



Agenda Item 5d

June 17, 2013

ITEM NAME: Extension of the Trial Neutrality Responsible Contractor Program Policy

PROGRAM: Targeted Investment Programs

ITEM TYPE: Policy & Delegation – Action

RECOMMENDATION

Approve the extension of the “Neutrality Trial Responsible Contractor Program Policy” from June 30, 2013 to June 30, 2015 as shown in Attachment 1. A consultant opinion letter from Pension Consulting Alliance is provided as Attachment 2.

EXECUTIVE SUMMARY

In February 2010, the Investment Committee (IC) approved the Neutrality Trial Responsible Contractor Program (Neutrality Trial RCP) Policy and its corresponding Neutrality Trial Program (NTP). In August of 2011, the IC reviewed the program, and approved extension of the Neutrality Trial RCP Policy for one year to allow time for additional data collection. This agenda item provides an update on program participation, and recommends the IC approve the extension of the program for an additional two years.

STRATEGIC PLAN

This agenda item supports the CalPERS Strategic Plan goal to improve long-term pension and health benefit sustainability. An extension of the NTP will allow staff additional time to gather more meaningful experience and data under the program with the goal of determining the investment impact, if any, of the NTP, and as such is actively managing business risks.

BACKGROUND

The purpose of the NTP is to gather data on the investment impact, if any, of requiring neutrality as to employee and union organizing efforts. Building service (e.g., janitorial, security, window washing, or food service) contracts of \$100,000 or more are subject to the NTP. All current core real estate managers are participating in the NTP and their delegates and subdelegates are subject to the Neutrality Trial RCP Policy.

The Responsible Contractor Program (RCP) Policy continues to apply to non-core managers for domestic assets. The RCP Policy supports manager neutrality, but does not require it. In contrast, the Neutrality Trial RCP Policy requires manager, delegate and subdelegate neutrality in the event of a lawful labor organizing event.

Specifically, the Neutrality Trial RCP Policy requires a manager and its contractors to remain neutral when employees providing services pursuant to Neutrality Trial RCP-covered contracts organize, or when unions try to organize them. According to the Neutrality Trial RCP Policy: "To remain 'neutral' means not to take any action or make any statement that will directly or indirectly state or imply any support for or opposition to the selection by employees of a collective bargaining agent, or preference or opposition to any particular union as a bargaining agent."

A manager or CalPERS staff can exempt a contractor from the neutrality requirement if requiring neutrality would cause material adverse harm to a CalPERS investment. Such exceptions are only to be made after competitive bidding fails to produce an acceptable contractor who would agree to neutrality or other similar extenuating circumstances exist. Managers and staff are required to file reports about such exceptions and copies of those reports are provided to unions and investment managers that request them. To date, only one contract for \$122,000 has required an exception to the NTP. This contract for snow removal at a secure airport site was reported to the IC in August 2011.

Annual reports on RCP Policies are provided to the IC each December.

ANALYSIS

Purpose of the Neutrality Trial Program

The purpose of the NTP is to gather data on the investment impact, if any, of requiring manager, delegate, and subdelegate neutrality in the event a labor organization lawfully attempts to organize workers providing services at a RCP investment. To date no managers have reported attempts to organize workers providing services to CalPERS investments. The NTP provides standards for determining whether the program has been successful. The Neutrality Trial RCP Policy requires staff, at the end of the trial period, to report results, and provide recommendations regarding the neutrality requirement based on the results of the trial.

Neutrality Trial Program Contracting Update

Managers and contractors subject to the NTP file quarterly reports on the impact of the neutrality requirement. As of December 30, 2012, managers reported the following:

- 57 contracts totaling approximately \$18.5 million met the program criteria and were bound by the NTP.
- No additional exemptions to the NTP were requested.

The total number of contracts that meet the program criteria and are bound by the NTP has remained approximately the same throughout the NTP period. The total dollar amount of contracts has decreased slightly. Of the 57 contracts noted above, 55 are with three core managers. The remaining managers have one or fewer contracts under the NTP, and as a result, have limited data and experience under the NTP.

Staff has asked managers whether participation in the NTP has resulted in any measurable compliance cost to them or CalPERS. No manager reported any such cost or burden. However, managers have stated concerns that an improved economy and increased contracting activity have the potential to increase costs. Some managers report that finding a qualified contractor that will sign the NTP can require additional outreach and time in certain markets and note that an improving economy may affect their ability to find qualified contractors that will sign the NTP.

Portfolio Restructuring

At the NTP's inception date, in 2010, there were eight core real estate investment managers all of which agreed to participate in the NTP. Due to portfolio restructuring half of the original managers are no longer in the program and new core real estate managers have been added. All new core real estate managers are subject to the NTP. In the past several months, several new core real estate managers have been hired. More new core real estate managers are anticipated to be added to the Real Estate portfolio in the upcoming months. Manager changes, due to portfolio restructuring, have reduced contracting activity and the resulting collection of data on the impacts, if any, of requiring neutrality.

Trial Extension

When the Neutrality Trial RCP Policy went into effect, contracting was at a relatively low level due to economic conditions and portfolio restructuring. In August 2011, when the NTP was extended for one year, staff noted challenging market conditions, portfolio restructuring and a relatively small amount of contracting activity as reasons to extend the NTP. Staff finds that these conditions continue to exist. Additionally, there are only three managers with substantial data and experience with the NTP and managers have concerns that an improving economy may increase contracting costs under the NTP. Improving economic conditions, the addition of new core real estate managers subject to the policy, and increased contracting activity should provide additional information, which is necessary to accurately assess the NTP.

In an effort to gather more meaningful experience and data under the NTP, staff recommends that the Investment Committee approve extending the term of the NTP from June 30, 2013 to June 30, 2015.

BENEFITS/RISKS

As outlined above, the benefits of extending the trial are to allow time for new core real estate managers to be incorporated into the NTP, economic conditions to improve and additional data to be collected. There are no risks associated with extending the trial.

ATTACHMENTS

Attachment 1 – Neutrality Trial Responsible Contractor Policy
Attachment 2 – Pension Consulting Alliance Opinion Letter

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