Shaping Our Future:
Ensuring Performance, Transparency and Accountability

Operations Summary
Fiscal Year Ended June 30, 2010

California Public Employees’ Retirement System
A Component Unit of the State of California

INVESTMENT RATE OF RETURN
13.3%

NET ASSET INCREASE
12.7%

$201.6 BILLION – NET ASSETS
The California Public Employees' Retirement System (CalPERS) is the nation's largest public pension fund with net assets of approximately $201.6 billion as of June 30, 2010.

Headquartered in Sacramento, CalPERS provides retirement and health benefit services to more than 1.6 million members and 3,033 school and public employers. The System also operates eight Regional Offices located in Fresno, Glendale, Orange, Sacramento, San Diego, San Bernardino, San Jose, and Walnut Creek.

Led by a 13-member Board of Administration, consisting of member-elected, appointed, and ex officio members, CalPERS membership consists of 1,116,044 active and inactive members and 513,623\(^1\) retirees, beneficiaries, and survivors from State, school and public agencies.

Established by legislation in 1931, the System became operational in 1932 for the purpose of providing a secure retirement to State employees who dedicate their careers to public service.

In 1939, new legislation allowed public agency and classified school employees to join the System for retirement benefits. CalPERS began administering health benefits for State employees in 1962, and five years later, public agencies joined the Health Program on a contract basis.

A defined benefit retirement plan, CalPERS provides benefits based on a member's years of service, age, and highest compensation. In addition, benefits are provided for disability and death.

Today CalPERS offers additional programs, including a deferred compensation retirement savings plan, member education services, and an employer trust for post-retirement benefits. Learn more at our website at [www.calpers.ca.gov](http://www.calpers.ca.gov).

\(^1\) This figure includes those retirees, beneficiaries and survivors who receive either a monthly allowance or a one-time-only payment. For fiscal reporting purposes, the *Comprehensive Annual Financial Report*, in most instances, includes only those who receive a monthly allowance.
# Operations Summary
Fiscal Year Ended June 30, 2010

Available online at www.calpers.ca.gov

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I am honored to serve as president of the CalPERS Board of Administration, and I am pleased to present the CalPERS Operations Summary and Comprehensive Annual Financial Report describing our accomplishments for the fiscal year ended June 30, 2010.

In elections held in the Fall 2010, George Diehr, Priya Mathur, and I were re-elected. Board Member Kurato Shimada left the Board in August. We will be holding a special election to fill his vacant seat in May 2011, and the newly elected official will serve out the remainder of the term, which runs through January 15, 2014.

The business environment in which we operate is undergoing broad changes at both the State and national level. Those changes are providing us the opportunity to shape the future of CalPERS by exploring how we can respond in ways that reaffirm our commitment to meeting our fiduciary responsibility of retirement and health security.

In January and February 2010, we held two California Retirement Dialogue events as government pensions became a significant public policy issue. The events—attended by more than 465 interested individuals—provided an in-depth exploration of pension issues facing State and local government members and retirees. We also hosted webcasts to further members’ and stakeholders’ knowledge on topics, including investments and the financing of pensions.
As reported in our Comprehensive Annual Financial Report, the total fund rate of return was 13.3 percent for the fiscal year ending June 30, 2010. This first positive return in three years gives us reason for cautious optimism that the worst of the recent financial crisis is behind us. All of CalPERS asset classes, except real estate, showed positive annual returns, led by global fixed income, which earned a 20.3 percent rate of return. Over the past 20 years, we have earned an 8.1 percent average annual rate of return, which is in line with our average long-term assumed return rate of 7.75 percent. At the end of the fiscal year, our net assets stood at $201.6 billion.

The total fund rate of return was 13.3 percent for the fiscal year ending June 30, 2010. This first positive return in three years gives us reason for cautious optimism that the worst of the recent financial crisis is behind us.

In light of the recent financial market turmoil, we continued to take a fresh look at our asset allocation. In conducting this review, we are being as open and transparent as possible, challenging old assumptions and hearing opposing views. We examined assessments about the future of capital markets, and took a hard look at our asset liability management process and methodology. We are also engaging in a comprehensive analysis of our actuarial assumptions to ensure our long-term benefits.

At the end of the last fiscal year, we launched an effort to better align our interests with those of our investment partners. That effort gained momentum this year, as we successfully negotiated with investment partners to obtain lower fees; achieved a greater degree of transparency and timeliness in the reporting of holdings and transactions; and created an ability to extract CalPERS capital from funds.

The role of placement agents in the investment industry continued to receive considerable attention during the year. In May 2009, we established internal policies regarding the use of placement agents. This year, we adopted regulations setting new standards and policies regarding the use of placement agents. We also sponsored successful State legislation that became law. It requires placement agents to register as lobbyists and prohibits them from receiving compensation contingent on capital allocated from CalPERS and CalSTRS.

Our organization is committed to promoting diversity among our staff, through our investments, and in the boardrooms of corporate America. Early in the fiscal year, CalPERS and CalSTRS held a Diversity on Corporate Boards conference to demonstrate how boards composed of individuals of different backgrounds and experiences make better decisions. We also joined with CalSTRS to catalyze efforts to build a Diverse Director Database of potential board candidates who have the creativity, knowledge, and ability to make a difference for shareowners.

In the arena of health benefits, the 2011 health benefits package increases overall premiums by an average of 9.1 percent. These are the best rates we could negotiate in the current market, and other employer purchasers are forecasting similar increases. As the second largest purchaser of health care in the nation, CalPERS remains committed to promoting cost containment, quality of care, cost transparency, and innovation in wellness, prevention, and disease management.

The enactment of federal health care legislation was a historic step for our nation. The legislation provides for genuine cost containment and puts people before profits. We look forward to working with the federal government, our health care partners, and our members to help realize the full potential of this landmark legislation.

We also continued to enhance and strengthen the customer service we provide our members and employers through enhanced education workshops, online services
and forums to promote greater understanding of the benefits of CalPERS. We remain committed to offering innovative programs and solutions that are in the best interests of our organization, our members, and our employers.

On behalf of the entire CalPERS Board, I want to thank all our employees for the dedication they bring to the job every day. Their hard work is instrumental in enabling us to meet our obligations.

As we respond to the environment in which we operate, we will do so with one commitment at the forefront of all our decisions — to continue to safeguard the retirement and health security of our members — and secondarily, to manage employer contributions.

CalPERS faced the challenges of the year, responding aggressively to calls for greater accountability and transparency in our operations. We will continue to pursue both internal and market reforms to ensure all our stakeholders that our decision-making processes are open and ethical. As we respond to the environment in which we operate, we will do so with one commitment at the forefront of all our decisions — to continue to safeguard the retirement and health security of our members — and secondarily, to manage employer contributions.

Sincerely,
Rob Feckner, President

CalPERS Board of Administration
Board of Administration

Rob Feckner, President
Employee Member (elected by school members)
Glazing Specialist, Napa Valley Unified School District
Term Ends: January 15, 2015

George Diehr, Vice President
Employee Member (elected by State members)
Professor, CSU San Mateo
Term Ends: January 15, 2015

John Chiang
State Controller
Ex Officio Member

Patricia Clarey
State Personnel Board Member (designated by the State Personnel Board)
Term Ends: Serves at the pleasure of the SPB

Dan Dunmoyer
Official of Life Insurer¹
Senior Vice President, Legislative and Regulatory Affairs
Farmers Insurance Groups of Companies and Zurich Financial Services
Term Ends: January 15, 2013

Debbie Endsley
Director, Department of Personnel Administration
Ex Officio Member

JJ Jelincic
Employee Member (elected by all members)
Investment Officer III, CalPERS
Term Ends: January 15, 2014

Henry Jones
Retired Member (elected by retirees)
Retired Chief Financial Officer, Los Angeles Unified School District
Term Ends: January 15, 2012

Bill Lockyer
State Treasurer
Ex Officio Member

Priya Mathur
Employee Member (elected by public agency members)
Economist, Bay Area Rapid Transit
Term Ends: January 15, 2015

Louis F. Moret
Public Representative²
Term Ends: January 15, 2012

Tony Oliveira
Elected Official of Local Government¹
Kings County Supervisor
Term Ends: January 15, 2011

Vacant
(Kurato Shimada through August 2010)
Employee Member (elected by all members)
Retired, Supervisor of Operations, Oak Grove School District
Term Ends: January 15, 2014

¹ Governor appointee
² Appointed jointly by the Speaker of the Assembly and the Senate Rules Committee
BOARD OF ADMINISTRATION  (as of December 2010)

From left to right: Bill Lockyer, Debbie Endsley, Henry Jones, Dan Dunmoyer, Patricia Clarey, George Diehr, Rob Feckner, Louis F. Moret, JJ Jelincic, Priya Mathur, John Chiang, Tony Oliveira
In addition to their regular duties, Board Members also serve on permanent and ad hoc committees to review specific programs, projects, or issues and make recommendations to the Board.

**PERFORMANCE & COMPENSATION**
This committee studies and evaluates compensation mechanisms and criteria, develops policies and procedures, and makes recommendations to the Board concerning compensation of key personnel.

*Patricia Clarey, Chair*
*Dan Dunmoyer, Vice Chair*
*George Diehr*
*Debbie Endsley*
*Bill Lockyer*
*Louis F. Moret*
*Tony Oliveira*

**FINANCE**
This committee provides financial oversight on all budget matters, evaluates funding alternatives, oversees preparation and recommends approval of the CalPERS budget, and oversees the CalPERS annual and periodic audits by both internal and external audit units.

*Henry Jones, Chair*
*Louis F. Moret, Vice Chair*
*John Chiang*
*JJ Jelincic*
*Bill Lockyer*
*Tony Oliveira*

**BENEFITS & PROGRAM ADMINISTRATION**
This committee reviews all matters related to benefit program structure, actuarial studies and rate setting, retirement program policy, and administrative issues.

*Vacant, Chair*
*Rob Feckner, Vice Chair*
*John Chiang*
*Patricia Clarey*
*George Diehr*
*Debbie Endsley*
*Henry Jones*
*Priya Mathur*
*Tony Oliveira*

**HEALTH BENEFITS**
This committee oversees the administration of the Public Employees’ Medical & Hospital Care Act program and the Public Employees’ Long-Term Care Act program.

*Priya Mathur, Chair*
*Tony Oliveira, Vice Chair*
*John Chiang*
*George Diehr*
*Debbie Endsley*
*Rob Feckner*
*JJ Jelincic*
*Henry Jones*
*Bill Lockyer*
Board Committees

AD HOC BOARD GOVERNANCE COMMITTEE
This committee reviews the Board’s internal governance procedures and recommends to the Board any changes or additions to existing policies.

Rob Feckner, Chair
George Diehr, Vice Chair
Henry Jones
Priya Mathur
Louis F. Moret
Tony Oliveira

AD HOC RISK MANAGEMENT COMMITTEE
This committee reviews and enhances the framework for system-wide risk of the pension fund’s governance and operations, including its primary business of investments, health care, and retirement. The committee is comprised of the Board President and the current Chairs of all other Board committees.

Tony Oliveira, Chair
Henry Jones, Vice Chair
George Diehr
Rob Feckner
Priya Mathur
Louis F. Moret

INVESTMENT
This committee reviews investment transactions, the investment performance of both internal and external managers, and establishes investment policy and strategy.

George Diehr, Chair
Tony Oliveira, Vice Chair
John Chiang
Patricia Clarey
Dan Dunmoyer
Debbie Endsley
Rob Feckner
JJ Jelincic
Henry Jones
Bill Lockyer
Priya Mathur
Louis F. Moret

INVESTMENT POLICY SUBCOMMITTEE
This subcommittee conducts an inventory of all existing investment policies, procedures, and guidelines for review by the Investment Committee and reviews and recommends revisions to these on a priority basis. It is also charged with developing a manual of policies, procedures, and guidelines, and a process for periodic revisions.

Louis F. Moret, Chair
JJ Jelincic, Vice Chair
Patricia Clarey
George Diehr
Priya Mathur
Executive Staff

Anne Stausboll
Chief Executive Officer

Stephen W. Kessler
Deputy Executive Officer, Operations

(Dale Jablonsky through June 2010)

Russell Fong
Assistant Executive Officer, Interim Administrative Services

(Doug McKeever, Interim, through November 2010)

Patricia A. Macht
Director, External Affairs

Larry Jensen
Chief Risk Officer, Interim Enterprise Risk Management

(Kathleen Hamilton through January 2010)

Janine Guillot
Chief Operating Investment Officer, Investment Operations

(Ken Marzion, Interim, through January 2010)

Peter H. Mixon
General Counsel

Alan W. Milligan
Chief Actuary

(Ron Seeling through March 2010)

Dale Jablonsky
Assistant Executive Officer, Information Technology Services

(Teri Bennett through June 2010)

Russell Fong
Assistant Executive Officer, Interim Administrative Services

(Larry Jensen through September 2010)

Donna Lum
Assistant Executive Officer, Member & Benefit Services

Kathleen Billingsley
Assistant Executive Officer, Health Benefits

(Doug McKeever, Interim, through November 2010)

Sheri Hofer
Privacy and Security Officer, Enterprise Privacy & Protection

Lori McGartland
Division Chief, Employer Services
EXECUTIVE STAFF (as of December 2010)

From left to right: Donna Lum, Alan W. Milligan, Dale Jablonsky, Sheri Hofer, Peter H. Mixon, Joseph A. Dear, Ann Boynton, Anne Stausboll, Stephen W. Kessler, Patricia K. Macht, Larry Jensen, Janine Guillot, Kathleen Billingsley, Lori McGartland, Russell Fong
## Division Chiefs, Project Managers, and Senior Investment Officers

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<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Department</th>
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</thead>
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<tr>
<td>Matthew Flynn</td>
<td>Division Chief, Operations, Performance &amp; Technology</td>
<td></td>
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<tr>
<td>Holly Fong</td>
<td>Division Chief, Office of Employer &amp; Member Health Services</td>
<td></td>
</tr>
<tr>
<td>Curtis Ishii</td>
<td>Senior Investment Officer, Global Fixed Income</td>
<td></td>
</tr>
<tr>
<td>Geraldine Jimenez</td>
<td>Division Chief, Affiliate Investment Programs</td>
<td></td>
</tr>
<tr>
<td>Nancy Johnson</td>
<td>Division Chief, Technology Services &amp; Support</td>
<td></td>
</tr>
<tr>
<td>Sherry Johnstone</td>
<td>Chief Compliance Officer, Office of Enterprise Compliance</td>
<td></td>
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<tr>
<td>Margaret Junker</td>
<td>Chief Auditor, Office of Audit Services</td>
<td></td>
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<tr>
<td>Ron Kraft</td>
<td>Division Chief, Customer Service &amp; Education</td>
<td></td>
</tr>
<tr>
<td>David Lamoureax</td>
<td>Deputy Chief Actuary, Actuarial Office</td>
<td></td>
</tr>
<tr>
<td>Farouki Majeed</td>
<td>Senior Investment Officer, Asset Allocation &amp; Risk Management</td>
<td></td>
</tr>
<tr>
<td>Kimberly A. Malm</td>
<td>Division Chief, Operations Support Services</td>
<td></td>
</tr>
<tr>
<td>Doug McKeever</td>
<td>Division Chief, Office of Health Policy &amp; Program Support</td>
<td>(Ellen Badley through April 2010)</td>
</tr>
<tr>
<td>Kami Niebank</td>
<td>Division Chief, Policy &amp; Business Support Investment Office</td>
<td></td>
</tr>
<tr>
<td>Ken Nitschke</td>
<td>Division Chief, Office of Policy &amp; Program Development</td>
<td></td>
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<tr>
<td>Renee Ostrander</td>
<td>Division Chief, Information Technology Administration</td>
<td></td>
</tr>
<tr>
<td>Brad Pacheco</td>
<td>Division Chief, Office of Public Affairs</td>
<td></td>
</tr>
<tr>
<td>Lindy E. Plaza</td>
<td>Diversity Officer of Internal Operations, Diversity Outreach Program</td>
<td></td>
</tr>
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**Division Chiefs, Project Managers, and Senior Investment Officers**
Nancy Quinlan  
Division Chief,  
Strategic Management Services

Gina Ratto  
Deputy General Counsel,  
Legal Office

Karen Ruiz  
Project Manager,  
Pension System Resumption  
Project  
(Terry Bridges through December 2009)

John Saxon  
Division Chief,  
Innovation & Implementation  
Services

Anthony Suine  
Business Deputy Project Manager,  
Pension System Resumption  
Project

Darryl Watson  
Division Chief,  
Member Services

Michael A. Willihnganz  
Division Chief,  
Human Resources  
(Chris O’Brien through April 2010)

Vacant  
Senior Investment Officer,  
Alternative Investments  
Management  
(Leon Shahinian through August 2010)

Regional Office Managers

Mary Aberg  
Walnut Creek

Christine Campana  
Sacramento

June Copple  
San Bernardino

Laura Duran  
Orange

Edith Mercer  
Glendale

Elwin Nash  
San Jose

Evelyn Perez  
Fresno

Betty White  
San Diego
### Financial Highlights

#### Public Employees' Retirement Fund

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<th>2010</th>
<th>2009</th>
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<tr>
<td><strong>Cash &amp; Cash Equivalent</strong></td>
<td>$660,374</td>
<td>$574,518</td>
</tr>
<tr>
<td><strong>Total Receivables</strong></td>
<td>2,255,272</td>
<td>3,316,502</td>
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<tr>
<td><strong>Total Investments at Fair Value</strong></td>
<td>203,523,909</td>
<td>183,543,809</td>
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<tr>
<td><strong>Securities Lending Collateral</strong></td>
<td>17,047,678</td>
<td>24,347,602</td>
</tr>
<tr>
<td><strong>Capital Assets &amp; Others</strong></td>
<td>677,715</td>
<td>434,038</td>
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<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td>$224,164,948</td>
<td>$212,216,469</td>
</tr>
<tr>
<td><strong>Retirement Benefits in Process of Payment, Investment Settlement &amp; Other</strong></td>
<td>$4,970,727</td>
<td>$8,310,894</td>
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<tr>
<td><strong>Securities Lending Obligations</strong></td>
<td>17,578,147</td>
<td>25,005,692</td>
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<tr>
<td><strong>TOTAL LIABILITIES</strong></td>
<td>$22,548,874</td>
<td>$33,316,586</td>
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<tr>
<td><strong>TOTAL NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</strong></td>
<td>$201,616,074</td>
<td>$178,899,883</td>
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#### Additions & Deductions

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<td><strong>ADDITIONS</strong></td>
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<td></td>
</tr>
<tr>
<td>Member Contributions</td>
<td>$3,378,867</td>
<td>$3,882,355</td>
</tr>
<tr>
<td>Employer Contributions</td>
<td>6,955,049</td>
<td>6,912,376</td>
</tr>
<tr>
<td>Net Investment (Loss) Income</td>
<td>25,567,295</td>
<td>(57,367,054)</td>
</tr>
<tr>
<td>Other</td>
<td>10,234</td>
<td>3,155</td>
</tr>
<tr>
<td><strong>TOTAL ADDITIONS</strong></td>
<td>$35,911,445</td>
<td>($46,569,168)</td>
</tr>
<tr>
<td><strong>DEDUCTIONS</strong></td>
<td></td>
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<tr>
<td>Retirement, Death &amp; Survivor Benefits</td>
<td>$12,972,457</td>
<td>$11,831,836</td>
</tr>
<tr>
<td>Refunds</td>
<td>182,387</td>
<td>186,783</td>
</tr>
<tr>
<td>Administrative Costs</td>
<td>278,036</td>
<td>427,809</td>
</tr>
<tr>
<td><strong>TOTAL DEDUCTIONS</strong></td>
<td>$13,432,880</td>
<td>$12,446,428</td>
</tr>
<tr>
<td><strong>(DECREASE) INCREASE IN NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</strong></td>
<td>$22,478,565</td>
<td>($59,015,596)</td>
</tr>
</tbody>
</table>

Complete financial information on all the funds administered by CalPERS can be found in the *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2010.

**Note:**

1 Differences in the amount shown for investment assets in these financial highlights and the investment portfolio amount reported in the Investments Section of this Summary are due to differences in reporting methods. In accordance with Governmental Accounting Standards Board Statement No. 28, the financial statements include securities lending collateral. Net investment receivables/payables are not included here.
In the midst of the worst economic recession since the Great Depression of the 1930s, critics of government pensions became more vocal. They began to question the sustainability of government pension benefits as pension fund assets were decimated by the sharp downturn in the financial markets. Calls for pension reform began to resonate in certain political circles.

The debate over pension reform was often punctuated by false or misleading statements, and selective use of statistics. CalPERS countered the misinformation by establishing the CalPERS Responds website to set the record straight.

Also, in an effort to better educate our stakeholders and the public about how government pension plans work, and to separate fact from fiction, we sponsored two all-day California Retirement Dialogue events, one in Northern California and one in Southern California, which featured the insights and perspectives of pension experts from California and around the country.

SERVING OUR MEMBERS

Despite the challenging economic and political environment, we stayed focused on our mission of providing excellent customer service to our members and employers. We currently administer defined benefit pension plans for more than 1.6 million California public employees, retirees, and their families on behalf of 3,033 public employers.
As of June 30, 2010, CalPERS provided retirement benefits for 1,116,044 active and inactive members and 513,623 retirees, beneficiaries, and survivors. Our membership is roughly divided into thirds between State, local public agency, and public school members.

Our Customer Contact Center and eight regional offices around the State provide outstanding frontline customer service to our members, which proved more challenging when the State mandated three employee furlough days per month. During the 2009-10 fiscal year, our Benefit Services Division processed 32,594 service retirement applications and 3,028 disability retirement applications.

We paid $12.97 billion in retirement, death, and survivor benefits, an increase of $1,140,621,453 over the prior year. One hundred percent of new retirees received their first retirement check within 30 days of retirement. We also processed 23,242 requests for refunds of member contributions that were paid within 30 days.

We handled 640,099 customer calls and 54,421 member-related correspondences during the year, completing 88 percent of the calls at the initial point of contact and 94 percent within 10 business days.

We continued to fine-tune our customer callback management system over the past year. The callback system allows callers on hold to hang up and, without losing their place in line, receive a callback when it is their turn. The system proved extremely beneficial due to reduced call center hours caused by employee furloughs. Call hold time was reduced by over 3.4 million minutes and CalPERS saved more than $127,000 in telephone toll charges.

The CalPERS Education Center, our online member education and training system, continued to grow over the past year. The Education Center offers both online classes and traditional instructor-led classes on topics such as:

<table>
<thead>
<tr>
<th>CalPERS Membership</th>
<th>Five-Year Review</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td></td>
</tr>
<tr>
<td>(a) 1,629,667</td>
<td></td>
</tr>
<tr>
<td>(b) 513,623</td>
<td>(c) 1,116,044</td>
</tr>
<tr>
<td>2009</td>
<td></td>
</tr>
<tr>
<td>(a) 1,626,910</td>
<td></td>
</tr>
<tr>
<td>(b) 492,513</td>
<td>(c) 1,134,397</td>
</tr>
<tr>
<td>2008</td>
<td></td>
</tr>
<tr>
<td>(a) 1,602,385</td>
<td></td>
</tr>
<tr>
<td>(b) 476,252</td>
<td>(c) 1,126,133</td>
</tr>
<tr>
<td>2007</td>
<td></td>
</tr>
<tr>
<td>(a) 1,549,270</td>
<td></td>
</tr>
<tr>
<td>(b) 462,370</td>
<td>(c) 1,086,900</td>
</tr>
<tr>
<td>2006</td>
<td></td>
</tr>
<tr>
<td>(a) 1,497,166</td>
<td></td>
</tr>
<tr>
<td>(b) 448,271</td>
<td>(c) 1,048,895</td>
</tr>
</tbody>
</table>

- (a) Total CalPERS Membership
- (b) Benefit Recipients
- (c) Active & Inactive Members
as understanding CalPERS benefits, planning for a financially secure retirement, and financial planning for retirees. Over the past year, we provided education and training to more than 50,000 members with 5,900 members taking classes online.

To help our members plan for a more secure retirement, we conducted five retirement planning fairs in four key cities in the State. The fairs offer participants more than a dozen information tables staffed by CalPERS and outside experts along with workshops scheduled throughout the day. More than 3,130 CalPERS members attended a retirement fair over the past year.

SERVING OUR EMPLOYERS
Over the past year, we began implementing special actuarial treatment of the unusually large investment losses during the 2008-09 fiscal year. We recognized the deep recession and asset losses as once-in-a-lifetime events that should be treated differently from normal years.

Under the Board-approved plan, CalPERS will phase in the rate impact of the 2008-09 asset decline over three years and amortize those three years over a fixed 30-year period instead of the normal rolling 30-year amortization.

The three-year phase-in began for the State and school employers in the 2010-11 fiscal year while local public agency phase-in begins in the 2011-12 year.

As of June 30, 2010, we administered 3,033 retirement plans for State, local government, public agencies, and school employers. Our Employer Contact Center provides frontline customer service to employers. During the year, we handled more than 125,000 employer calls, completing 91 percent of the calls at the initial point of contact, generating a 95 percent customer satisfaction rate.

In addition, we conducted training workshops for 874 employer representatives at 84 State, school district, and public agency offices. We conducted 26 employer workshops by special request and five workshops for new CalPERS employers.

We also processed more than 280,000 member transactions, and conducted more than 6,400 compensation reviews — an increase of 30 percent over the prior year. We completed 81 public agency contract amendments, completed 128,000 employer inquiries, and processed 50,000 payroll reports. More than 1,900 employers were given online access to their Annual Employer Statements.

Our tenth annual Employer Educational Forum, held in Santa Clara, California, drew more than 550 attendees. Participants chose from more than two dozen workshops on topics ranging from the nuts-and-bolts of administering CalPERS benefit programs, to emerging issues such as new laws and proposed legislation that impact public employers, to a dialogue with our chief actuary. The forum also provided participants with an opportunity to network with their colleagues from around the State, CalPERS staff, and Board Members.

Given the challenging environment, we are working harder than ever with our employers to administer affordable, sustainable benefits for their employees.
The California Employers’ Retiree Benefit Trust (CERBT), administered by CalPERS, is an investment trust available to all California public employers to prefund their future other post-employment benefits (OPEB) obligations. OPEB generally refers to retiree health benefits but can also include other benefits such as dental and vision benefits. The CERBT has proven to be both resilient and adaptable, even during the worst recession since the Great Depression. In a little more than three years of existence, despite the challenging economic environment, the CERBT has grown into the biggest public sector OPEB trust in the nation.

The CERBT’s success is based on:

• The strong commitment of public employers to keep their promises to their retired employees
• The willingness of public employees to collaborate with employers to preserve OPEB for mutual interest
• CalPERS record of excellent long-term investment management
• Uncomplicated, low-cost program administration that delivers high value
• Effective employer and member education about the benefits of prefunding and reporting compliance
• Ongoing efforts to improve the CERBT services

EMPLOYERS MEETING THE CHALLENGE

We know public employers are facing tremendous financial challenges caused by the Great Recession. Public employers have to make tough decisions to balance budgets during a period of declining tax revenues.

Despite these economic challenges, many public employers are responsibly planning for the future by prefunding their OPEB costs. By the end of the 2009-10 fiscal year, 258 California public employers were prefunding their OPEB obligations by contributing more than $674.4 million to the trust fund.
EMPLOYEES MEETING THE CHALLENGE

Public employees have partnered with employers to preserve post-employment benefits. Recently, California Highway Patrol (CHP) members agreed to forego future pay increases in lieu of the State of California prefunding employer OPEB liabilities for CHP members. The State of California turned to the CERBT to manage and invest its OPEB contributions. Other State employee bargaining units are following the CHP’s lead. The Sacramento County Office of Education and its employee groups provide another noteworthy example of collective bargaining through which OPEB is preserved by sharing cost agreement. The formula for a productive collaboration can be found, if the bargaining parties are willing.

CERBT INVESTMENTS

The CERBT receives voluntary contributions from employers and invests the funds in public market securities. The contributions and the investment earnings are held in a trust fund dedicated exclusively to paying for other post-employment benefits promised by employers to their employees.

By June 30, 2010, the CERBT had recovered the losses suffered during the financial market collapse of the preceding two years. Total net assets exceeded total net contributions.

Currently, CERBT staff is developing two additional asset allocation strategies with a distinct investment risk and expected return profiles. We also added more asset classes to reduce investment risk while strengthening expected returns. These strategies will be implemented in fiscal year 2010-11. When the new asset allocation strategies are implemented, employers will be able to better match their OPEB prefunding strategy with their risk-tolerance profile.

<table>
<thead>
<tr>
<th>CERBT Covered Members</th>
<th>Four-Year Review</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Active &amp; Retired Covered Members</strong></td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>187,213</td>
</tr>
<tr>
<td>2009</td>
<td>157,968</td>
</tr>
<tr>
<td>2008</td>
<td>109,416</td>
</tr>
<tr>
<td>2007</td>
<td>727</td>
</tr>
</tbody>
</table>

CERBT Fund Asset Growth Since June 2007 Inception as of June 30, 2010 (Dollars in Millions)
CERBT EMPLOYER SERVICES
In addition to trust fund management, CERBT staff also assist participating employers with financial reporting requirements and actuarial support services.

We provide employers with actuarial assumption models and help them find an OPEB actuary. Every year we provide participating employers with financial disclosures required under governmental OPEB accounting standards. We also provide employers who contract with the CalPERS health benefit plan (sometimes called PEMHCA) a participant demographic data report required for an OPEB actuarial valuation report. The CERBT program has become an important information and technical resource to public employers, actuaries, accountants, and the Governmental Accounting Standards Board (GASB).

We also provide education services by offering workshops and meeting with public employers and public employee organizations to educate them about the benefits of OPEB prefunding and reporting requirements.
1.3 million employees, retirees and family members are covered through the CalPERS health plans.

Providing affordable, sustainable, quality health care for our more than 1.3 million members has been a priority for the CalPERS Health Benefits Program for nearly 50 years. Our Health Benefits Program remains stable in spite of a rocky economy as we continue to focus on containing costs, preserving benefits, and educating our members so they can effectively manage their health care costs and prevent disease.

Market declines of recent years, and the higher costs of today’s health care economy, have had a negative economic impact on the nation and California. Despite those, the CalPERS Board of Administration held 2011 premium rate increases to an average 9.1 percent. The increases were primarily due to the health plans’ anticipated higher costs for hospital, medical and prescription drug use in 2011. The new health care reform laws helped us keep the increases below 10 percent. We applied the expected receipt of funds from the Early Retiree Reinsurance Program (ERRP) to offset 2011 health plan costs. ERRP is a temporary federal program that reimburses employment-based health plans for a portion of the cost of benefits provided to retirees age 55 or older who are not eligible for Medicare. CalPERS had about 100,000 retirees and their families who qualified for this program.
NATIONAL HEALTH CARE REFORM
March 22, 2010 marked the historic passage of the national Patient Protection and Affordable Care Act (Act). As amended by the Health Care and Education Reconciliation Act of 2010, the Act is meant to ensure all Americans have access to quality, affordable health care and significantly reduce health care costs.

CalPERS was a staunch supporter of passage of the health care reform law from its inception as rising health care costs hindered the ability of purchasers, such as the pension fund, to provide this vital benefit to its members. Our priorities for supporting the law were based on our commitment to protecting the interests of our members and employers. Our position on health care reform rested on these essential priorities:

• Making health care more affordable for our members, their employers, and all Americans.
• Reforms should include innovative proposals to constrain costs, increase value, and improve quality and efficiency in the health care system.

Three significant provisions of the Act have near-term impacts on CalPERS employers and members:
• As of January 1, 2011, CalPERS members may now provide health care coverage for their children up to age 26.
• Also, as of January 1, 2011, CalPERS health plans will be prohibited from imposing lifetime limits on the value of benefits provided for participants or beneficiaries.

• The Act provides a temporary program (through 2014) that reimburses employment-based plans for a portion of the cost of benefits provided to retirees age 55 or older who are not eligible for Medicare, and their families. CalPERS estimates it could be reimbursed approximately $200 million from this program.

A provision of the Act with a more long-term impact on CalPERS is the federal requirement that states establish health insurance exchanges by 2014 to facilitate the purchase of insurance by individuals and small businesses. Legislation was signed into law that created California Health Benefit Exchange.

National health care reform efforts also encompass the use of information technology to expand use of electronic health records. Broader use of health information exchanges (HIE) can help improve health care quality, increase efficiency and reduce costs. CalPERS is helping to lead the way for expanded use of electronic HIE in California by working with other public, nonprofit and private organizations to support Cal eConnect, a nonprofit corporation designated by the State to accomplish that goal.

With reform at the federal level, our country is moving toward improving our national health care system. As the measures unfold, we will continue to advocate for additional proposals that are in the best interest of our members. In addition, CalPERS staff will continue to work diligently to implement new aspects of the law as regulations develop and federal guidance is provided.
THE HEALTH CARE MARKET
With health care reform still in its infancy, health care costs continue to take a greater toll on family budgets. According to the Kaiser Family Foundation’s Annual Employer Health Benefits Survey\(^1\), the average annual family contribution for employer-sponsored health coverage in 2010 was $3,997, consuming nearly 8 percent of pre-tax income for a family earning $50,000. Insurance premiums for covered workers rose 9.7 percent in 2010, and employers indicated they increased the cost of the employees’ share of the premiums, reduced the scope of coverage, or increased the amount workers pay for insurance to help cover those increases.

Basic Health Maintenance Organization (HMO) premiums rose 10.6 percent, Basic Preferred Provider Organizations (PPO) by 8.7 percent, and Medicare plans went up 3.4 percent. Rates for the California Association of Highway Patrol (CAHP) were unchanged.

However, the California Correctional Peace Officers Association (CCPOA) Basic plan premium rates increased by 13.4 percent and its Medicare plan premium rates increased 9.9 percent for 2011. The Peace Officers Research Association of California (PORAC) Basic plan premium rates increased 8.9 percent and Medicare plan rates went up 15.2 percent in 2011.

This year we spent more than $5.9 billion providing health care to our members and their families. In an effort to continue providing the best possible care at the lowest possible cost to our members we modified some member benefits and copayments to encourage more efficient use of medical services and products, for example using hospitals with good quality outcomes and lower surgical costs.

CalPERS will evaluate how members respond to the efforts and whether there are improvements in health outcomes and cost moderations.


EXPANDING MEMBER AND EMPLOYER ENGAGEMENT
In developing the 2011 Health Program Open Enrollment material, we continued to enhance the way we inform members about their options. Based on feedback from members and employers, we continued using our easy-to-understand guides to help members select the best plan for their families. We improved the 2011 CalPERS Medicare Enrollment Guide to a smaller, more convenient size that is less costly to produce but does not reduce content.

On the employer side, we continued our recruitment and retention strategies to attract new contracting agencies and retain existing agencies. During 2009-10, we enrolled 17 new public agencies, including six school districts and the Los Angeles Community College District, our largest employer ever. As a result of these activities, our public agency “total covered lives” increased 9 percent to 548,551.

At the end of the fiscal year, we distributed another $15 million in Medicare Retiree Drug Subsidy (RDS) funds to more than 800 eligible contracting local public agencies. This is the third subsidy disbursement we have issued to contract agency employers since the Medicare Part D Program was established in January 2006. Over the past three years, we distributed a total of $45.2 million in RDS funds. Contracting agencies receive RDS funds...
based on a formula that considers each agency’s contribution toward Medicare health care premiums in 2007. CalPERS participates in the Medicare Part D RDS Program for all Medicare health plans except Kaiser Permanente Senior Advantage. (CalPERS does provide the Kaiser Medicare Advantage Prescription Drug Plan for Kaiser Permanente Senior Advantage enrollees.)

City and county agencies welcomed these reimbursements as they struggled to maintain health care benefits for retirees and their beneficiaries.

**PARTNERING TO CONTAIN COSTS AND VALUE**

CalPERS may be the largest organization of its type in the country, but we realize even we cannot effect positive changes in the health care marketplace by ourselves. We do, however, take advantage of our size to leverage the best value for our members’ health care dollars.

This year, we initiated a new contract for our pharmacy benefits manager to support the CalPERS self-funded PPO health plans. The proposals were required to focus on integrating evidence-based design with health improvement initiatives.

Also this year, CalPERS concluded a 12-month pilot program in collaboration with Blue Shield of California, Catholic Healthcare West (CHW) and Hill Physicians that examined ways to improve health care quality, enhance service and reduce costs. The pilot program — available to CalPERS members in Sacramento, Placer and El Dorado counties — created an integrated health care model that aligned incentives among the health plan, hospital system and medical groups. The partners agreed to bear the financial risk should the pilot’s cost reduction goals fall short of expectations.

The pilot program is consistent with provisions under the health care reform laws that encourage wider use of Accountable Care Organizations, which emphasize improving the quality of medical care while lowering costs. These strategies are important to bringing us closer to our goals where doctors and hospitals are paid for improved health outcomes rather than for each service.

CalPERS, Blue Shield of California, CHW, and Hill Physicians are reviewing the results and will make a recommendation on expanding the program to additional counties. The pilot program is in line with our strategic vision to be a leader in providing best-in-class sustainable health benefit options for members and employers. If the results indicated the program was successful, we hope to positively impact health outcomes and costs for more members in the future.
WORKING TO IMPROVE HEALTH OUTCOMES

Long-term management of chronic diseases is one of the biggest health care challenges facing the United States, and a key driver in increasing costs. CalPERS joined Kaiser Permanente, Solano County and California State University at Northridge in a comprehensive pilot workplace program designed to improve the lives of employees who are Kaiser Permanente members and at risk for diabetes. It will also address overall employee wellness. The pilot aims to engage employees at risk for diabetes and work with them to encourage healthy lifestyle choices aimed at preventing the disease.

Aggregated data from Kaiser Permanente indicated diabetes was more common among its CalPERS members than among its California membership as a whole. Type II diabetes, the form that most often strikes adults, can be a chronic and debilitating disease, but it is also preventable with proper screening, intervention strategies, and patient motivation.

Other areas where we are working to improve health outcomes include a pilot program with Anthem Blue Cross and Quest Diagnostics to encourage members to participate in early testing to detect signs of colon cancer, and a pilot with Delta Dental to develop therapeutic intervention opportunities for patients at risk for diabetes.

SELF-FUNDED HEALTH PLANS

Although the Board kept 2010 premium increases as low as it could despite rising health plan costs, we recognize that any premium increase can be a burden during these difficult economic times. To provide relief, the Board approved using $265 million in excess reserves from our self-funded Preferred Provider Organization (PPO) health plans to provide a one-time offset equal to two months of premiums and contributions paid by PPO members and employers during the 2009-10 fiscal year. The excess reserves resulted from PPO members increasing their use of generic drugs and having fewer hospital admissions, both attributed to an ongoing member education campaign.

Active and retired State member participants paid no premiums during September and October 2009, and public agency employee participants had no premium payments in November and December 2009. Participating public agency employers were not billed for two months of PPO premiums.

This one-time offset meant an average $134-a-month in premium savings for 324,000 Basic PPO members for a total savings of more than $43 million. Retirees also benefited, with savings varying depending on the employer benefit level. It freed up nearly $131 million for the State of California and more than $91 million for the 1,140 contracting agency employers.

LONG-TERM CARE PROGRAM

CalPERS continued to manage the not-for-profit, self-funded Long-Term Care (LTC) Program. For enrolled members, the program provides help with basic activities of daily living in the event of an accident, chronic illness, disability, or frailty of old age.

The CalPERS LTC Program is unique in that it is voluntary and funded entirely through premium payments. It is not supported or provided by public employers. The Program has encountered funding challenges, resulting in a deficit in the Program funding reserves. A number of factors converged to contribute to this challenge including a decline in investment returns and greater-than-expected plan usage. To ensure the continued sustainability of the program, the CalPERS Board adopted a one-time premium increase that ranged from 15–22 percent for the LTC policyholders with some policyholders receiving on-going premium increases of 5 percent. The combination of these premium increases significantly improved funding status of the Program.

All policies issued prior to 2005 with either lifetime benefits or inflation coverage incurred a 22 percent increase. All policies in this group with both lifetime benefits and inflation coverage issued prior to 2003 will receive an additional annual increase of 5 percent per year beginning in July 2011. Any policy issued prior to 2005 with only non-lifetime benefits and without inflation coverage, and all policies issued after 2005, will receive a single 15 percent increase.
The CalPERS Fund ended fiscal year 2009-10 up 12.7 percent, a solid recovery from a financial collapse that buried investors large and small in every corner of the globe. That nearly every asset class was boosted by real year-over-year growth added to an increasing sense of optimism that the worst days were behind us. Headwinds remained, to be sure, but the dark financial times of the previous year or two appeared to be gone.

We saw gains across the investment spectrum. Private equity was up 23.9 percent. Global Fixed Income increased 20.4 percent. Total Global Equity rose 14.4 percent, and commodities, infrastructure, forestland and inflation-linked bonds moved up 8.7 percent. Only Real Estate continued to battle hard times, falling 10.8 percent in the fiscal year. It was certainly no surprise that trouble still lingered in the sector whose collapse pulled the world into the worst financial crisis since the Great Depression. But it was nonetheless a painful reminder of the challenges ahead as we continued to restructure our real estate program, writing down property values, reducing leverage and ending relationships with partners who didn’t meet our expectations.

Still, the overall success of our diversified portfolio highlighted one important fact: The 13.3 percent fiscal year return marked the 17th time in the past 27 years that the CalPERS Fund has seen double-digit investment returns. It also meant that we easily surpassed
our 7.75 percent assumed rate of return. Over the course of the fiscal year, the Fund grew by more than $20 billion, to $200.5 billion.

Such growth was hard fought. Over much of the fiscal year, financial markets rose steadily, but trouble in Greece and rippling fear that the turmoil would spread across Europe revealed once again how interlocked the world’s financial systems are. The markets that saw 52-week highs swooned in May and June.

That gave an even greater sense of urgency to the thorough examination of our traditional asset allocation model that we began at the start of 2010. The meltdown of nearly every market around the world and the cascading impact on the CalPERS Fund meant the old theories of asset allocation didn’t hold up. Our portfolio, as widely diversified as it was, didn’t provide us with the level of safety we needed when the crash came. So, as part of the asset allocation review that CalPERS conducts every three years, we began a robust evaluation of why that happened and what kind of changes we might make to better protect us when the next financial firestorm comes.

The year saw us continuing our efforts to restructure the portfolio, aggressively cutting costs and successfully negotiating with several external money managers to better align our interests and reduce the fees we pay them. Our agreement with Apollo Global Management LLC, which manages the largest portion of the CalPERS Alternative Investment Management (AIM) Program, calls for a $125 million reduction over the next five years. Relational Investors LLC and Ares Management LLC agreed to five-year cuts of $30 million and $10 million, respectively.

Despite the continued market volatility and the economy’s uncertain recovery, the fiscal year finished on a high note. In June, Congress finally approved the most important financial reform since the 1930s, and CalPERS role in seeing it through to the end was significant. We pushed continually for more transparency across the financial landscape and worked tirelessly to keep our top priority — proxy access — securely in the legislation. We kept up our efforts deep into the summer as the Securities and Exchange Commission wrote the rules to implement the new proxy access regulations. And when the President signed the Dodd-Frank Wall Street Reform and Consumer Protection Act in July, our hard work was rewarded: CalPERS Chief Investment Officer Joseph A. Dear had a front row seat, next to the chairman of the Federal Reserve at his elbow on the right.
ASSET ALLOCATION/RISK MANAGEMENT

The asset allocation review, which began in the second half of the fiscal year, offered an opportunity to challenge every assumption, including discussions about alternative ways to classify some assets, a complete examination of the wide-ranging views about the future of capital markets and a look at the asset liability management process and methodology. There was general agreement that the five broad CalPERS asset classes — Global Fixed Income, Global Equity, Real Estate, Inflation-Linked Asset Class and AIM (private equity) — did not effectively shield the Fund from the market’s volatility during the downturn.

In March, the CalPERS Board heard a discussion about creating additional categories in which to place assets based on the factors that drive their growth, along with their fundamental characteristics. At a workshop in May, outside consultants and CalPERS Staff assessed the future of capital markets. Their general agreement: equities were unlikely to reach the lofty heights of the past but emerging markets held out the possibility of benchmark-beating returns. The evolving discussions continued throughout the year.

This thorough look at where to invest and what percentage of the Fund should be invested in any one place came right after the CalPERS Board increased target adjustments to private equity and cash. Those were made the previous fiscal year in response to the changes that the financial markets were undergoing at the time. The asset allocation examination this fiscal year was a look ahead, with the Board scheduled to set new targets by the end of the calendar year. The new asset allocation ranges will play the leading role in determining the success of CalPERS investments and the assumed rate of return, the rate necessary to pay future benefits to CalPERS members.

GLOBAL FIXED INCOME

As skittish investors moved in and out of public equities over the past fiscal year, fixed income remained a steady player in the search for risk-adjusted returns. CalPERS Global Fixed Income portfolio finished the fiscal year with a market value of about $46.6 billion, up 20.4 percent. The portfolio’s strength was across the board, but domestic fixed income proved the real star, gaining 21.7 percent. International fixed income increased 7.5 percent for the fiscal year.

The investments represented about 24.5 percent of the Fund’s $200.5 billion fair value as of June 30, 2010.

Over the long term, CalPERS Global Fixed Income portfolio has been a benchmark-beating asset class. The five- and 10-year returns — 6.7 percent and 8.0 percent — are about a half percentage point above their respective benchmarks. This fiscal year’s 20.4 percent return was even more significant, beating the benchmark by 7.9 percentage points.

<table>
<thead>
<tr>
<th>ASSET CLASS</th>
<th>CURRENT ALLOCATION¹</th>
<th>CURRENT YEAR TARGET</th>
<th>PRIOR YEAR TARGET</th>
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</thead>
<tbody>
<tr>
<td>CASH EQUIVALENTS</td>
<td>1.6%</td>
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<td>0.0%</td>
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<tr>
<td>GLOBAL DEBT SECURITIES</td>
<td>24.5%</td>
<td>22.5%</td>
<td>22.0%</td>
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<tr>
<td>GLOBAL EQUITY</td>
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<td>49.0%</td>
<td>56.0%</td>
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<tr>
<td>ALTERNATIVE INVESTMENTS/PRIVATE EQUITY</td>
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<tr>
<td>INFLATION LINKED (ILAC)</td>
<td>2.4%</td>
<td>3.5%</td>
<td>2.0%</td>
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<tr>
<td>TOTAL REAL ESTATE</td>
<td>7.5%</td>
<td>10.0%</td>
<td>10.0%</td>
</tr>
<tr>
<td>TOTAL FUND</td>
<td>100.0%</td>
<td>100.0%</td>
<td>100.0%</td>
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</table>

¹ Target allocation effective January 1, 2010.

² The current allocation percentages differ from investment asset percentages presented in the MD&A and Statement of Net Assets as a result of different methodologies used for categorizing investment assets for investment purposes versus financial statement presentation purposes.
GLOBAL EQUITY

Our global equity investments returned 14.4 percent for the fiscal year, despite the steep drop suffered by equity markets in the final two months following spreading concern over debt levels in Euro zone countries. The revitalized public equity market was testimony to the general stabilization in the financial industry and the increase in market liquidity. And CalPERS ability to capitalize on the recovery was testimony to our commitment to stay calm and fully invested even in the worst of times. As of June 30, 2010, global equity represented about 49.5 percent of the CalPERS Fund, well within its strategic target range of 44 percent to 54 percent.

Though the market free-fall may have ended, the lessons we learned from it are still fresh. We continued our thorough re-evaluation of the portfolio, examining our relationships with external managers and working to cut costs. During the fiscal year, we struck agreements to save $99 million in fees across all asset classes, but the majority of savings—$56 million—came from 10 managers in the hedge fund component of global equity, Risk Managed Absolute Return Strategies (RMARS). We continue to engage external managers about basing fees on long-term performance and obtaining more timely disclosures of information to better assess, measure and manage the risks within the RMARS portfolio.

New rules contained in the Dodd-Frank financial reform bill will bring a large measure of transparency to the little-understood world of derivatives trading. The law shifts the majority of trading to exchanges and clearing-houses that require pricing regularly marked to market. It also requires regulators to establish record-keeping and reporting standards that will allow transactions to be monitored. We firmly believe that exposing trading activity and pricing to the light of day will make the markets more efficient and benefit all investors.

Global Public Markets

<table>
<thead>
<tr>
<th></th>
<th>Domestic</th>
<th>International</th>
<th>Total</th>
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<tr>
<td>Fixed Income</td>
<td>$50.8</td>
<td>$2.5</td>
<td>$53.3</td>
</tr>
<tr>
<td>Equity</td>
<td>43.0</td>
<td>48.9</td>
<td>91.9</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>$93.8</td>
<td>$51.4</td>
<td>$145.2</td>
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</table>

1 Domestic and International Fixed Income and Equity totals reflect data reported in the 2010 Comprehensive Annual Financial Report.

International Equity & Fixed Income Investments

Country Diversification

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<tr>
<th></th>
<th>Domestic</th>
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REAL ESTATE

The Real Estate asset class continued to be challenged but is beginning to see signs of stabilization in the marketplace.

The real estate team focused on numerous initiatives with the goal of strengthening the foundation of the real estate investment program. The team continued restructuring the real estate portfolio with its review of all managers and its restructure of select relationships. The real estate team enhanced its systems and internal controls by further refining the Automated Real Estate Investment System and implementing a procedures manual.

During the year, the team worked with the Investment Office to define a new role for Real Estate in the context of the Total Fund and began development of a new strategic plan. The focus of the new program is shifting from an emphasis on total returns to one that provides diversification from equities and a reliable income orientation. The program also is focusing on lower risk and lower leverage.

By the end of the fiscal year on June 30, 2010, Real Estate, with a market value of $15.15 billion, represented about 7.4 percent of the total CalPERS portfolio.

INFLATION-LINKED ASSET CLASS

On April 1, 2010, the Senior Investment Officer for Real Estate assumed management and oversight of the Investment-Linked Asset Class (ILAC), which invests in commodities, infrastructure, forestland and inflation-linked bonds.

The roadmap for all of 2010 called for additional investments of up to $1.3 billion, with $900 million into ILAC funds and another $400 million in direct investments on a selective basis.

In June, we announced our first direct investment in the infrastructure program — a commitment to buy 12.7 percent of London’s Gatwick Airport for up to $155 million. Gatwick Airport is 28 miles south of London and serves approximately 33 million passengers a year, making it the UK’s second most active airport and one of the busiest in Europe. Direct investments such as this one give us more control and offer the promise of greater returns over the long term.

At the end of the fiscal year, the market value of the still-young program — barely two years old — stood at approximately $5.1 billion, about 2.4 percent of the total CalPERS portfolio.

### Real Estate Investments & Commitments

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<thead>
<tr>
<th>Real Estate Investments &amp; Commitments</th>
<th>Dollars in Millions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CORE REAL ESTATE</strong></td>
<td></td>
</tr>
<tr>
<td>Apartment</td>
<td>$1,111.0</td>
</tr>
<tr>
<td>Industrial</td>
<td>2,036.8</td>
</tr>
<tr>
<td>Office</td>
<td>1,019.1</td>
</tr>
<tr>
<td>Retail</td>
<td>1,966.0</td>
</tr>
<tr>
<td>Core REIT Composite</td>
<td>982.3</td>
</tr>
<tr>
<td><strong>TOTAL CORE REAL ESTATE</strong></td>
<td>$7,115.2</td>
</tr>
<tr>
<td><strong>OPPORTUNISTIC</strong></td>
<td></td>
</tr>
<tr>
<td>Housing</td>
<td>$1,886.2</td>
</tr>
<tr>
<td>Opportunistic–Tactical</td>
<td>4,635.7</td>
</tr>
<tr>
<td>Urban</td>
<td>1,527.1</td>
</tr>
<tr>
<td><strong>TOTAL OPPORTUNISTIC</strong></td>
<td>$8,049.0</td>
</tr>
<tr>
<td><strong>TOTAL REAL ESTATE</strong></td>
<td>$15,164.2¹</td>
</tr>
</tbody>
</table>

¹ Differences between investment values above and the values on the Summary of Investments on page 89 of the Comprehensive Annual Financial Report are due to differences in reporting methods.
ALTERNATIVE INVESTMENT MANAGEMENT
With a 23.9 percent return, the AIM portfolio saw the largest percentage gain of all the CalPERS asset classes. The portfolio’s nearly $29 billion market value represented 14.3 percent of the total CalPERS fund. What’s more, CalPERS closed the fiscal year with about $19 billion in unfunded commitments in the AIM program, meaning that we have the resources to make smart investments into funds seeking assets whose underlying foundations are still strong but whose market values tumbled in the financial turmoil. Over time, investments made on the heels of recessions have proved to be among the most lucrative and successful.

<table>
<thead>
<tr>
<th>AIM Portfolio Diversification by Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>1% Mezzanine Debt</td>
</tr>
<tr>
<td>2% Secondary Interest</td>
</tr>
<tr>
<td>8% Special Situation</td>
</tr>
<tr>
<td>9% Venture Capital</td>
</tr>
<tr>
<td>10% Expansion Capital</td>
</tr>
<tr>
<td>12% Distressed Securities</td>
</tr>
<tr>
<td>58% Corporate Restructuring</td>
</tr>
</tbody>
</table>

CORPORATE GOVERNANCE
It took years of debate, negotiations and dedicated hard work, but CalPERS finally achieved its top corporate governance goal — the right for shareholders to nominate candidates for seats on corporate boards. Known as proxy access, it was part of the Dodd-Frank financial reform act, but its final inclusion wasn’t always a sure thing. Plenty of corporate lobbyists lined up against it, but top CalPERS officials pressed Congressional leaders on the need to hold corporate boards accountable and restore investor confidence in the capital markets. Their efforts proved overwhelmingly successful.

As implemented by the Securities and Exchange Commission, the new rule gives shareholders who own 3 percent of a company’s stock for at least three years the opportunity to propose a candidate for the board of directors. Shareholders will be limited to a total number of nominees not to exceed 25 percent of the board at any given company and cannot nominate candidates with intent to take over the company or control of the board.

As an investor in more than 9,000 public companies, we believe that proxy access is one of the most important tools shareholders have to improve corporate governance, and we see its inclusion in the financial reform package as a victory for shareholders and businesses alike. In the meantime, we’re working with our industry colleagues to build a diverse database of potential board candidates who, should they be nominated and elected, would bring fresh ideas and a new perspective to a company’s operations.

This fiscal year, CalPERS did not publish a Focus List of companies targeted for governance reform, the first time in the list’s 23-year history that one was not publicly produced. The reason: discussions with companies selected for engagement improved their performance and corporate practices. That success also was highlighted in a new Wilshire Associates study showing that CalPERS Focus List process strongly contributed to better financial results for companies previously included on the list. Still, as the fiscal year closed, CalPERS Corporate Governance staff launched a comprehensive review of the Focus List to ensure the process reflected the changes sparked by the recent financial turmoil and the regulatory reforms that followed.
DEFINED CONTRIBUTIONS: SUPPLEMENTAL INCOME PLAN

Employee participation in the three Supplemental Income Plans remained relatively flat during the fiscal year 2009-10. The 457 and Supplemental Contribution plans had more than 29,000 participants, with the 457 Plan closing the fiscal year with assets over $803.0 million. The Supplemental Contribution had 687 participants with a market value of $18.0 million. The third Supplemental Income Plan, the Peace Officers and Firefighters Defined Contribution Plan, had 40,020 participants and assets over $405.6 million. All three plans saw returns close to double digits.

The number of agencies adopting the CalPERS Supplemental Income 457 Plan grew slightly during the first six months of 2010, to 708. The Supplemental Income Plans benefited by negotiating administrative and program fee cuts of $322,306, another example of our continued focus on cost reduction.

CALIFORNIA INVESTMENTS

CalPERS investments in California generate jobs and services and provide a strong financial boost to the State’s economy. We had about $17.7 billion invested and another $2.3 billion committed in California across all asset classes at the end of the fiscal year, including a more than $3 billion investment in California real estate. Taken together, the $20.0 billion in investments and commitments represented about 10.0 percent of the total CalPERS portfolio.

The California Initiative, part of our AIM program, invests in companies in markets historically underserved, looking for opportunities that may have been bypassed by other sources of investment capital and creating jobs for workers who reside in economically disadvantaged areas. Started in 2001, the Initiative’s success is tangible. Despite the economic downturn, the companies support more than 60,000 jobs in the State, while at the same time creating 2,000 jobs nationally. More than half of the California workers live in areas with low and moderate income levels.

INVESTMENT DIVERSITY EFFORTS

Diversity opens the doors to new perspectives and fresh views—in the corporate world and in the financial industry. In the boardroom, we’re looking to match the right person with the right company—someone whose skills and broad experience can bring sharp, new insights to a company’s operations. In fall 2009, CalPERS and CalSTRS organized a workshop to discuss how to find those individuals. The two pension funds are the catalysts behind efforts to build a database

CalPERS Operations Summary, Fiscal Year Ended June 30, 2010

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate</td>
<td>$3.3 billion</td>
</tr>
<tr>
<td>AIM (Private Equity)</td>
<td>$5.4 billion</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>$5.5 billion</td>
</tr>
<tr>
<td>Equities</td>
<td>$5.8 billion</td>
</tr>
</tbody>
</table>

1 Figures presented differ from the California Investments reported in the 2010 Comprehensive Annual Financial Report due to the inclusion of commitment amounts to CalPERS California investments. Commitment amounts represent funds earmarked for particular investment strategies that have not yet been deployed.
of potential board candidates. When it’s eventually launched, we hope to attract potential directors who have the creativity, knowledge and ability to make a difference for shareholders.

During fiscal year 2009-10, we hired a new investment officer for diversity to be a key contact for new and emerging managers throughout the industry, across all types of investments and asset classes. Our goal is to help the financial industry understand the type of emerging manager we’re looking for and the type of investments we’re interested in—and at the same time help potential partners navigate our investment decision-making process.

That also was the goal of a February 2010 workshop cosponsored by CalPERS and CalSTRS. Nearly 100 emerging managers from around the country spent a day at our offices as top investment officials from both systems explained the ins and outs of doing business with the two largest public pension funds in the United States.

ENVIRONMENTAL INVESTMENT INITIATIVES
We believe sustainability is a core business issue for the 21st century. That’s why we have more than $2 billion in environmental investments, including more than $1 billion in our private equity program designed to spur clean technology and green jobs. It’s also why we so firmly supported the Securities and Exchange Commission’s decision in January 2010 to require that a company disclose the risk that climate change presents to its business.

Along with our colleagues in Ceres and its Investor Network on Climate Risk, we repeatedly urged policy-makers to adopt national environmental standards to guide us—and the companies we invest in. Those policies should include the creation of short- and long-term greenhouse gas reduction targets and the establishment of rules setting a market-based price on carbon emissions. Investors and business alike need the certainty and transparency that come with national legislation to make smart, targeted investments in clean energy industries.

Through the CalPERS infrastructure program, we invested this past fiscal year in a solar and wind project in North America and a wastewater recycling facility. Our forestland investments have achieved the Sustained Forestry Initiative Certification and the Forest Steward Council Certification. Our private equity investments in environmental and clean tech companies help keep more than 3,200 Californians employed. With care and due diligence, we believe these environmental commitments are good investments for California and CalPERS.

DISCLOSURE, TRANSPARENCY AND ACCOUNTABILITY
We make investment decisions based solely on their merits. And we want to make sure that our door is wide open to the best investment ideas the marketplace has to offer. That’s why we spearheaded some important initiatives to protect and strengthen the integrity of the investment process during fiscal year 2009-10.

The CalPERS Board of Administration voted to toughen ethics policies that guide governance of the Fund. Among other things, the new guidelines tighten rules regarding the Board’s interaction with CalPERS staff concerning investment proposals and give the Board President authority to discipline fellow members whose actions violate policy.

Early in 2010, the Board cosponsored State Legislation to regulate the role of placement agents, who are sometimes hired by money managers to seek business from investors. The measure required placement agents to register as lobbyists and banned them from receiving compensation based on whether CalPERS invested with their client. Some in the financial industry worked steadily to oppose the bill, but CalPERS officials repeatedly testified that the proposal would in no way restrict the ability of skilled money managers to do business with us. That argument carried the day: The bill won widespread support and was signed into law.

The introduction of the legislation followed our voluntary release of more than 600 placement agent disclosures that we obtained from external investment managers who do business with us. The documents
showed that the vast majority of external money managers did not use a placement agent when they sought CalPERS business. We are the only public pension fund in the country to compile and publicly release such a list.

Still, we steadfastly believe investment professionals don’t need to hire someone to get their proposals before us. So we reach out to money managers in numerous ways, through seminars, workshops and industry events. During the fiscal year, we expanded those efforts by launching a new Web-based tool that enables money managers wherever they are to electronically send their detailed proposals directly to our Investment Office for evaluation.
STRENGTHENING ENTERPRISE-WIDE OPERATIONS

A key priority during the fiscal year has been pursuing our commitment to becoming a “risk intelligent” organization. Throughout the year, we have taken steps to enhance the framework for system-wide risk of our governance and operations, including our primary business of investments, health care, and retirement. A complementary focus has been restoring trust in our organization by strengthening performance, transparency, and accountability across the enterprise.

Assisting with this focus, our Office of Audit Services conducted internal audits and special reviews to increase assurance that our assets are safeguarded, we are promoting operating efficiency, and that we are complying with appropriate laws, rules and policies. The Office of Audit Services also recommended measures to reduce fraud risk. The office assessed our information technology governance practices and assisted in the development of our enterprise risk management, including participation in the ongoing Governance and Risk Management Initiative. The office also increased its onsite reviews of contracting public agencies to ensure accuracy of membership and payroll reporting.

MOVING INTO THE FUTURE WITH THE NEW myCalPERS AND OTHER INFORMATION TECHNOLOGY ENHANCEMENTS

We continued to move forward with the creation of myCalPERS, the Web-based platform that will consolidate 49 standalone “legacy” information systems. The creation

The cost of administering retirement and health benefits for active and retired members in 2009-10 was approximately $171 per individual, a decrease of approximately $93 per individual from the fiscal year 2008-09.
CalPERS is the largest automation and business transformation we have ever undertaken.

Employers will enjoy a higher level of customer service and expanded self-service options. For CalPERS staff, the new system will streamline work processes and facilitate access to comprehensive member and employer data, which will improve our financial and operational integrity.

A group of teams is working collaboratively to develop and implement myCalPERS. The teams are composed of CalPERS staff, various consultants, and our prime contractor for the project, Accenture. Working under the leadership of a single Project Director, the Pension System Resumption (PSR) project teams include Technical Services and Testing (TSAT), Business Services and Testing (BSAT), Enterprise Transition Management (ETM), and the Public Employer Readiness Team (PERT). These teams are leveraging the skills and experience of all resources to ensure staff, employers, and members are prepared to take full advantage of the system when the new myCalPERS capabilities are delivered.

During the 2009-10 fiscal year, the project focused on confirming system design, building and testing system functionality, and preparing for the challenge of converting data from a variety of legacy systems for use in the new environment.

In addition to the activities related to myCalPERS, the Information Technology Services Branch (ITSB) adopted a new organizational design and roadmap that transforms ITSB from a focus on specific technologies and systems to a service-based model that is aligned to support CalPERS business needs. Individual learning plans and “work area”-specific transition plans will be used to bridge the gap between existing and prospective roles, responsibilities, and skill sets.

Working with the Investment Office, ITSB also developed and finalized a joint plan to focus on the unique, rapidly changing, niche technologies commonly offered and utilized in the investment area. Objectives of this strategy include moving toward cloud computing and application service providers.

### Capabilities and Benefits of myCalPERS Currently Under Development

<table>
<thead>
<tr>
<th>MEMBER CAPABILITIES</th>
<th>EMPLOYER CAPABILITIES</th>
<th>SYSTEM IMPROVEMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt; Submit service credit applications</td>
<td>&gt; View contract information</td>
<td>&gt; Provides integrated full view of customer data</td>
</tr>
<tr>
<td>&gt; Generate accurate benefit estimates</td>
<td>&gt; Resolve payroll discrepancies</td>
<td>&gt; Reduces time needed for paper processing</td>
</tr>
<tr>
<td>&gt; Apply for retirement</td>
<td>&gt; Make electronic payments</td>
<td>&gt; Creates single source of financial and pension data</td>
</tr>
<tr>
<td>&gt; View health account summaries</td>
<td>&gt; Track status of requests</td>
<td>&gt; Allows customers self-service access to account information</td>
</tr>
<tr>
<td>&gt; Monitor health enrollment and deduction history</td>
<td>&gt; View billing invoices, reporting, and contribution histories</td>
<td>&gt; Increases integrity of all member and employer data</td>
</tr>
<tr>
<td>&gt; Enroll in a health plan (retirees)</td>
<td>&gt; View employee and retiree health enrollment data</td>
<td>&gt; Reduces time required to prepare for and conduct annual valuations</td>
</tr>
<tr>
<td>&gt; Track status of requests</td>
<td>&gt; Make prior year payroll and contribution adjustments</td>
<td>&gt; Minimizes time spent on routine tasks such as correcting payroll errors and tracking documents</td>
</tr>
<tr>
<td>&gt; Update demographic information</td>
<td>&gt; Allow more agencies participating in the Supplemental Income Plan to use electronic reporting</td>
<td></td>
</tr>
</tbody>
</table>

**MEMBER CAPABILITIES**
- Submit service credit applications
- Generate accurate benefit estimates
- Apply for retirement
- View health account summaries
- Monitor health enrollment and deduction history
- Enroll in a health plan (retirees)
- Track status of requests
- Update demographic information

**EMPLOYER CAPABILITIES**
- View contract information
- Resolve payroll discrepancies
- Make electronic payments
- Track status of requests
- View billing invoices, reporting, and contribution histories
- View employee and retiree health enrollment data
- Make prior year payroll and contribution adjustments
- Allow more agencies participating in the Supplemental Income Plan to use electronic reporting

**SYSTEM IMPROVEMENTS**
- Provides integrated full view of customer data
- Reduces time needed for paper processing
- Creates single source of financial and pension data
- Allows customers self-service access to account information
- Increases integrity of all member and employer data
- Reduces time required to prepare for and conduct annual valuations
- Minimizes time spent on routine tasks such as correcting payroll errors and tracking documents
ENHANCING STAKEHOLDER UNDERSTANDING OF CalPERS

As part of our commitment to being an honest broker of information, we created a new website — CalPERS Responds. The website provides education about important topics related to pension security and financing, investments, and national health care reform. The new website had more than 160,000 hits between its September 2009 launch and the end of the fiscal year, demonstrating the high level of interest in the issues it addresses.

In addition to a “Myths vs. Facts” section, CalPERS Responds includes a resource library, which provides access to narrative reports, supplemental information, and material from webinars and conferences. For those who prefer to obtain their information in a visual format, the website offers a collection of charts and graphs. The website also provides streaming video conversations with CalPERS leaders. To expand the reach of our message, the video conversations are also available via YouTube.

To ensure a consistent message is being communicated to our various audiences and to handle the increased interest in health care reform, pension sustainability, and investment market reform, we reorganized our outward-facing functions. The new External Affairs Branch includes Public Affairs, which handles member information, media relations, and communication material; Governmental Affairs, which addresses federal and State issues; and a new Office of Stakeholder Relations.

The Office of Stakeholder Relations coordinates our relationships with member and employer associations, advocacy groups, and industry professional organizations. The unit will also represent CalPERS in highly visible and influential public forums, ensuring communication of our interests on high-profile, policy-oriented issues. Under this office is our Conference Services unit, which coordinates our annual Educational Forum, our Board of Administration’s biannual offsite meetings, and other conferences and workshops hosted by CalPERS.

ENHANCING ETHICS AND ACCOUNTABILITY

During the year, our Office of Enterprise Compliance (ECOM) established an ethics helpline that allows CalPERS staff and constituents to anonymously report fraud, waste, and illegal conduct. The internal helpline was a temporary measure, as efforts were underway to launch an externally managed 24/7 Ethics Helpline early in the new fiscal year.

ECOM continued to expand the Enterprise Fraud Prevention Program to administer our internal compliance-related complaint process to ensure organizational compliance with applicable laws, regulations, and policies. Investigative procedures were established and some investigations were conducted. The office also participated in the ongoing enterprise-wide Governance/Risk Management Initiative, which was created to explore existing structures and processes to ensure we have a systematic and disciplined approach to managing risk.

DIVERSITY OUTREACH PROGRAM

Diversity and inclusion have long been key priorities for CalPERS. During the year, our Diversity Outreach Program (CDOP) hosted Achieving Diversity and Inclusion Leadership Commitment. The event allowed our leadership to gain valuable knowledge on the importance of diversity and inclusion while giving the group an opportunity to collaborate and explore ways to strengthen and improve these efforts across the enterprise. CDOP continued to work with the Senior Leadership team throughout the year to develop an enterprise-wide strategic plan for diversity and inclusion. The Enterprise Diversity and Inclusion (D&I) Strategic Planning Committee was created to develop an Enterprise Diversity and Inclusion Strategic Plan. In the fall of 2010, a survey of staff was conducted to help build an effective diversity and inclusion strategy for CalPERS.

The Senior Management Working Group on Diversity (Group) continues to advance diversity by supporting the development and implementation of enterprise initiatives and outreach efforts. During the year, the Group sponsored two educational sessions.
First, executive teams and senior leaders participated in an interactive session that addressed understanding the diversity and inclusion business case; leadership’s role in diversity; the framework for an enterprise strategic plan on diversity; and the next steps in the diversity cycle according to industry best practices.

Senior leaders also participated in the educational session Managing Multiple Generations in the Workforce, which was delivered by CDOP and Human Resource’s Workforce Management and Leadership. This session explored CalPERS multigenerational workforce and the impact of generational differences on management.

CalPERS is a longstanding supporter and partner of the Toigo Foundation, an organization created to increase diversity in the financial services industry by awarding scholarships and providing mentors to MBA students from diverse backgrounds who are preparing to enter the profession. Early in the fiscal year, CalPERS hosted “A Day at CalPERS,” which allowed Toigo Fellows and Alumni to explore CalPERS employment opportunities. Participants attended the Investment Committee meeting and workshops hosted by investment office staff. They also had an opportunity to network with the staff and learn about CalPERS employment criteria.

The theme of this year’s annual Cultural Diversity Day was unity. The event helps raise overall awareness, understanding, and appreciation of cultural diversity within CalPERS and our community. Attendees at the event had an opportunity to decorate a paper outline of their hands for the Global Art Project’s Let’s All Join Hands. Paper hands from across the globe were presented in October 2010 at the Sixth International Conference of Museums for Peace in Japan.

**COMMITMENT TO THE ENVIRONMENT**

Our commitment to being environmentally responsible was demonstrated in a number of ways during the year. Energy efficient modifications to our Data Center resulted in actual energy savings of 19.5 percent, or a projected annual savings of approximately 932,000 kilowatts. This energy savings is equal to a reduction in yearly carbon footprint emissions of almost 297 metric tons and an annual savings of approximately $86,000.

In recognition of this achievement, the SMUD Board of Directors presented CalPERS with a rebate check of nearly $80,000. Additional savings were achieved using a technology called “virtualization,” which allows us to run multiple applications on a single machine. Implementing Data Center virtualization significantly reduced both the number of power circuits and the number of cables being used. Since the project was completed, applications run faster and are more reliable and secure.

Our Lincoln Plaza North received a LEED Existing Building gold certification from the U.S. Green Building Council. The LEED (Leadership in Energy and Environmental Design) certification program is a nationally recognized benchmark for the design, construction, and operation of green buildings. It demonstrates our commitment to efficient use of water, energy, and other resources; lower operation and maintenance costs; and minimizing the human footprint on the environment. Our Lincoln Plaza East and West buildings had previously received the LEED gold certification for new buildings.

We were also awarded a Move Green California Award from the Department of General Services for administering exemplary alternative commute programs, and we were certified as a Climate Action Leader by The California Climate Action Registry for commitment to managing Greenhouse Gas inventory.
This past fiscal year, the CalPERS Board of Administration sponsored legislative proposals, adopted legislative positions and supported policy initiatives that served the interest of our members and employers. Using its Legislative Policy Standards as a guide in formulating positions, the Board considered legislation on a variety of fronts.

The Office of Governmental Affairs (GOVA) advocates on behalf of CalPERS members and stakeholders at the direction of the Board to ensure the integrity of the CalPERS trust and advance CalPERS mission in State and federal policy areas.

**STATE LEGISLATIVE UPDATE**

Following is a brief summary of some of the CalPERS related State Legislation enacted during the legislative session.

**Assembly Bill (AB) 1592, Chapter 163 (Buchanan)**

State Employees: Ratification of MOUs

Provides legislative ratification for memoranda of understanding between the administration and three State bargaining units: CDF Firefighters (BU 8); Physicians, Dentists, and Podiatrists (BU 16); and Health and Service Professionals (BU 19).

**AB 1602, Chapter 655 (John A. Perez) California Patient Protection and Affordable Health Choices Act**

Creates the California Health Benefit Exchange (The Exchange); specifies the powers and duties of the board

**BENEFITS PAID**

$12.97 billion in benefits were paid to retirees in fiscal year 2009-10.
governing the Exchange; requires the board to facilitate the purchase of qualified health plans through the Exchange by qualified individuals and qualified small employers by January 1, 2014; creates the California Health Trust Fund as a continuously appropriated fund; imposes various requirements on participating plans and insurers and, commencing January 1, 2014, on nonparticipating plans and insurers, as specified; requires that loans awarded under the bill be made from the California Health Facilities Authority Fund and requires repayment of the loan by a specified date.

AB 1625, Chapter 728 (John A. Perez) State Employees: Ratification of MOUs
Among other things, provides legislative ratification for memoranda of understanding between the administration and nine State bargaining units: 1, 3, 4, 11, 14, 15, 17, 20 and 21.

AB 1651, Chapter 574 (De La Torre) Furloughed School and Safety Employees: Service Credit and Final Compensation
Legislation was enacted in 2009 to guarantee that all State employees who are furloughed will receive the same amount of retirement service credit and final compensation he or she would have received absent the furlough. This bill extends the same treatment to furloughed school employees who are employed by a county office of education, a school district, a school district that is a public agency, or a community college district, as well as local safety members employed by a contracting agency.

AB 1743, Chapter 668 (Hernandez) Placement Agent Registration and Reporting¹
Requires placement agents who do business with CalPERS or California State Teachers’ Retirement System (CalSTRS) to be subject to the same reporting and ethics rules that govern lobbyists under the California Political Reform Act, including bans on campaign contributions and contingent fee arrangements. The bill also requires placement agents who do business with local public retirement systems to register as lobbyists if those jurisdictions have similar lobbyist registration requirements in place. It also requires CalPERS and CalSTRS to report to the Legislature on or before August 1, 2012 on the use of placement agents.

AB 1856, Chapter 197 (Fong) After-Tax Service Credit Purchase Elections
Allows CalPERS members to suspend or cancel after-tax installment payments for service credit purchases on a voluntary basis, without needing to show financial hardship. It also allows CalPERS to cancel service credit purchases that remain delinquent with no response by the member for at least one year.

AB 1873, Chapter 583 (Huffman) Property Assessed Clean Energy (PACE) Bonds
Authorizes the CalPERS Board of Administration and other specified State agencies to purchase bonds issued to finance the installation of distributed generation renewable energy sources or energy or water efficiency improvements through local property assessed clean energy (PACE) programs.

AB 2510, Chapter 600 (Fletcher) Public Employees’ Retirement: Contracting Agencies: Post-Retirement Health Coverage
Allows the City of San Diego to establish a vesting requirement for post-retirement health benefits for employees who are either members of the San Diego Police Officers Association, or unclassified and unrepresented employees of the City of San Diego; and who have at least 10 years of service credit. This would take effect for employees retiring on or after the effective date of the memorandum of understanding authorizing this benefit.

¹ CalPERS sponsored bill 2010
Senate Bill (SB) 846, Chapter 162 (Correa) State Employees: Ratification of MOUs
Ratifies the provisions of the memoranda of understanding (MOU) between the State and the following three State bargaining units: Highway Patrol (BU 5); Craft and Maintenance (BU 12); and Psychiatric Technicians (BU 18).

SB 856, Chapter 719 (Budget and Fiscal Review) State Administration
Among other things, allows the Franchise Tax Board to provide information from their records to facilitate the CalPERS filing of required data pursuant to the federal Early Retiree Reinsurance Program.

SB 867, Chapter 733 (Hollingsworth) Contribution Rates: Reports
Requires CalPERS, when adopting contribution rates, to report to the Legislature alternative data regarding its investment returns, amortization periods, and discount rates using specific analytical guidelines. It also requires the State Treasurer to report to both houses of the Legislature during a publicly noticed floor session on the contents of this report within 30 days of its receipt.

SB 1007, Chapter 633 (Hancock) Board Campaign Contributions Reporting
Requires candidates for the CalPERS and CalSTRS Boards to file campaign reports in generally the same manner and frequency as candidates for other State offices and extends existing campaign contribution limits to them as well. Committees formed or existing primarily to support or oppose those candidates would also be similarly affected. This bill also authorizes the Fair Political Practices Commission (FPPC) to adopt regulations to tailor these reporting requirements to be consistent with the Political Reform Act (PRA).

SB 1088, Chapter 660 (Price) Dependent Health Coverage
Prohibits the limiting age for dependent children covered by health care service plan contracts and individual and group health insurance policies, from being less than 26 years of age, with respect to plan or policy years beginning on or after September 23, 2010, except for certain group contracts and policies for plan or policy years beginning before January 1, 2014, as specified. The bill also requires plans and insurers to provide certain dependents who have lost or been denied coverage an opportunity to enroll, as specified.

SB 1139, Chapter 639 (Correa) CalPERS 2010 Omnibus Bill¹
Makes several minor policy and technical amendments to various sections of the Government Code administered by CalPERS. These include coordinating the timing of the Power Purchasing Protection Allowance with the cost-of-living increase in May each year; extending existing statutory provisions allowing State employees subject to mandatory furloughs to receive their full service credit into the current fiscal year, making clarifying changes to PEMHCA to align it with JRLS II regarding Judges' health benefits after leaving office; authorizing contracting public agencies to provide health coverage to a survivor who is not receiving an allowance, but was otherwise eligible prior to the effective date of the contract; and expanding the types of retirement savings programs the Board may establish to include those with after-tax payments such as Roth 401K.

SB 1271, Chapter 702 (Romero) Conflict of Interest Reporting
Requires a board, agency or commission of a public pension or retirement system to attach an appendix that lists each position for which an individual occupying that position is required to file a statement of economic interests to its conflict of interest code. This information must also be posted on its website.

¹ CalPERS sponsored bill 2010
SBX6 22, Chapter 3 (Hollingsworth) Pension Formulas for New State Employees

Establishes reduced first tier benefit formulas for all State, legislative, judicial, and CSU employees first hired on or after January 15, 2011 and replaces the 12-month highest compensation period used to calculate pension benefits with a 36-month highest compensation period. These changes apply to new State employees whose bargaining units have not already negotiated other first tier benefit formulas or 36-month highest compensation periods, or who first become employed after the bargaining agreements expire.

FEDERAL UPDATE

As the United States’ largest pension fund and second-largest provider of health benefits, CalPERS has a unique perspective on some of the country’s most pressing issues. Given this, the CalPERS Board of Administration is committed to working with governments at all levels to address those subjects in ways that most benefit the fund’s 1.6 million members and the nation as a whole. On national issues, CalPERS defines its goals in Federal Legislative Policy Priorities documents, and in 2010, its federal legislative program achieved an unprecedented level of success.

Like all other providers of health benefits, CalPERS has been frustrated by the inefficiencies of the U.S. system, the quality shortcomings, the absence of even near-universal coverage and, perhaps most of all, the spiraling costs. As a result, health care reform has long been a priority for the pension fund. The push for reform that the Obama administration began in 2009 stretched into 2010, as did CalPERS efforts to shape the legislation and help to get a quality bill passed. After many stops and starts and more than a few declarations that the reform effort was dead, on March 23 President Obama signed into law the most sweeping health care reform bill since Medicare was established nearly a half-century ago.

The reform law, among other things, requires all U.S. residents to have insurance or pay a penalty, provides federal subsidies for the purchase of insurance (contingent on income levels), establishes health care “exchanges” to connect consumers with insurers, prohibits insurance denials based on pre-existing conditions and insurance cancellations based on illnesses, bans lifetime benefit caps, expands Medicaid eligibility, closes the Medicare prescription drug benefit “doughnut hole” and creates multi-state insurance plans offered by private insurers through a program run by the federal Office of Personnel Management. It includes several other CalPERS priorities, including a new long-term care coverage program, an expansion of the use of comparative effectiveness research and strengthening of Medicaid’s financial condition.

CalPERS Board President Rob Feckner called enactment of the reform bill “a historic action for our nation and for all Americans. This legislation represents genuine cost containment and puts people before profits. Most of all, it provides health care coverage for Americans—a moral imperative.”

CalPERS is now working to ensure that regulators implement the bill’s provisions in appropriate ways. The financial crisis of 2008-09 threw the country into a deep recession from which it is still struggling to emerge. Millions of Americans have lost jobs and homes, and investors, including CalPERS and other pension funds, saw their assets drop in value by billions of dollars. Many observers blamed the crisis on financial improprieties and excessive risk-taking; problems that some critics say were abetted by the inadequacy of the U.S. regulatory structure. This led to a push in Congress for financial reform, one that, like the battle over health care reform, extended from 2009 into 2010.

CalPERS took an active role in this effort, advocating for regulations that would protect investors and the public without hurting economic development or discouraging prudent risk-taking. The pension fund was especially active on corporate governance issues. CalPERS is one of the country’s leading investor advocates, and for several years, its top goal has been to get rules enacted that would enable shareholders to place director nominees on corporate proxy ballots. This bit of corporate democracy, CalPERS has argued, is the most fundamental way of ensuring transparency and accountability in corporate boardrooms.
In July, Congress narrowly passed, and President Obama signed, the most significant overhaul of financial regulations since the Great Depression. The main provisions of the bill are intended to end the notion that some firms are too big to fail, establish oversight of entities and activities whose failure could threaten the stability of the nation’s entire financial system, and create a regulator for mortgages, credit cards and other consumer financial products. It also creates a regulatory mechanism for derivatives, something that CalPERS has strongly supported. In fact, the bill’s Senate sponsor, Christopher Dodd, D-Connecticut, quoted CalPERS Chief Investment Officer Joseph Dear on the subject while discussing the legislation on the Senate floor in May.

The measure also included several corporate governance provisions, including one that clarifies the authority of the Securities and Exchange Commission (SEC) to issue rules to enable shareowners to put director nominees on proxy ballots. The SEC had been working on this before the reform bill was introduced, but there was some question about whether the commission could enact such a rule. The bill also achieved another CalPERS priority by guaranteeing the ability of shareowners to cast advisory votes on executive pay packages. In addition, it requires that compensation committees include only independent directors; mandates that companies establish “clawback” procedures for compensation awarded on the basis of inaccurate financial statements; directs the SEC to clarify compensation-related disclosures; and requires federal regulators to issue compensation rules for the firms they regulate. For CalPERS, this was a major victory.

“We have worked for many of these protections for upwards of a decade, especially for independent boards, access to the proxy, and better executive compensation policies,” Feckner said. “This reform goes a long way to plug the gaps that contributed to the recent financial crisis. It’s good for shareowners, good for business and for taxpayers.”

On August 25, the SEC approved rules that ensure that shareowners who own at least three percent of a company and have done so for at least three years can put nominees for up to one-fourth of a company’s directors on the ballot. (Shareowners may combine holdings to meet this threshold.) Dear lauded the SEC vote, calling proxy access “one of the most important tools we have to improve corporate governance in America’s boardrooms. When necessary, long-term investors now have an opportunity to propose knowledgeable individuals for election to a board who can bring fresh ideas and new perspective to a company’s operations.”

As with the new health care law, CalPERS is now working with regulators on the implementation of the financial reform provisions.

CalPERS also worked on several other key federal issues during the year. For example:

• In April, representatives of CalPERS and others in the public pension community met with an IRS official to discuss an initiative from the agency that focuses on public pension plans and ensure that the plans have input into the project.
• CalPERS supported moves to respond to the Supreme Court’s Citizens United ruling—which struck down a long-time ban on political spending by corporations and unions—in a way that protects shareowner rights.
• CalPERS has continued to back responsible action on the climate change issue that would provide greater certainty about the direction of climate and energy regulation, ensure transparent markets, benefit consumers and workers, create jobs and allow the United States to seize new economic opportunities.

In 2011, a new Congress will be seated, and new challenges will emerge. But CalPERS, as always, will take a leading role in advocating for sensible legislation and regulations on health care, investments and other important issues.
The events of the past few years have taught us that managing risk and ensuring accountability across our organization are essential. We have taken many steps to increase transparency, strengthen our ethics and accountability and enhance our internal strength as an organization. During the new fiscal year, we will implement additional measures to strengthen and rebuild our organization with renewed leadership, culture and performance.

Early in the fiscal year, we will begin efforts to shape the future of CalPERS through three enterprise-wide priorities. First, we will reexamine our organization’s structure to ensure effective customer service, risk intelligence, and innovation. This effort will position us to fulfill our mission and strategy in the future, and take full advantage of the tremendous capacity we will have with myCalPERS. Second, we will analyze the three parts of our business strategy: business planning, performance management, and budgeting processes to ensure they are aligned. Finally, we will reevaluate our core values to determine if they are relevant to our changing business culture and the environment in which we operate. During this reevaluation, we will engage our staff in a conversation about whether we have the best core values to shape the future and whether we should add additional values.

The PERF net assets increased from $178.9 billion to $201.6 billion for fiscal year 2009-10.
The new fiscal year will be pivotal for our organization as we prepare for the launch of myCalPERS. Once full testing is complete, myCalPERS will be implemented in several phases. The initial launch will deliver core functionality to CalPERS internal staff and business partners. Subsequent releases will address enhanced member self-service features and additional functionality for staff and employers.

myCalPERS is just one of our priorities. Risk management across our organization will be another. Our new Senior Level Enterprise Risk Management Office will ramp up its operations. The new office will bring together all aspects of risk management, including internal compliance operations, privacy and security, disaster recovery, and business continuity programs. It will also ensure that we ask important questions, challenge our own assumptions, and manage threats that could hamper our ability to deliver the best services to members and employers. We will be hiring a Chief Risk Officer to help take our organization to the highest level of risk management possible.

On the investment front, we will explore changes to our traditional asset allocation approach and revisit our assumed rate of return by evaluating current economic and market conditions as well as forecasts for the future. The question that we face now is whether the historic economic upheaval of the past few years has dramatically altered long-held assumptions about investing in the world’s financial markets. Are investors in for a sustained period of meager or below-average market growth? Or will the traditional business and economic cycles—the ones investors have grown accustomed to over the past couple of decades—return? These are the questions we will address with fearless research, robust debate and sound judgment.

In health care, we will implement key provisions as part of the landmark national health care reform legislation. These include the extension of dependent coverage and the removal of lifetime and annual limits. We will also begin implementing health benefit design changes to conform to the health care reform laws and launch a new strategy to negotiate health care rates.

Finally, we will address the changing health care and pension environments with an eye toward preserving the value of defined benefit plans like CalPERS, minimizing pension costs for employers and ensuring the financial security and health care of our members for years to come.
The 2010 Comprehensive Annual Financial Report (CAFR) and this Operations Summary are available online at www.calpers.ca.gov. For questions, please contact the Office of Public Affairs at (916) 795-3991.