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UNIVERSITY OF MAINE SYSTEM

DEFINED BENEFIT PENSION FUND – ANNUAL REPORT

YEAR ENDED JUNE 30, 2011

Additional copies are available at <http://www.maine.edu/system/oft/PensionFund.php> or by contacting:

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Defined Benefit Pension Fund – Annual Report

University of Maine System Year Ended June 30, 2011

The University of Maine System (UMS) Defined Benefit Pension Plan (Pension Plan) is a closed plan, maintained for eligible employees who chose not to join the Defined Contribution Plan established for hourly employees on July 1, 1998. This plan covers a shrinking group of active employees, vested terminated employees, and pensioners.¹

Funded Status of the Pension Plan

The Defined Benefit Pension Plan assets are invested in a separate fund (Pension Fund or the Fund) with assets totaling \$45.4 million at June 30, 2011 compared to \$42.1 million at June 30, 2010. UMS obtains an actuarial valuation once every two years. The most recent valuation, completed as of July 1, 2011, showed an Unfunded Actuarial Accrued Liability (UAAL) of \$1.6 million and a funded status of 97%. This compares with a \$2.9 million UAAL on July 1, 2009 and a funded status of 94%.

Oversight and Management

Portfolio and investment management is an ongoing process with the following parties meeting quarterly to provide oversight of Pension Plan assets:

- Board of Trustees Investment Committee
- Investment Consultant – New England Pension Consultants (NEPC) – Cambridge, MA
- Rebecca Wyke, Vice Chancellor for Finance and Administration and Treasurer, UMS
- Tracy Elliott, Director of Finance and Controller, UMS

Governing Guidelines

Formal guidelines, established by the Investment Committee, govern the Pension Fund investment process. These guidelines, last updated August 1, 2011, may be found at <http://www.maine.edu/system/oft/InvestmentGuidelines.php>. They include:

- Total risk and return objectives
- Statement of goals and objectives
- Investment guidelines including
 - Asset allocation with target percentages, permissible ranges, and evaluation benchmarks, and
 - Permitted and excluded investments
- Investment manager performance standards and evaluation
- Responsibilities of all parties
- Conflict of interest statement

¹ For a more detailed history, description and actuarial status of this Pension Plan, see the University of Maine System Annual Financial Report for the Year Ended June 30, 2010, note #13 on Pension Plans which starts on page 49. The financial statements may be viewed at <http://www.maine.edu/pdf/annrpt10.pdf>

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These guidelines currently target a long-term return objective of 7.25% with low to moderate risk. This rate represents a reduction from the 8.0% return objective used during the last valuation. The 7.25% reflects the lower market return environment. Factors informing this view include bond yields that are the lowest in 50 years, stock fundamentals that do not appear likely to support high risk premiums over bonds, and muted economic growth expectations due to unemployment and governmental debt overhang concerns.

Fiscal Year 2011 Performance

The market continued to appreciate during fiscal year 2011 (FY11) allowing the Pension Fund to far exceed its goals and objectives. Nonetheless, the economic recovery going forward remains weak with continued high unemployment, high governmental debt levels, general market uncertainty and volatility, and a recovery largely based on governmental actions. As a result, forward-looking expected returns have declined.

The Pension Fund experienced a return of 21.2% [20.5% net of fees] in FY11, placing the Fund in the 33rd percentile (i.e., exceeding 67%) of the total fund universe tracked by the UMS's investment consultant. Performance is a function of market appreciation, asset allocation and the investment managers utilized. The Fund's managers during the fiscal year added 150 basis points of value, net of fees. Importantly, at 21.2%, the Fund did exceed the 7.25% discount rate used in the Pension Plan's July 1, 2011 actuarial valuation. On June 30, 2011, the Fund totaled \$45.4 million, increasing \$3.3 million over the prior year-end balance as detailed below under the section "Pension Fund Inflows and Outflows".

The Fund's 5-year annualized return was 4.4% [3.8% net of fees] ranking the Fund in the 65th percentile of the total fund universe (meaning 64% of other funds in the universe performed better) while the risk taken by the UMS Pension Fund was equal to other funds in the universe. The UMS 4.4% return compares to the S&P 500 return of 2.9% and the Barclays Capital Aggregate Bond Index return of 6.5% over the same 5 year period.

The Fund is well diversified among a number of asset classes with allocations to eleven investment managers at fiscal year-end.

Changes in Investment Managers and Holdings

Hedge Fund Manager

At its June 1, 2010 meeting, the Investment Committee agreed to restructure the hedge fund category by conducting a search for a new manager and terminating Fidelity Market Neutral. The Investment Committee interviewed firms in December 2010 and engaged Blenheim Global Markets Fund Ltd to manage a 3% target allocation in the Pension Fund.

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Plan Participants

The Defined Benefit Pension Plan is closed to new participants. Eligible employees who were hired before July 1, 1998 and age 50 or older on June 30, 1998 could elect to roll over their accrued defined benefit to the Defined Contribution Program or remain in the Defined Benefit Pension Plan. Hourly employees hired July 1, 1998 or later participate in the Defined Contribution Program.

Regarding the Defined Benefit Pension Plan, an actuarial valuation is performed every two years. Participant information as of the last two valuations is shown here:

	<u>July 1, 2009</u>	<u>July 1, 2011</u>
Participating Employees ²	106	48
Retirees and Beneficiaries	871	895
Deferred Vested Participants ³	<u>404</u>	<u>381</u>
Total Participants	<u>1,381</u>	<u>1,324</u>

Pension Fund Inflows and Outflows

	(\$ in Thousands)	
	<u>FY10</u>	<u>FY11</u>
Beginning Market Value – July 1	<u>\$42,359</u>	<u>\$42,148</u>
Net External Outflows (e.g., benefit payments, expenses)	(\$4,775)	(\$4,935)
Interest and Dividend Income	761	912
Net Gain or (Loss) on Investments	<u>3,803</u>	<u>7,264</u>
Net Activity for the Fiscal Year	<u>(\$211)</u>	<u>\$3,241</u>
Ending Market Value – June 30	<u>\$42,148</u>	<u>\$45,389</u>

Returns, Historical Growth, and Allocation

Attachment I reports the total returns for the Pension Fund on a net of fees basis and the year end market value for the past 5 years, as well as the asset allocation on June 30, 2010 and 2011.

² Shrinking population of those employees who were over age 50 on July 1, 1998 and elected to stay in the Pension Plan. Participating employees includes 19 participants accruing benefits on long-term disability on 7/1/2011 and 29 participants on 7/1/2009.

³ Those who have terminated employment from UMS and are vested but not currently drawing a benefit.

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Market Values, Asset Allocations, and Total Returns
June 30, 2011

	June 30, 2010		June 30, 2011	
	Market Value	% Allocation	Market Value	% Allocation
Domestic Equities	\$13,860	33%	\$14,852	33%
International Equities	5,060	12%	5,893	13%
Fixed Income	7,064	16%	7,581	16%
Market Neutral	1,667	4%	0	0%
Global Asset Allocation	6,646	16%	6,958	15%
Hedge Funds	5,803	14%	7,631	17%
Core Real Estate	2,048	5%	2,474	6%
Total	\$42,148	100%	\$45,389	100%

Total returns (net of fees) and the market value of the Pension Fund for the five years ended June 30, 2011 are shown here:

