations of state fiduciary law and the investment policy statement.

OFFSHORE INVESTMENTS

It is unclear how many offshore investments are in the Chicago Police plan, but there clearly are some like the Apollo Real Estate Caymans.

I was quoted in International Business Times (IBT) in November 2017 that *"Based on SEC data, it appears that public pensions alone hold around $300 billion offshore in the Cayman Islands in hedge funds and private equity,"*[135]

Former SEC attorney Edward Siedle told IBT that Wall Street firms may set up shell corporations in tax havens *"not to help public pension fund investors, but really to protect the managers from taxes and regulations."* [136]

"Out of all the risks of moving pensioners' money overseas," said South Carolina State Treasurer Curtis Loftis, *"few raise as much concern as "custody," or where pensioners' money and assets are ultimately stored and accounted for."*. He noted that whereas state and local governments' investments in stocks and bonds are typically held in U.S.-regulated banks, offshore funds can hold money in opaque accounts and

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[135] *http://www.ibtimes.com/political-capital/paradise-papers-your-retirement-cash-may-be-caymans-can-you-get-it-back-2615694 November 2017*

[136] *http://www.ibtimes.com/political-capital/paradise-papers-your-retirement-cash-may-be-caymans-can-you-get-it-back-2615694 November 2017*

brokerages across the globe. "Custody was a pretty big part of the Bernie Madoff and Jon Corzine problems," Loftis told IBT, referring to high-profile cases where investors lost their money. He said, *"Those guys were custodying money all over the world, allowing them to do all sorts of things with it because offshore does not have the same protections as in the United States. So, when public pensions are investing offshore, they are agreeing to have their money custodied in ways that are very risky."* [137]

Mary Pat Campbell, a self-described conservative and actuarial expert, commenting on the offshore piece by progressive writer David Sirota wrote:

Now, I don't particularly have a problem with hedge funds, private equity the Caymans, Bermuda, etc. But let us not be coy about the reasons for these items: they're trying to optimize returns by using legal structures that …I think this is just fine for private investors… I don't think this is fine for public pensions.[138] *So here's the problem as a member of the public: I can read the CAFR for a public pension plan. For public securities, anyone can get the valuation information. But not for hedge funds or private equity.*

More to the point, if all these arrangements are private… how do we know the deals are aboveboard? Sirota and Ted Siedle like to point to the asset management fees. But fees aren't the only issue. Do these investments really have adequate oversight? We saw some incredible meltdowns in

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[137] *http://www.ibtimes.com/political-capital/paradise-papers-your-retirement-cash-may-be-caymans-can-you-get-it-back-2615694 November 2017*

[138] *http://stump.marypat.org/article/864/are-hedge-funds-or-private-equity-investments-appropriate-for-public-pension-funds*

Dallas over awful alternative investments, and that was local real estate. [139]

Discussing Sirota's assertions of fraud Campbell points out that it doesn't take fraud for a public pension to lose money and sees two big problems:

1. These assets are opaque, difficult to value, and when they go bad, they can go catastrophically bad without the legal protections common stockholders or bondholders get in the U.S. system. It does not take any outright fraud for a lot of money to be lost. Long Term Capital Management wasn't a fraud — they just screwed up massively. Is it appropriate for pension funds which are supposed to guarantee very non-volatile pension benefits to get into such risky assets? Or, let me put it another way: is it appropriate that public pension funds put ***so much*** *of their portfolios in such strategies?* [140]

2. The lack of transparency in the arrangement makes the situation ripe for outright corruption. If outside interested parties cannot tell the terms of the arrangement – such as fees, etc. – how do we know these arrangements are on the up-and-up?

Campbells points out the risk of playing with taxpayer money.

But it's not the public pension fund manager's money. It's supposed to cover the pension benefits. And if the manager assumes that the taxpayers can make investment losses good, then they're really playing with taxpayer money. Is it an appropriate use of taxpayer money to try to chase yields? I understand you're trying to achieve the assumed

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[139] http://stump.marypat.org/article/864/are-hedge-funds-or-private-equity-investments-appropriate-for-public-pension-funds

[140] http://stump.marypat.org/article/864/are-hedge-funds-or-private-equity-investments-appropriate-for-public-pension-funds

investment returns that evidently public securities haven't provided. But this can be like doubling down at the casino – the martingale betting system of doubling bets, of making larger and larger bets, often ends in complete ruin as one does not have infinite money to bet with. [141]

Siedle in his North Carolina report points out that many alternative investment funds that are incorporated and regulated under the laws of foreign countries, present additional, unique risks which pension fiduciaries must consider. Also, since alternative investment assets are held by different custodians located around the world, as opposed to being held by the plan's master custodian, the custodial risks are heightened and should be considered and disclosed to the public. [142]

CONSULTANT CONFLICTS

Many public pension reviews fail to monitor external consultant conflicts of interest. During the period being examined, New England Pension Consultants (NEPC) has been the sole consultant to the PABF. I was a Senior Consultant for NEPC from 2008-2009, am familiar with their practice and believe they have fewer conflicts of interest than many other major consulting firms. However, there are still some concerns.

Like many other leading Investment consultants NEPC has a bias toward high fee high risk alternative investments. They overstate potential

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[141] *http://stump.marypat.org/article/864/are-hedge-funds-or-private-equity-investments-appropriate-for-public-pension-funds*

[142] *North Carolina Pension's Secretive Alternative Investment Gamble: A Sole Fiduciary's Failed "Experiment" By Edward Siedle*
http://nebula.wsimg.com/2c61c80993914081e45d8ee4ad97e4d2?AccessKeyId=706D4353590FAA6ED8CE&disposition=0&alloworigin=1

return and understate risk, and this has been borne out in the underperformance of Chicago PABF.

The NEPC philosophy favors high fee high risk alternatives by using assumptions that exaggerate their returns and lower their perceived risk in their asset allocation models. They look at risk in one-dimension standard deviation which can easily be gamed by private equity and real estate smoothing of valuations. Alternatives contain, liquidity, fee, governance, regulatory, and many other risks they ignore.

Their geometric assumption for the returns of the S&P 500 is 5.4% while their return assumption for private equity is 9.3%. They love private equity giving it a 70% premium (only 49% more volatility) after fees over the S&P index.

Their geometric assumption for the returns of the Barclays Aggregate bond index is 1.4% while their return assumption for Private Debt is 6.1%. NEPC loves Private Debt giving it over a 300% premium after fees over the Aggregate bond index. More egregious is they contend High Yield and Private Debt will have similar volatility of 11%, but that that Illiquid Private Debt Returns will be 6.1%, double that of high yield at 2.9%.

Like many of the consultants in love with hedge funds NEPC lowered their return expectation to 4.0% from around 8.0% There is just enough transparency in hedge funds that they could not hide their horrible performance over recent years. They justify hedge funds by saying they lower risk with a standard deviation of 8.7% compared to 16.6% for the S&P 500.

Alternative investment has put NEPC in trouble with several plans. With the Fairfield CT Police & Fire Plan they put them in the Maxam

Hedge Fund of Funds which happened to have Madoff as one of the secret hedge funds underneath, and they were sued. [143] Dallas Police & Fire used NEPC from 2006 to 2018 when they were not rehired after poor alternatives (especially real estate) performance.

One possible conflict arose when investment manager GMO was hired by PABF in 2011 to manage over $200mm. GMO employed a spouse of a NEPC executive.

More inspection may produce more conflicts, but the $400,000 paid annually to NEPC is relatively small compared to the huge undisclosed fees paid to alternative managers. NEPC's main fault has been promoting underperforming, high fee alternative managers in their asset allocation recommendations.

FINANCIAL MANAGERIAL OVERSIGHT WEAKNESS

The Accountability Group has received numerous complaints from Retirees, Disabled Officers and Widows who have been concerned with the poor treatment of retired and disabled police officers by the staff, Trustees and Management. They have also expressed concerns with financial oversight.

A detailed examination of audited financial statements from 2019 shows poor expense control on the administration of the fund. Total costs went from $4.064 mm in 2018 to $4.734 mm in 2019 or 16%, while personnel salaries & benefits went from $1.827 mm to $2.796 mm or 53% in 2019. According to the minutes of JUNE 26, 2020, there was a Presentation by Mitchell Titus, of the Fund's Annual Financial Report

[143] *https://www.nytimes.com/2009/04/07/business/07consult.html*

Audit and Financial Statements for the year ending 12/31/2019. The minutes reflect no discussion whatsoever of these increases and it passed unanimously. Either the trustees rubberstamped the financials without paying attention, or they knew it would not look good and they kept it as quiet as possible.

Another questionable part of the financials is the $13.6mm Gift Reserve Fund. [144] The accountability group had asked for funds to pay for a wheelchair needed by a disabled officer but were denied without explanation. The board has no apparent rules or procedures or controls for this Gift Fund despite its size. .

The Chicago Police Pension has decided to stop issuing Comprehensive Annual Financial Reports (CAFR). They did not do one in 2019 and are not doing one for 2020. This is highly irregular for such a large pension.

The CAFR is one of the most important documents for any local or state government to establish financial transparency and establish credibility with its creditors and oversight agencies.

Most state and local governments are required by law to issue basic financial statements, and some, including Texas, are legally required to issue a CAFR as well. Many governments not required to issue a CAFR do so anyway because it represents a best practice in government finance.[145]

It is not clear why the Chicago Police Pension one of the worst funded pensions in U.S. history is creating less transparency in its financial statements.

[144] *https://chipabf.org/pdfs/audit/final_pabf_fs_2019.pdf Pg 40*

[145] *https://www.bakertilly.com/insights/the-benefits-of-cafrs*

The Accountability Group continues to find questionable spending and expenses in their own FOIA requests which call for a deeper look into those issues as well.

BUILDING LEASE

Members of the Chicago Police Accountability Group have questioned if PABF is paying too much to lease it's building.

They have questioned why they signed a non-cancellable 16-year lease now costing $354 thousand a year working up to $476,000 a year in 2031. A more typical office space lease is 3 to 5 years.

PABF is paying $32 a square foot currently which goes up in steps to $40 a square foot in 2032. While this is not unusual pricing for the Chicago Loop, there are buildings in the $20-$25 square foot price range. [146]

Are they paying for too big an office? According to the staff directory PABF has 21 employees.[147] Space requirements are around 150 square feet per employee[148] This means PABF needs around 3,150 ft of office space for daily operations. They have leased 10,809 square feet over triple that amount. An argument can be made of having a large public conference room, but it would be more cost effective to rent this space since it is used only once a month.

From these numbers it Is conceivable that PABF could get by with 3,150 square feet at $20 square foot in a lower rent space in the Chicago Loop. This adds up to $63 thousand a year. They currently pay $354 thousand or 561% (5 times) that amount for their lease, and it continues to go up every year.

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[146] *https://www.cityfeet.com/cont/chicago-loop-chicago-il/office-space-for-lease?llz=41.88151,-87.63202,16z*
[147] *https://chipabf.org/wp-content/uploads/2021/06/Staff-Directory-June-2021.pdf*
[148] *https://www.officefinder.com/how.html*

DISABILITY

I am not an expert on disability issues, however serving as a public pension trustee, I sat in on several disability committee meetings. What I found in my experience as a trustee was that there was staff and a few trustees who seemed to take pleasure in denying benefits. They also tended to hire Doctors who shared their bias against disabled officers and many of these Doctors have had other ethical issues.

There seems to be an attitude of discrimination in the disability function of the Chicago Police Pension system. One trustee brags on denying disability benefits and follows injured officers to attempt to prove they are not disabled. Unqualified Doctors are hired for an agenda to lean toward denying benefits. They also appear to be a pattern of bias against female police officers.

This report will recount some of the stories of disabled officers to try to provide transparency on these issues.

This information comes from officers directly and indirectly via members of the Chicago Police Pension Board Accountability Group. This is one side of the story from interviews. The PBAF management may have another side which they have ample ability to provide.

STORIES

Anonymous officer 1 complained of excessive examinations and threats to discontinue benefits if she refused to show up for yet another scheduled FCE/IME examination. This officer also states that her medical records were shredded by the Pension Board Physician and she was forced to go see the doctor again after he lied in his email to the Disability Manager that she didn't give him her medical reports.

Anonymous officer 2 is forced to do a ridiculous FCE test including one to push a 2000 lb car to prove he didn't have a back injury. He had to hire an attorney.

Anonymous officer 3 committed suicide. Many in the group believe excessive surveillance caused depression contributing to his death.

Anonymous officer 4 after having her leg amputated was refused a wheelchair and ramp by the City of Chicago, Chicago Police Medical Section and the city refuses to pay her ongoing medical bills.

Living out of state and clearly total and permanently disabled, this Officer 4 continues to be forced into excessive examinations and still needs to prove she is disabled by submitting yearly medical records and forced into yearly examinations by the Pension Board disability manager. Retirees asked numerous times during CHIPABF pension board meetings to help this catastrophic officer with her needs by using a part of the $13 Million gift reserve fund.

Anonymous officer 5 after being approved for disability was harassed in examinations by the PABF physician. She said the Pension Board berated her for *"being too young to be on disability"* without even doing an examination. She accuses physician of falsifying exam records.

Anonymous Officer 6 Female was sitting in front of the trustees applying for disability when an elected trusteed rudely interrupted her saying, *"You only have three or four years on the job and didn't pay into the pension!"*

Anonymous Officer 7 was followed to the grocery story by an elected trustee carrying a small bag of groceries. Elected trustee filmed him walking up his stairs and approached saying*, " I have you on film and you will go back to work, retire or I will file charges for disability fraud."*

Anonymous Officer 8 a 61-year-old male was ordered back to work. He had to move back to Chicago for two years on the job.

Anonymous Officer 9 female had two fina fusions, two steel plates, screws and bolts from a cadaver holding her spine together. During her hearing she was yelled at by an elected trustee, *"You're morbidly obese* *and a disgrace to the uniform and no longer qualified to be a duty disabled officer."* Trustee threw out previous pension board doctor medical records citing this officer was duty disabled. Trustee then replied, *"We have Dr Orris and he sided with the trustees she is no longer disabled."* She returned to work and finally retired because she couldn't work with all the pain.

Another issue that received dozens of concerned comments from officers was not receiving **duty availability in their duty disability payments.** The staff and trustees need to discuss this issue in public meetings and come up with transparent policies around this issue.

COURT CASES ON DISABILITY

The Illinois Court of Appeals reversed the denial of benefits by the Retirement Board of the Policemen's Annuity and Benefit Fund of the City of Chicago (Board)

"*We agree with Ms. Nelson that the injury she experienced was in her performance of an act of police duty. She was on duty, responding to the call of a violent crime, when the trauma of her fear and the lack of support from her dispatcher caused her to experience PTSD. Regardless of whether she ever encountered the alleged offender, she was experiencing the special risks of police duty when she suffered the trauma that led to her disability.*[149]

This case shows a pattern of prejudice against female officers and mental disability. Dr. Alan Hirsch who was used by the board to make the psychological evaluation that said Ms. Nelson was not disabled. Dr. Hirsch's evaluation was not only rejected by the court, but he has a troubling record outside his work for Chicago Police Pension. Dr. Alan

[149] https://courts.illinois.gov/r23_orders/AppellateCourt/2020/1stDistrict/1192032_R23.pdf

Hirsch's company Sensa was fined $26.5 million[150] to settle charges of unfounded weight-loss claims" and was fined $905,000 to settle false advertising charges California.[151]

In another 2019 case De Jesus v. Policemen's Annuity & Benefit Fund of Chicago was thrown out on the technicality of a missed deadline. The Accountability group feels that the pension board failed to notify disabled officers they were entitled to pensionable duty availability pay and failed to inform them they had 35 days to appeal benefits after retirement. They felt this secrecy and lack of transparency by the fund was deliberate to deny benefits adding to pensionable income.

SURVEILLANCE

While surveillance can be legal with private disability annuitants it is often abused. Anonymous officers 1 and 4 claimed to be subject to surveillance abuse.

The CPD Pension Board Accountability Group questions its use, especially using public plan resources to spy on police officers by elected trustees.

In the private sector a legal website reports: *In response to insurers' high demand for surveillance "evidence" to use against claimants, a cottage industry of boutique disability investigative firms has sprung up nationwide…….. The primary problem with today's advanced surveillance techniques is that they provide insurance companies with a comprehensive system for manufacturing "evidence" that the companies can misuse to argue that a claimant is lying about his or her condition…… Individuals with legitimate claims often find themselves targeted by*

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150 https://www.ftc.gov/sites/default/files/documents/cases/140107sensacmpt.pdf?fbclid=IwAR2Z2itEsxpl1xplXfeGv1Rinov75lwrUWe-xM4YiGvBCbTxUVkTFs043IE

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improper surveillance or denied benefits based on misconstrued "evidence." [152]

Denial of some disability claims for law enforcement revolve around stigma like mental illness.

"Stigma about mental health is very real, at least in certain law enforcement agencies," Davies said. "I had a sergeant tell me not to mention mental health around here." Davies fears ignoring reality could actually cause harm to individuals who need treatment but who won't seek help for fear of being fired.[153]

The CPD Pension Board Accountability Group has found one Trustee who they feel has been overzealous in his denial of valid disability benefits. They point to a statement they provided he used in an application for another job.:

"During my 5 years as the elected trustee, I conducted multiple investigations of suspected pension fraud. The result was that during my tenure, 67 officers either went back to work, resigned or retired. This alone had saved the fund in excess of 27 million dollars had these cases gone unchecked."

One officer was angry about these remarks because of the officer who committed suicide which she attributed *"because he was hounded like a dog by the board over his disability benefits."* This trustee taking surveillance duties upon himself is a clear conflict of interest. If surveillance is to be done at all there must be clear guidelines and policies.

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[152] https://www.disabilitycounsel.net/resources/articles/misuse-of-surveillance/

[153] https://disabilityrightsnc.org/news/press-release/police-officer-ada-lawsuit

CONCLUSION

The Chicago Police pension is one of the worst funded public pension plans in the U.S. today and in U.S. history. It has a conflicted management structure and a total lack of transparency that it puts the interest of Wall Street & Chicago Investment Managers over its own current and retired officers.

PABF has hidden $10s of millions in investment fees, while denying payment for a disabled officer's wheelchair. Investment performance over the last 5 years has been poor. The toxic mix of the defunding of the police pension, conflicted and high-risk investments, and the poor management of the PABF demand the transparency and accountability this report will provide.

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BIO

Chris Tobe is uniquely qualified as he was a Trustee for the only major public pension with the worst funding ratio in the US, the Kentucky Employees Retirement System, and he wrote a book on this experience called Kentucky Fried Pensions

Chris Tobe, CFA, CAIA is author of the "Kentucky Fried Pensions" currently serves as the Chief Investment Officer of the Hackett Group which consults to Public Pension plans where in 2016, he completed a major investment audit for the $40 billion Maryland System in 2015 he completed an investment performance review of the $26 billion Utah Retirement Systems. From 2008-2012 he served as a Trustee and on the Investment Committee for the $13 billion Kentucky Retirement Systems. From 2008-2009 he was a Sr. Consultant with NEPC and worked with a number of public pension plans in OK,MO, MI, DC. From 1997-1999 he worked with KY Auditor Ed Hatchett and published a report on the investments of both KRS & TRS Systems. He earned an MBA in Finance and Accounting from Indiana University Bloomington and his undergraduate degree in Economics from Tulane University. He has the taught the MBA investment course at the University of Louisville, and has served as President of the CFA Society of Louisville. As a public pension trustee in 2010, he completed the Program for Advanced Trustee Studies at Harvard Law School and in 2011, the Fiduciary College at Stanford University. See more at http://www.christobe.com/publicpensions/

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Disclaimer

Tobe Consulting has conducted a high-impact, limited preliminary forensic review of the pension. The purpose of a high-impact limited forensic review is to readily identify, at a reduced cost, deficiencies which, in our opinion, if addressed, would significantly improve investment management and performance results and some governance and transparency issues.

As noted earlier, our requests for key documents from the pension were overwhelmingly rejected. As a participant-funded review, we had limited opportunity to communicate with or interview people directly associated with the board. We held a limited number of telephone interviews with various individuals and firms. Nevertheless, we believe that our expert findings are credible and our recommendations, if followed, would result in significant improvements. In the likely event that PABF or its vendors disagree with our opinions, and are willing to fully disclose all the relevant documents, we welcome the opportunity to review the totality of the relevant information. We reserve the right to change our findings in the event that additional information should be forthcoming.

This report should be read and evaluated with several caveats in mind. First, many of the subjects addressed in this report are inherently judgmental and not susceptible to absolute or definitive conclusions. We assumed the information we were provided, whether by the service providers or PABF is accurate, and could be relied upon. We were not hired to detect or investigate fraud, concealment or misrepresentations and did not attempt to do so. We were not hired to, and did not attempt to conduct a formal or legal investigation or otherwise to use judicial processes or evidentiary safeguards in conducting our review. Our findings and conclusions are based upon our extensive review of limited documents, the limited interviews we conducted with the board and others associated with PABF, independent analysis, and our experience and expertise. This Report does not and is not intended to provide legal advice. Although the report considers various legal matters, our analysis, findings and recommendations are not intended to provide legal interpretations, legal conclusions or legal advice. For that reason, action upon such matters should not be taken without obtaining legal advice addressing the appropriate statutory or regulatory interpretation and legal findings regarding such matters. Finally, our observations are necessarily based only on the information we considered as of and during the period we performed our review.