



VEACO GROUP
Corporate Governance Advisors

August 27, 2012

To: Members of the CalPERS Board Governance Committee

From: Veaco Group—Kristina Veaco, Cheryl Sorokin

Re: 2012 Board Self-Assessment Process-Implementation Phase

Action Requested: Review, Prioritize and Approve Action Steps to Implement Refinements to CalPERS Governance Processes

Attached are four overarching recommendations to help refine your governance practices and improve the effectiveness of your board and committees. Each of the four recommendations is followed by specific action steps that we recommend to facilitate implementation of the recommendations. We have also included our suggestions as to whom overall responsibility for carrying out the various recommended steps should be assigned.

The attached umbrella recommendations are, of course, based on what you reported to us during the self assessment process. The action steps for implementation are also based on what you told us, as well as our own experiences as to processes and procedures that have helped boards and board members become more effective.

Background:

In April you commissioned us to conduct a board self assessment process. The various steps of assessment process are outlined on Attachment A should you wish to refresh your memory. In addition to the steps listed, we also recently reported our findings to the senior executives, to the extent applicable to them. We are now at the final phase of the basic assessment process: **Refinement of recommendations and priorities, with management and board leadership.**

In July we reported the results of what you, as board members, told us during the self-assessment. There was a great deal of information and a number of suggestions in that report and we are aware that efforts are already underway to address some of the issues raised. However, in our experience, it is important for boards to prioritize actions, assign specific responsibility for implementation, and systematically review progress, if real change is to occur.

We have created the attached chart to assist you with the process of prioritization and implementation and plan to discuss the attached recommendations with you at the upcoming meeting.

If you would like us to assist directly with implementation, we are prepared to do so.

It has been a pleasure to work with you on this project.

Assessment/Development Phase

- Review of prior CalPERS Board Governance Project work and prior evaluation process
- Board leadership interviews
- Executive management interviews
- Committee Chair interviews
- Interviews with select key stakeholders
- Real time observation of CalPERS governance including board practices and committee meetings, agenda and materials preparation process, communications mechanisms and use of technology, as appropriate
- Development of tailored written questionnaires considering the multiple bases identified in the Board Governance Project as well as issues identified through initial interviews
- Development of oral questions for director self-assessment and peer reviews

Administration of Board and Committee Evaluation Processes Phase

- Distribute questionnaires
- Conduct oral interviews with individual board members
- Compile and analyze results
- Design presentations to be made to CalPERS board, committees and individuals

Summary and Presentation of Findings/Recommendations Phase

- Discussion of overall findings/recommendations with CEO and Board President
- Presentation of overall and specific findings/recommendations to full board and committees in closed session
- Separate oral discussions of any individual evaluation findings with each affected individual
- Refinement of recommendations and priorities, with management and board leadership



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**CalPERS Board of Administration
2012 Board Assessment Process**

Recommendations

**Board Governance Committee
September 11, 2012**

Recommendation 1: Focus agendas and educational efforts on significant issues, reallocate time accordingly

Major Component	Recommended Action Step	Suggested Responsibility
Review (zero-base) agendas that come to board and committees	Understand what matters must come to the board because of : <ul style="list-style-type: none"> • constitutional requirements • statutory/regulatory requirements • case law • other legal requirement • board action in reserving to itself the power to act on such matters 	Senior Execs.
	Review pension fund and other governance literature to determine umbrella categories of substantive matters recommended for board/committee consideration as a matter of sound governance practice and compare to CalPERS agenda setting process	Senior Execs.
	Use governance committee or a small, ad hoc committee of senior executives and board members (Ad Hoc Committee) to work on board/committee agendas, materials and other board process redesign issues	Bd. Pres., CEO
	Prioritize strategic/critical issues for board/committee agendas, and estimate amount of time required	Gov. Comm. and Senior Execs., or Ad Hoc Comm.
	Prioritize areas for educational presentations to be given at board and committees, or otherwise during week of board/committee meetings, and estimate time required	Gov. Comm., Senior Execs. or Ad Hoc Comm.
	Reduce routine operational matters and materials on agendas	CEO
	Tie most board/committee agenda items and materials to one or more of the following broad categories: <ul style="list-style-type: none"> • legally required • reserved or delegated power • strategic/critical issue • education of board members • sound governance practice 	Bd. Pres., Comm. Chrs., CEO

Recommendation 1: Focus agendas and educational efforts on significant issues, reallocate time accordingly

Major Component	Recommended Action Step	Suggested Responsibility
	Create annual calendar of agenda items, categorize each item as indicated above	Senior Execs.
	Revise ongoing agenda setting process after above steps completed, focusing on ways to reduce meetings and reallocate time to strategic/critical issues and board member education as priorities	Senior Execs.
Review written materials that come to board and committees	<p>Review rationale and format for all board/committee materials whether authored internally or externally, redesign as appropriate and provide guidelines. Focus particularly on:</p> <ul style="list-style-type: none"> • whether the matter is ready for board review • level of detail • level of analysis • sufficiency of summary information • how best to highlight important issues and provide context to assist board member understanding of issues 	Senior Execs.
Review substance and form of oral presentations made to the board	<p>Review rationale and format for all oral presentations made to the board/committees, by internal or external presenters, redesign as appropriate and provide guidelines. Focus particularly on whether:</p> <ul style="list-style-type: none"> • an oral presentation is required at all • the matters presented are at the right stage for presentation to the board • the substance of the presentation is linked to strategic and critical issues • whether the level of detail and analysis is appropriate • presentations simply repeat what is stated in written materials • the person making the presentation has not only substantive expertise but the skill to make board-level presentations 	CEO and CIO

Recommendation 1: Focus agendas and educational efforts on significant issues, reallocate time accordingly

Major Component	Recommended Action Step	Suggested Responsibility
Coordination of governance matters under CEO	<p>Designate a “governance professional” or “governance coordinator” under, or ultimately reporting to, CEO to oversee and coordinate governance matters. Role might be incorporated within existing senior manager position or be a new position, but highly recommend that individual selected be someone that is:</p> <ul style="list-style-type: none"> • capable of functioning similarly to a Corporate Secretary in the public company arena • familiar with the organization and the board • familiar with corporate governance matters and trends, preferably a lawyer 	CEO
Develop chart of authority	Develop an easy to read chart of authority so it’s clear what matters require what approval and by whom	Senior Execs.

Recommendation 2: Focus on organizational leadership and internal controls

Major Component	Recommended Action Step	Suggested Responsibility
Continued shaping of leadership reporting structure and the relationship between board and CEO and CIO	<p>Increase the leadership role of the CEO at board meetings</p> <ul style="list-style-type: none"> • Focus the CEO’s reports to the board on the significant operations of CalPERS and on significant issues being considered by board/committees • Use CEO reports and cover letters to guide the board with respect to the nature and relative importance of the top issues to be considered at the board and each committee meeting • Have the CEO introduce staff members as they present, and provide background for those not known to the board • Position the CEO next to the Board President during meetings when possible 	<p>Bd. Pres. and CEO</p> <p>CEO</p> <p>CEO</p> <p>CEO</p> <p>Bd. Pres. and CEO</p>
	<p>Increase the leadership role of the CIO at Investment Committee meetings</p> <ul style="list-style-type: none"> • Use CIO reports and cover letters to guide the investment committee re nature and relative importance of the top issues to be considered at each investment committee meeting • Position the CIO next to the Investment Committee Chair during meetings when possible 	<p>CIO and Chr. of Invest. Comm.</p> <p>CIO</p> <p>CIO and Chr. of Invest. Comm.</p>
	<p>Resolve issues with the delegations of authority to CEO and CIO</p>	<p>CEO, CIO and Legal (written delegation)</p>
	Regular focus on performance and compensation	<p>Regularly include time on board executive session agendas for board members to provide input to the Chair of the Performance and Compensation Committee on performance of the CEO and CIO– tied to performance objectives</p>
<p>Direct the Chair of the Performance and Compensation Committee to give regular feedback to the CEO and CIO throughout the course of the year</p>		<p>Bd. Pres.</p>

Recommendation 2: Focus on organizational leadership and internal controls

Major Component	Recommended Action Step	Suggested Responsibility
Continued strengthening of internal controls and oversight of risk	Ensure establishment of internal controls over significant processes similar to those Sarbanes-Oxley (SOX) requires of public companies	CEO
	Include risk as a strategic/critical issue for review and discussion at board/ committee meetings	Bd. Pres., Chr. of Audit Comm., CEO
	Focus on internal control issues at Audit Committee—particularly in the area of financial controls	Chr. of Audit Comm., CEO
	Review and clarify the respective roles of the Audit Committee and Finance Committee with respect to internal controls, risk and financial reporting	Gov. Comm.

Recommendation 3: Develop a plan for board member education

Major Component	Recommended Action Step	Suggested Responsibility
Systematic and comprehensive focus on board member and overall board and committee education	Designate an “Education Coordinator” under CEO to develop education plans and provide oversight and tracking of educational efforts. Role requires someone <ul style="list-style-type: none"> • familiar with the organization and the board • familiar with corporate governance matters and trends (preferably a lawyer) Consider consolidation with governance professional role because of overlap with governance issues	CEO/Gov. Prof.
	Analyze educational needs for individual directors and board as a whole, based on input from CEO, CIO, Governance Committee and individual board members	Gov. Prof./ Ed. Coord.
	Review and determine best possible options for providing needed education including: <ul style="list-style-type: none"> • external programs—particularly those designed for trustees of pension funds • internal education and workshops • outside experts • specialized education on topics dealt with in committees • education on corporate governance and fiduciary responsibilities 	Gov. Prof./ Ed. Coord.
	Prioritize subject matter training for board members who lack experience in a particular area	Gov. Prof./ Ed. Coord.
	Tailor internally developed education programs for management to board level education, when appropriate	Ed. Coord.
	Schedule regular presentations at the board by outside experts, including those with differing points of view—in the nature of a “speakers series”	CEO and CIO
	Develop a schedule of workshops prior to the start of each board year tied to strategic/critical issues and other matters to come before the board in that year	CEO and CIO with Gov. Prof./Ed. Coord.

Recommendation 3: Develop a plan for board member education

Major Component	Recommended Action Step	Suggested Responsibility
	Require board members to attend “director colleges” such as the one at Stanford designed for directors of public companies and major nonprofits, and encourage attendance at repeat or subsequent programs as well	Gov. Comm.
	Create board policy/protocol requiring board members to provide written evaluation of external programs attended prior to being reimbursed for expenses	Gov. Comm.
Specialized education programs for committees	Develop training for committee chairs focused on the role of committees and the role of committee chairs	Gov. Prof./ Ed. Coord.
	Institutionalize a process for communication among committee chairs re committee chair roles and governance issues at committee levels	Gov. Prof.
	Develop a separate educational curriculum for committee members focusing on issues that come before their committees	Gov. Prof./Ed. Coord.
	Develop program to build the expertise of committee members with oversight responsibility for the organization’s financial statements and related audit, similar to that required at public companies	Gov. Prof./Ed. Coord.
Refinements to existing orientation for new board members	Create glossary of terms to help new members understand the language you use	Gov. Prof./Ed. Coord.
	Provide fundamental level of education in each of the major areas for which CalPERS has responsibility	Gov. Prof./Ed. Coord.
	Build in follow up after each board/committee meeting to check in and review the topics again	Gov. Prof./Ed. Coord.
	Make these orientation briefings/programs available to any of the current board members as well	Gov. Prof./Ed. Coord.
	Create opportunities for new board members to get to know existing board members and management socially	Bd. Pres., Gov. Prof.

Recommendation 4: Focus on governance style; continue systematic refinement of other board processes

Major Component	Recommended Action Step	Suggested Responsibility
Reflect on governance style	Consciously shift more towards oversight role and away from operational one	Bd. Pres. and Comm. Chrs.
	Work to reduce tendency of some board members to focus too intently on operational details and routine matters	Bd. Pres. and Comm. Chrs
	Use ad hoc board committees to deal with particular areas where significant operational issues continue to be a major concern	Bd. Pres. and CEO
Reduce number of meetings	Set goal of eventually reducing overall number of board and committee meetings to be closer to that of peers	Gov. Comm.
Board room setting	Schedule more meetings in a large conference room or examine other ways to allow for more interaction between the board and management	Bd. Pres.
Re-examination of communications issues between board members and staff	Consider returning to one-on-one briefings for at least some board members	Bd. Pres., CEO in consultation with individual board members
	Develop some form of one-way communication—perhaps postings on board portal or Diligent Board Books—to help all directors stay informed more equally between meetings	Gov. Prof.
	Revisit current policy on communication with staff	Gov. Comm., CEO
Development and enforcement of additional board protocols	Develop Board protocols covering what is expected of board members, including expectations re treating staff with respect	Gov. Comm.
	Support Board President in actively calling board members out on conduct that is inappropriate or contrary to board policy	Bd. Mbrs.

Recommendation 4: Focus on governance style; continue systematic refinement of other board processes

Major Component	Recommended Action Step	Suggested Responsibility
Reinforcement and refinement of current board policies	Reinforce the zero tolerance policy re leaking board information before made public and remove violators (including delegates) from committee assignments and take away other privileges for violations	Bd. Pres. and Gov. Comm.
	Refine Governance Policy on leadership and committee appointments to: <ul style="list-style-type: none"> • clarify how chairs are actually selected • encourage periodic rotation to include board members in addition to elected board members • favor selection of committee chairs based on their experience and/or education in relevant areas • prohibit reappointment of committee chairs who do not take advantage of opportunities to become educated about their responsibilities 	Gov. Comm.
	Review disparities in time, support and compensation among board members	Gov. Comm.
Examination of needed board member expertise and criteria	Review existing board member expertise and competencies	Gov. Prof.
	Develop a list of board member criteria, including necessary skills, competencies and experience needed by the board, to be made available to the constituencies and appointing authorities	Gov. Comm., Gov. Prof.
Review of committee structure, scheduling and authority	Rethink scheduling of committee meetings based on need to increase focus on governance, performance and compensation and audit issues	Gov. Comm./Gov. Prof.
	Create committee charters which are “mission” driven and clearer about overall authority and responsibilities of each committee	Gov. Prof.
	Consider which committee responsibilities can be discharged at the committee level and not require board approval of every committee action	Gov. Comm.

Recommendation 4: Focus on governance style; continue systematic refinement of other board processes

Major Component	Recommended Action Step	Suggested Responsibility
	Annually review structure and functioning of standing committees to make sure that functioning properly, not engaged in matters more typically delegated to management, and leadership is effective	Gov. Comm., Gov. Prof.
	Reconsider the wisdom from a governance standpoint of use of committees comprised of all or almost all board members	Gov. Comm.
	Adjust the committee reporting process to provide better information to all board members before they are asked to approve committee recommendations or ratify committee actions	Gov. Prof., Comm. Deputies
Interactions with constituents	Develop a standard approach for board member interactions with stakeholders/members with issues needing resolution or attention	Gov. Comm.
	Appoint a senior executive to serve as the liaison between staff and the board—a point person—to handle constituent complaints raised with board members (someone board members can rely on to make sure issues are addressed and report back to the board member)	CEO