

**Fiscal Year 2014-15
Annual Budget Proposal**

Second Reading
April 14, 2014

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Background

The annual budget process for the California Public Employees' Retirement System (CalPERS) is the period for reviewing the organization's existing resources and requests to meet CalPERS mission, strategic plan, and business plan priorities. The CalPERS Annual Budget Process is an ongoing and robust budget planning activity that considers the priorities of the enterprise, the mission of CalPERS, and ultimately the members that we serve. This process runs from October through April of each year with Board approval of the Total CalPERS Budget for the upcoming fiscal year. The Financial Office work collaboratively with divisions on analyzing the operational needs while ensuring the alignment with CalPERS strategic goals and business plan. The next phase is submittal and review of Formal Budget Requests for new services and initiatives. The Financial Office budget staff prioritize requests, conduct thorough analysis, and provide a formal recommendation for Executive review. In February, an Executive Review Panel allows division management the opportunity to present their requests prior to the finalization of the proposed budget for submittal to the Board for approval.

The following proposed budget provides the annual financial plan for FY 2014-15 with projections for the FY 2015-16. CalPERS is committed to maintaining efficient and effective administration that is accountable and transparent to its stakeholders. This document compiles the financial data needed to support CalPERS goals, is aligned with the proposed initiatives outlined in the CalPERS 2014-16 Business Plan, and is based on the departmental review of operations.

This budget was built upon five key areas:

- Sound organizational governance
- Alignment of the budget to strategic and business planning
- Realistic cost containment
- Expanded use of technology
- Strong customer focus

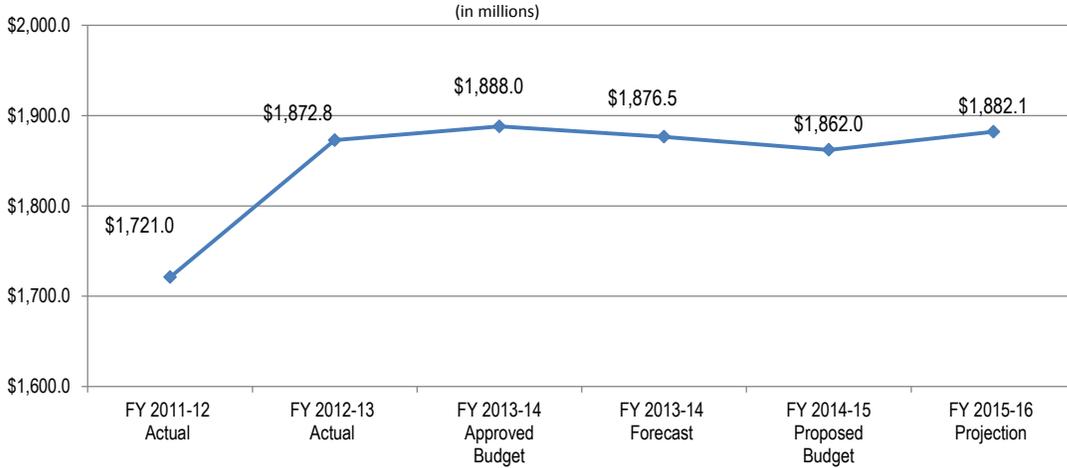
Budget Highlights

The FY 2014-15 Proposed Budget is estimated to be \$1,862.0 million, a decrease of \$26.0 million or 1.4 percent from the FY 2013-14 Approved Budget of \$1,888.0 million. The results reflect the collaborative effort of CalPERS management and staff who worked to identify efficiencies in the organization, resulting in a decrease in the overall budget costs from the current year budget. The Proposed FY 2014-15 Total Budget reflects a reduction of \$3.1 million from the first reading.

Highlights of the FY 2014-15 Proposed Budget include the following:

- Optimization of the myCalPERS system and ongoing knowledge transfer to realize increased operational efficiencies
- Redesign of the Actuarial Valuation System (AVS) to support Governmental Accounting Standards Board (GASB) reporting requirements
- Resources to develop and implement strategies for the continued growth of the California Employers' Retiree Benefit Trust (CERBT) Program
- Development of an enterprise treasury management function to enhance cash controls, cash integrity, and liquidity management
- Continued development of Business Intelligence tools to leverage data and information to support decision making
- Ongoing cost saving efforts to transition portfolio management activities from investment consultants to State staff
- Continued efforts to support the Long-Term Health Care program and employer wellness partnerships to improve health cost trends and increase the number of covered lives
- Additional lease space for relocation of call center staff to accommodate expanding workspace requirements
- Continuation of Security Roadmap Phase III effort to protect and secure CalPERS technology and data

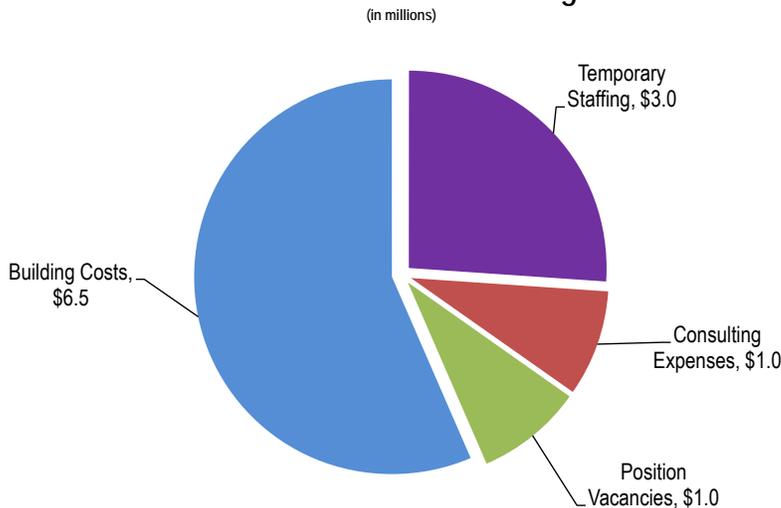
CalPERS Total Budget Forecast / Projection



FY 2013-14 Forecast

The FY 2013-14 Forecast is estimated to be \$1,876.5 million, a decrease of \$11.5 million or 1.0 percent from the FY 2013-14 Approved Budget of \$1,888.0 million. Potential budget savings are a result of reductions in temporary staffing (\$3.0 million), less than anticipated consulting expenses (\$1.0 million), position vacancies (\$1.0 million), and lower than anticipated building costs (\$6.5 million). Compared to the FY 2013-14 Forecast of \$1,876.5 million, the FY 2014-15 Proposed Budget of \$1,862.0 million represents a decrease of \$14.5 million or 0.8 percent. Investment External Management Fees, Third Party Administrator Fees, and Investment Operating Costs are unchanged from the FY 2013-14 Approved Budget.

FY 2013-14 Forecast Savings



FY 2015-16 Projection

The FY 2015-16 Projection¹ anticipates an increase of \$20.1 million or 1.1 percent from the FY 2014-15 Proposed Budget. Increases in Personal Services are due primarily to anticipated Merit Salary Adjustments for CalPERS staff and an increase of 2.5 percent to staff salaries as stated and anticipated in the 2014-15 Governor's Budget. Increases in Operating Expenses have been projected at an inflationary rate of 1.8 percent.² It is estimated that the Enterprise Project costs will be \$25.0 million based on the known projects scheduled for the FY 2015-16 Projection. The Investment External Management Fees and Third Party Administrator Fees projections are unchanged from the FY 2014-15 Proposed Budget.

¹The FY 2015-16 Projection is a high level estimate and is intended to be used for informational purposes only

² Inflationary rate is based on the Bureau of Labor Statistics Consumer Price Index (CPI)

Budget Summary

The FY 2014-15 CalPERS Total Budget focuses on CalPERS' strategic goals:

- Improve long-term pension and health benefit sustainability
- Cultivate a high-performing, risk-intelligent and innovative organization
- Engage in state and national policy development to enhance the long-term sustainability and effectiveness of our programs

The proposed FY 2014-15 CalPERS Total Budget is \$1,862.0 million, which represents an overall decrease of approximately \$26.0 million or 1.4 percent from the FY 2013-14 Approved Budget of \$1,888.0 million. Specifically, this is a \$27.4 million (4.7 percent) decrease to the Total Operating Costs, a \$13.5 million (1.3 percent) decrease to the Investment External Management Fees, and a partial offsetting increase of \$14.8 million (5.4 percent) for Third Party Administrator Fees.

Fiscal Year 2014-15 CalPERS Total Budget

(in millions)

	FY 2013-14 Approved Budget ¹	FY 2013-14 Forecast	FY 2014-15 Proposed Budget	Budget to Budget	
				\$ Change Incr / (Decr)	% Change Incr / (Decr)
Administrative Operating Costs	\$425.2	\$420.5	\$415.1	(\$10.1)	(2.4%)
Investment Operating Costs	84.4	84.4	80.6	(\$3.8)	(4.5%)
Total Operating Costs²	\$509.6	\$504.9	\$495.7	(\$13.9)	(2.7%)
Enterprise Projects	33.3	33.0	27.9	(5.4)	(16.2%)
Headquarters Building Costs	40.7	34.2	32.6	(8.1)	(19.8%)
Subtotal	\$583.6	\$572.1	\$556.2	(\$27.4)	(4.7%)
Investment External Management Fees³	\$1,030.0	\$1,030.0	\$1,016.5	(\$13.5)	(1.3%)
Third Party Administrator Fees⁴	\$274.5	\$274.5	\$289.3	\$14.8	5.4%
CalPERS Total Budget	<u>\$1,888.0</u>	<u>\$1,876.5</u>	<u>\$1,862.0</u>	<u>(\$26.0)</u>	<u>(1.4%)</u>
Total Positions	2,696.0	2,696.0	2,727.0	31.0	1.1%

¹ FY 2013-14 Midyear budget approved by CalPERS Board of Administration on December 18, 2013

² Effective FY 2014-15, investment related expenses are now reflected with all CalPERS Administrative Operating Costs.

³ Investment External Management Fees consist of both Base Fees and Performance Fees

⁴ Third Party Administrator Fees for FY 2013-14 include \$159.7 million annualized fees approved by the Board for the newly implemented self funded health plans with an effective start date of January 1, 2014

D. Total Operating Costs

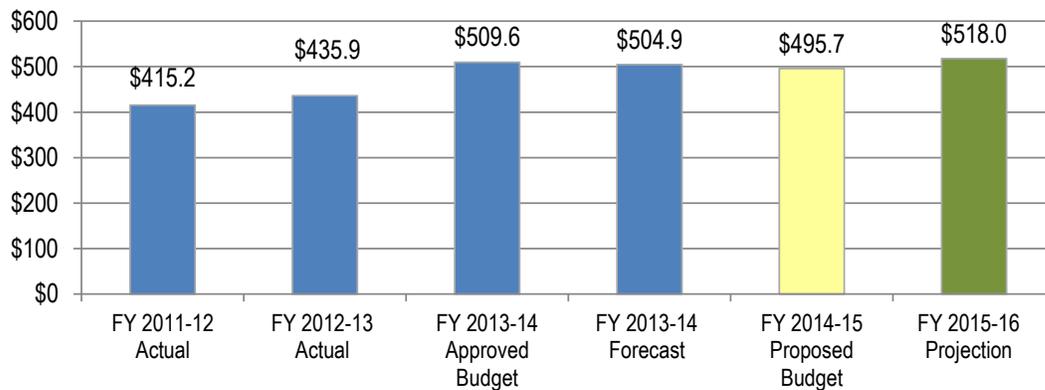
The CalPERS Total Budget is composed of five main areas which are presented on a consolidated basis to increase transparency and provide a holistic perspective. The budget areas are:

- Total Operating Costs
- Enterprise Projects
- Headquarters Building Costs
- Investment External Management Fees
- Third Party Administrator Fees

Each budget area will be covered separately and detailed to provide an analysis of the historical trending and current proposal of the costs.

Total Operating Costs Trend

(in millions)



Total Operating Costs for FY 2014-15 Proposed Budget are \$495.7 million compared to \$509.6 million in the FY 2013-14 Approved Budget, a decrease of \$13.9 million or 2.7 percent. Of that total, \$306.9 million or 61.9 percent, represents Personal Services costs which are projected to increase by \$17.8 million or 6.2 percent over the FY 2013-14 Approved Budget. As an offset, Operating Expenses & Equipment, which represent 38.1 percent are decreasing by \$31.7 million or 14.4 percent.

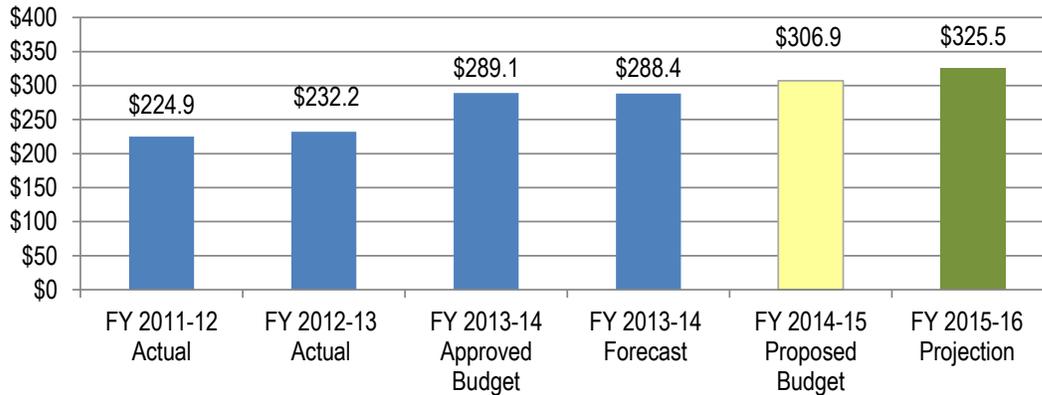
The following pages highlight each notable change for the expense items within the Total Operating Budget.

D. Total Operating Costs

	(in thousands)				
	FY 2012-13 Actual	FY 2013-14 Approved Budget	FY 2014-15 Proposed Budget	\$ Change Incr / (Decr)	% Change Incr / (Decr)
BUSINESS PLAN OPERATIONS:					
[1] PERSONAL SERVICES					
Salaries & Wages [1.1]	\$ 155,470	\$ 178,502	\$ 192,753	\$ 14,251	8.0%
Temporary Help [1.2]	10,147	20,600	14,256	(6,345)	(30.8%)
Overtime	1,490	2,224	2,012	(212)	(9.5%)
Benefits [1.3]	65,052	87,812	97,911	10,100	11.5%
Total Personal Services	\$ 232,158	\$ 289,137	\$ 306,932	\$ 17,795	6.2%
[2] OPERATING EXPENSES & EQUIPMENT *					
General Expense [2.1]	\$ 7,471	\$ 7,645	\$ 9,440	\$ 1,795	23.5%
Fund Admin Services/Subscriptions	4,464	6,478	5,759	(719)	(11.1%)
Software	4,901	1,717	1,714	(4)	(0.2%)
Printing	1,605	1,784	1,861	77	4.3%
Postage	3,050	3,439	2,528	(910)	(26.5%)
Communications [2.2]	2,241	2,757	4,099	1,342	48.7%
Data Processing Services [2.3]	20,380	18,033	9,510	(8,523)	(47.3%)
Travel [2.4]	1,732	2,652	3,628	976	36.8%
Training	1,234	1,465	1,829	364	24.9%
Medical Exam/Disability Travel	1,042	1,370	1,150	(220)	(16.1%)
Facilities Operations [2.5]	3,787	3,911	5,387	1,476	37.7%
Central Administrative Services [2.6]	18,026	19,078	22,263	3,185	16.7%
Attorney General Services	133	189	189	0	0.0%
Consultant & Professional Services [2.7]	54,366	68,498	53,746	(14,751)	(21.5%)
Outside Counsel [2.8]	26,641	25,111	19,853	(5,258)	(20.9%)
Audit Services	1,481	1,096	1,528	431	39.3%
Master Custodian Fees	7,528	5,867	5,934	66	1.1%
Appraisal Fees/Tax Advisory Services	7,376	5,892	5,949	57	1.0%
Federal Lobbyist	790	800	900	100	12.5%
Admin Hearings	472	500	500	0	0.0%
Other Admin & Operating Expenses	522	661	1,310	649	98.2%
Consolidated Data Centers	191	777	777	0	0.0%
Trading & Portfolio Mgmt Systems [2.9]	9,282	11,995	14,335	2,340	19.5%
Data/Analytics	11,791	12,156	12,983	827	6.8%
Business Operations Tool/Other Technology	757	685	818	133	19.4%
Equipment (includes EDP) [2.10]	12,519	15,902	743	(15,159)	(95.3%)
Total Operating Expenses & Equipment	\$ 203,782	\$ 220,458	\$ 188,733	\$ (31,725)	(14.4%)
GRAND TOTALS	\$ 435,940	\$ 509,596	\$ 495,665	\$ (13,931)	(2.7%)

[1] PERSONAL SERVICES

Personal Services Costs Trend
(in millions)



[1.1] Salaries & Wages

Increases in Personal Services of \$17.8 million are mainly due to higher salaries and wages (\$11.3 million), the proposed addition of 31 positions (\$3.6 million), retirement and health benefits (\$9.4 million), offset by reductions in temporary help and overtime (\$6.6 million). To recognize the impact of vacancies on the cost of salaries and wages, a factor of 6.5% has been used to reduce the total cost of salaries and wages, reducing the budget by \$12.5 million for salaries and wages and \$5.9 million for corresponding benefits. Considerable strides have been made by the organization to reduce the number of vacancies. The current vacancy rate of 8.7 percent is 2.8 percent lower than the 12.3 percent vacancy rate at this same time last year. It is anticipated that the vacancy rate will continue to decline, although at a slower pace as each division evaluate their existing vacancies and redirect or fill as part of their workforce planning.

The request for 31 positions at a cost of \$3.6 million resulted from a close look at each business area's needs, as staffing requests address several key functions to further advance the strategic objectives of the organization, including:

Benefit Program Policy and Planning

[\$204,000 – 2 PYs]

Continued customer focus in Health and Long Term Care (LTC) Programs with the support of 2 PYs to assist with the increased workload associated with the Health Program's self-funded health plans, as well as the LTC program contract monitoring, market research and program oversight.

In 2014, CalPERS replaced one statewide Health Maintenance Organization Plan with five self-funded health plans. The new 2014-18 contracted health plans require a position responsible for critical health plan oversight, compliance, and contracts workload. The requested position will perform separate workload functions, not yet supported in this new unit and helps to support CalPERS Strategic Plan, Goal A, to ensure high-quality, accessible and affordable health benefits. The risk of not approving the request would affect core business processes of Health care fund management, contract oversight,

and health plan compliance. This includes the inability to sustain levels of customer service, mitigate risk, and could impact the opportunity for significant return on investment.

In February 2013, the CalPERS Board of Administration Plan approved re-opening the LTC Program to new applicants; the first time the application period has been open since 2008, and the first time the application period will be continuous. The re-opening of the LTC Program supports Strategic Plan, Goal A, to implement changes to the LTC Program in order to strengthen the financial viability and enhance participant and applicant access to needed information. This requires a dedicated staff person to conduct long-term care market research, provide project oversight during open application periods, produce benefit design, third party administrator system changes coordinate all communication projects and support increased workload related to the new continuous open enrollment process. The risk of not approving this request could affect LTC growth projection estimates, fund growth, and present value of future premiums, which could lead to rate instability. There would also be increases in consulting costs related to open application period management and benefit design.

Customer Services and Support

[\$491,500 – 5 PYs]

Ongoing customer service by adding 3 PYs to support Public Agency eligibility verifications and an additional 2 PYs to manage the workload growth in the California Employer Benefit Trust (CERBT) program.

Of the three positions for the Customer Account Services Division Retirement Section, two are to support public agency contract process and risk management related to new Internal Revenue Service (IRS) public agency eligibility requirements. The new requirements require an eligibility determination for each new contract to ensure that the public agency meets Internal Revenue Code (IRC) standards. The new positions are needed to ensure public agencies meet the IRC parameters and that non-qualified public agencies do not participate in the IRC 414 governmental plans; putting CalPERS at risk of potential loss of IRC 414 status. The risk of not approving this request would negatively impact the timely completion of new agency reviews, and increase the likelihood that CalPERS could enter into contracts with non-qualified public agencies, jeopardizing CalPERS status as a governmental retirement plan under IRC 414.

The third position for the Customer Account Services Division Retirement Section in this division is needed to address external business partner support for my|CalPERS resulting from implementation, system integration, new system releases and future enhancements of the member self-service functionality, as well as to ensure compliance with CalPERS laws, regulations, and policies. These positions help support CalPERS Strategic Plan, Goal B, to deliver superior end to end, customer service that is adaptive to customer's needs; actively manage risks with an enterprise-wide view; and cultivate a high performing risk intelligent and innovative organization. The risk of not approving this request is the potential risk to data and financial integrity within the my|CalPERS System, and the inability to sustain critical levels of efficiency and customer service for business partners.

CalPERS is contracted to administer the CERBT trust in compliance with the Internal Revenue Code Section 115, to report trust results in compliance with Governmental Accounting Standards Board (GASB) statements, and provide fiduciary care in managing records and trust assets. The average

D. Total Operating Costs

growth rate of the CERBT Program's contracted employers is at 13% and 28% for assets under management; continued growth is projected. CERBT is a small unit of only nine staff; the two new positions are needed for the program growth to provide assistance in outreach efforts, administrative support, and review of actuarial reports for compliance with governmental accounting and actuarial standards of practice. This request supports CalPERS Strategic Plan, Goal A, to improve long-term pension and health benefit sustainability by adhering to GASB statement 68 reports. The risk of not approving this request could impact existing contracted employer's retention, growth of the program, and employer education and outreach.

Office of External Affairs

[\$275,000 – 3 PYs]

Due to the expansion of technology through social media and increased external communication workload, 3 PYs are requested to support Public Records Act inquiries, social media platforms, and enterprise digital communications.

The Public Affairs Office (PAOF) is responsible for CalPERS internal and external communications including media, video and print communications, website content and social media networks. Of the two proposed positions for this division, one position is needed to provide support for CalPERS new internal social media platform, the second position is for a new unit needed for complex strategic communications and analytical functions to maximize branch efficiencies and focus on enterprise strategic projects, stakeholder communications and branch administrative support. This request supports the Business Plan Objective service delivery transformation, to meet increased information demands and transparency, and improve customer service through social media. This request supports CalPERS Strategic Plan, Goal B, to deliver superior end-to-end customer service that is adaptive to customer needs to improve access, effectiveness and quality in service delivery and self-service capabilities. The risk of not approving this request would negatively impacts the demands of digital communications supporting the enterprise. PAOF would be unable fulfill the obligations as outlined in the Service Delivery Transformation Roadmap, posing a reputational risk of being non-responsive to our members and stakeholders.

The third position in the Office of Stakeholder Relations will be used to support stakeholder outreach requirements in an effort to broaden and increase the frequency of CalPERS engagement with key stakeholders. Additionally, the position will take the lead in quality assurance over the Public Records Act (PRA) process to provide a prompt and legally required response to PRA requests, which helps to mitigate risk of litigation and promote transparency. This position helps support CalPERS Strategic plan, Goal C, to clarify and communicate CalPERS perspective on pension, health and financial markets. The risk of not approving this request could be increased litigation by not meeting PRA requests in timely manner mandated by law. This could put CalPERS reputation at risk.

Financial Office

[\$804,000 – 7 PYs]

The development and implementation of new functionality for treasury management requires the addition of 4 PYs. An additional 3 PYs are requested to reduce reporting risks and implement new financial reporting requirements for the new Governmental Accounting Standards Board (GASB).

The new treasury management functionality is needed to sufficiently and adequately address cash flow and liquidity risks, fulfill Board mandated objectives, and produce cost savings. The risk of not approving this request could delay the implementation of the Treasury Management activities and the ability to effectively address cash flow and liquidity needs.

The Financial Reporting Unit needs to improve internal controls and meet new and existing GASB requirements, including GASB 40 and 53. The remaining 3.0 positions are proposed to meet these requirements and needs of the Financial Reporting Unit. The area is going through a reorganization and every position is being analyzed very closely as the Financial Office builds stronger internal controls and new functionality. These positions assist in meeting CalPERS Strategic plan, Goal B, to develop and implement improved processes and data integrity, and improve policy management throughout the entire financial process. The risk of not approving this request could increase the number of audit findings, incorrect financial reporting, and increase consultant costs needed to meet GASB reporting requirements.

General Counsel

[\$368,000 – 3 PYs]

The addition of 3 PYs, including an Assistant Chief Counsel, manager and analyst are requested to provide better coordination and review of professional legal staff and manage outside legal contracts to better manage costs and efficiencies.

The number of attorneys in the Advice Unit of the Legal Office (LEGO) has doubled to twelve positions over the last four years due to the increase in retirement and health membership, the number of retirement and health programs CalPERS administers, pension reform, municipal bankruptcies and the number and magnitude of contracts entered into by CalPERS. An Assistant Chief Counsel position is needed to manage the multiple legal assignments and new staff. This position will provide greater oversight and efficiencies resulting in greater output, quality, and timeliness in dealing with sensitive legal issues which will protect CalPERS and its members. Additionally, the LEGO has experienced a large increase in legal contracts and complex invoice tracking and handling. The additional two positions are for administrative support to assist in managing this increased workload and mitigate costs with stronger controls in place.

This request applies to Goals A, B and C of CalPERS Strategic Plan to improve long term pension and health benefit sustainability, cultivate a high-performing, risk intelligent and innovative organization and engage in state and national policy development. This request relates to many strategic objectives as outlined in the Business Plan. The work performed by LEGO touches each division of CalPERS and is varied. The approval of these positions will allow LEGO to continue to focus on the quality, timeliness and overall management of highly sensitive legal issues, to protect CalPERS and the members. The risk of not approving this request would impact LEGO's ability to manage their existing legal work and the services provided by staff counsel would be impeded, and potentially impact LEGO's professional responsibilities for CalPERS and the Board.

Investment Office

[\$1,060,000 – 7 PYs]

The continued efforts toward internalization of core, high value functions previously outsourced requires the addition of 7 PYs to implement workforce planning efforts for the resource strategy outlined in the Investment Office (INVO) Roadmap. The resource strategy identifies skill gaps and resource needs for better alignment with industry benchmarks to meet INVO's Target Operating Model.

The Interim CIO assessed the total request for FY 2014-15 and determined that the Investment Office's critical need was 7.0 positions for continued progress in implementation of the Roadmap. In their efforts to reduce the number of positions requested, INVO applied a number of considerations that included the evaluation/redirection vacant positions between programs and pushing any non-critical Roadmap efforts into the future. This request support CalPERS Strategic plan, Goal A, to improve long-term pension sustainability by delivering target risk adjusted investment returns and implementation of programs and initiatives that improve investment performance and ensure effective systems, operations and controls are in place. These positions are driven by the overall resource plan envisioned in the INVO Roadmap. The risk of not approving this request is potential delays in the progress of key INVO Roadmap initiatives, including implementation of the continued insourcing of investment operating functions and the reduction of external investment management consultants.

Operations and Human Resources

[\$366,500 – 4 PYs]

To administer an effective Equal Employment Opportunity (EEO) program, an internal investigator position is being requested to assist with follow up to inquiries. Additionally, to manage the growth in workload due to resources being added to the organization, 3 PYs are requested to address recruitment, classification and strategic workforce planning work.

An Equal Employment Opportunity (EEO) Investigator is needed in the CalPERS Diversity Outreach Program to investigate complaints, reduce costly outside investigation services, and comply with Government Code that requires all state agencies to establish and administer an effective EEO program; minimizing CalPERS risk and liability in not being able to conduct an investigation within the state mandated timeframe. The proposed Investigator position would be distinguished from other investigative and Human Resource classifications by having specialization in the EEO field. This request supports CalPERS Strategic plan, Goal B, to cultivate a high-performing, risk-intelligent and innovative organization by actively managing business risks with an enterprise-wide view. The risk of not approving this request will require the division to contract externally with employment law attorneys to investigate discrimination case over flow and close cases within the state mandated timeframe, at a substantially higher cost.

Three of the positions are being recommended for the Human Resources Division, two for the Classification and Consultation Unit as part of the strategic workforce plan presented to the Board of Administration in May 2013. The new positions are needed to address the classification changes, promotions, transfers, recruitments, organization structure changes, and performance management and discipline issues; functions that have increased in volume and complexity. The third position is for the Personnel Transactions Unit, which deals with payroll issues and leave, benefit and disability processing for CalPERS staff, needed to manage workload due to enterprise growth. This request supports CalPERS Strategic plan, Goal B, to cultivate a high-performing, risk-intelligent and innovative

organization by actively managing business risks with an enterprise-wide view by incorporating recruitment outreach and marketing, supervisory skills enhancement, and talent management strategies. The risk of not approving this request could result in transactional delays in processing personnel transactions for program areas, and potentially create unacceptable errors in payroll processing.

[1.2] Temporary Workload Assistance

Due to enterprise efforts to reduce reliance on temporary resources, the temporary staffing cost for CalPERS is anticipated to decrease by \$6.3 million, from \$20.6 million to \$14.3 million. This represents a reduction of \$3.1 million from the first reading.

[1.3] Retirement and Health Benefits

Retirement and health benefit costs for CalPERS state staff are anticipated to increase by \$9.5 million (\$4.3 million for retirement and \$5.2 million for health).

The table on the following page provides a detail summary on the new position requests.

D. Total Operating Costs

Agenda Item 6a. Attachment 1

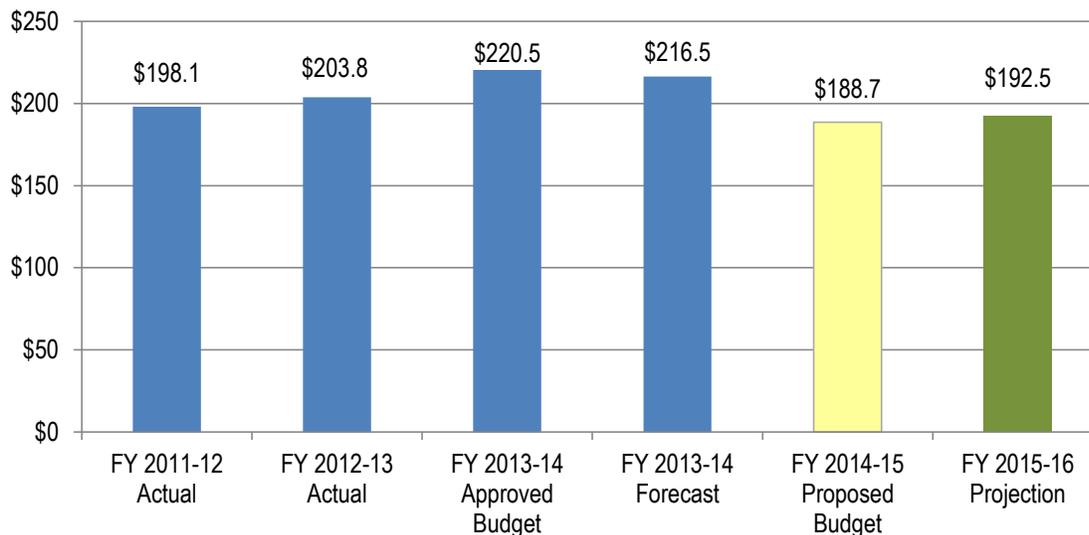
Branch	FY 2013-14 Authorized Positions	FY 2014-15 Proposed Positions	Change in Positions	% Change
Actuarial Office	55.0	55.0	-	0.0%
Benefit Program Policy and Planning	133.0	135.0	2.0	1.5%
1.0 – Health Maintenance Organization Compliance Workload				
1.0 – Long Term Care Contract and Market Research for Open Enrollment				
Customer Services and Support	890.5	895.5	5.0	0.6%
2.0 – Public Agency Eligibility				
1.0 – Business Partner Support Unit				
2.0 – CERBT Program Workload Expansion				
Office of External Affairs	63.0	66.0	3.0	4.8%
1.0 – Enterprise Digital Communications Support				
1.0 – Strategic Projects Support				
1.0 – Public Records Act Coordinator				
Executive Office	19.0	19.0	-	0.0%
Financial Office	209.0	216.0	7.0	3.3%
4.0 – Treasury Management				
3.0 – Financial Reporting				
General Counsel	127.0	130.0	3.0	2.4%
2.0 – Legal Administrative Unit				
1.0 – Legal Assistant Chief Counsel				
Investment Office	341.0	348.0	7.0	2.1%
1.0 – Global Equity Capital Allocation & Risk				
1.0 – Quantitative Research				
1.0 – Global Fixed Income Investment Support				
1.0 – Portfolio Manager Real Estate				
1.0 – Asset Allocation Risk Factor				
1.0 – Targeted Investment Program				
1.0 – Infrastructure & Forestland				
Operations and Technology	858.5	862.5	4.0	0.5%
1.0 – Investigation in the Diversity Office				
2.0 – Human Resources Classification & Consultation				
1.0 – Human Resources Personnel Transactions and Health & Safety Units				
Total	2,696.0	2,727.0	31.0	1.1%

[2] OPERATING EXPENSES & EQUIPMENT

Operating Expenses & Equipment costs of \$188.7 million represent a decrease of \$31.7 million or 14.4 percent from the FY 2013-14 Approved Budget, and \$27.8 million or 12.8 percent from the FY 2013-14 Forecast.

Operating Expenses & Equipment Costs Trend

(in millions)



[2.1] General Expense

Examples of items that post to the General Expense budget line item are general office supplies, subscriptions, membership fees, and conference costs. The \$1.8 million increase for this line item is a cumulative net effect to the enterprise primarily due to cost increases caused by the increase in staffing for the organization.

[2.2] Communications

The Communications budget is increasing by \$1.3 million primarily due to the transfer of the Telecommunications line item from the Headquarters Building Costs Budget to the Information Technology Services Branch Total Operating Costs Budget.

[2.3] Data Processing Services

Data Processing Services for the organization are decreasing by \$8.5 million due to larger expenditures in the current FY 2013-14 Approved Budget to fund Oracle hardware and software costs and the maintenance and operations costs that benefit enterprise-wide applications.

[2.4] Travel

The increase of \$1.0 million to the travel budget line item is primarily due to the Investment Office bringing more portfolio management functions in-house, which requires more due diligence traveling. The Customer Service and Support Branch is increasing the number of remote retirement planning fairs in FY 2014-15, increase the opportunities for travel.

[2.5] Facilities Operations

The facilities operations line item is increasing by \$1.5 million due to the Fresno Regional Office acquiring additional square footage and a newly planned off-site location for the CalPERS Call Center of the Customer Service and Outreach Division.

[2.6] Central Administrative Services

The State of California identifies and recovers central administrative services costs such as accounting, computing, payroll services, etc., from State departments funded from special and non-governmental cost funds (Pro Rata). The increase of \$3.2 million to the central administrative services budget line is due to a higher allocation assessed to the CalPERS organization.

[2.7] Consulting and Professional Services

The Consulting and Professional Services budget is anticipated to decrease by \$14.8 million. Over \$9.0 million of these costs are attributable to the Health Program area removing one-time costs from the previous budget year allocation. These costs included one-time marketing and consulting resources to assist with the reopening of the Long Term Care program to new members. In addition, there were one-time costs that also include funding for the procurement of the Health Data warehouse. Another \$5.0 million is a reduction from the Investment Office as they continue to make efforts to bring their contracted workload in house to state staff.

[2.8] Outside Counsel

The outside counsel budget is decreasing by \$5.3 million from \$25.1 million to \$19.8 million due to a reduction in public agency bankruptcy litigation (\$3.2 million) and the Investment Office anticipating a reduction in their outside legal counsel expenses (\$2.1 million) based on average historical trend. Of the \$19.8 million, \$10.5 million will be dedicated to investment related legal expenses, \$5.3 million to bankruptcy litigation and \$4.0 million to general outside counsel expenses.

[2.9] Trading & Portfolio Management Systems

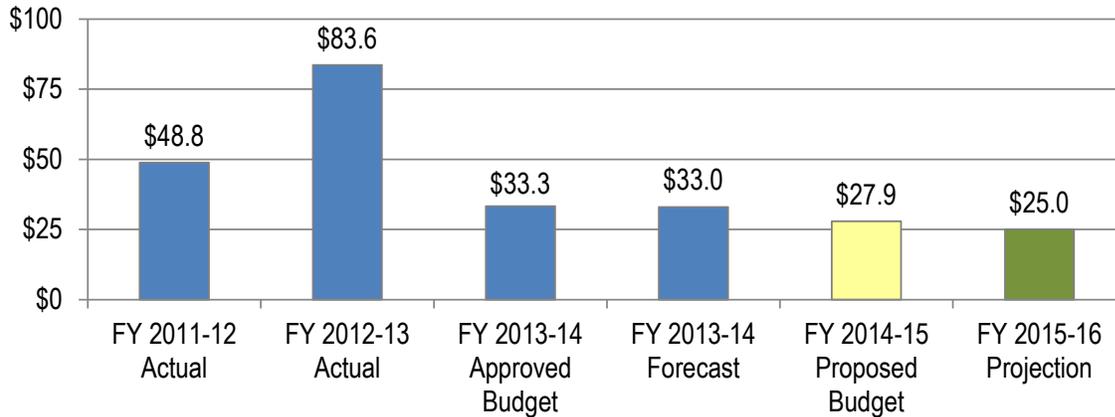
Trading and Portfolio systems are anticipated to be higher in cost by \$2.3 million from \$12.0 million to \$14.3 million due to the Investment Office commitment to building the infrastructure needed to support the investment management of assets that have been brought in-house.

[2.10] Equipment (includes EDP)

Equipment costs are decreasing by \$15.2 million primarily due to information technology hardware upgrades completed in FY 2013-14.

Enterprise Projects Costs Trend

(in millions)



The FY 2014-15 Enterprise Projects Budget Costs of \$27.9 million represent a decrease of \$5.4 million or 16.2 percent from the FY 2013-14 Approved Budget of \$33.3 million. Compared to the FY 2013-14 Forecast of \$33.0 million, the FY 2014-15 Proposed Budget represents a decrease of \$5.1 million or 15.5 percent. The \$27.9 million FY 2014-15 Proposed Budget is the lowest budget amount in the last five years.

Enterprise Projects (in thousands)	FY 2013-14 Approved Budget	FY 2014-15 Proposed Budget	\$ Change Incr / (Decr)	% Change Incr / (Decr)
[-] my CalPERS System	\$22,569	\$ -	(\$22,569)	(100.0%)
[1] my CalPERS Business Optimization	-	\$18,900	\$18,900	n/a
[2] Actuarial Valuation System	-	3,200	3,200	n/a
[3] Security Roadmap Phase III	5,979	2,608	(3,371)	(56.4%)
[4] Business Intelligence	2,460	1,000	(1,460)	(59.3%)
[5] Human Capital Management System	1,532	1,200	(332)	(21.7%)
[6] PeopleSoft Financials eProcurement Module	-	500	500	n/a
[7] Enterprise Migration to SharePoint	748	500	(248)	(33.2%)
Total of Enterprise Projects	\$33,288	\$27,908	(\$5,380)	(16.2%)

The concentration of the projects for the FY 2014-15 are centered around the my|CalPERS system optimization component, the reengineering of the Actuarial Valuation System, the third phase of the Security Roadmap Project, and finally continued reinforcement efforts towards the Business Intelligence and Enterprise Roadmap initiatives as follows:

[1] my|CalPERS Business Optimization

\$18.9 million

The my|CalPERS system has been integrated into the business processes of the organization. This funding will provide key optimization opportunities identified to leverage the system and realize increased operational efficiencies. Specific foundation work has been addressed for continued efforts to stabilize the my|CalPERS system for years to come. The pension area of CalPERS has been identified as a program area that would benefit from system optimization especially in the further enhancement of preparing retirement calculations, death processing, and disability retirement determinations. The Customer Service area would also benefit with special summary pages where most frequently accessed data could be viewed. Additionally, the Financial Office would benefit with increased reconciliation capability from the my|CalPERS system to their specific PeopleSoft Financials accounting and budgeting system.

[2] Actuarial Valuation System

\$3.2 million

The current Actuarial Valuation System (AVS) has been in existence for over eighteen years and will no longer meet evolving actuarial practices including changes required for employers to comply with new standards as required by the Governmental Accounting Standards Board (GASB). The investment to reengineer the AVS system would provide the capabilities needed to keep current with evolving practice and comply with GASB Statement Number 68 scheduled to be effective June 2015. A request for proposal for a vendor is planned for October 2014. The Actuarial Office plans on having a project manager and an AVS redesign consultant in place by December 2014. This is year one of a multi-year request requiring funding over a four year period for an estimated total investment of \$22.0 million.

[3] Security Roadmap Phase III

\$2.6 million

The Office of Enterprise Risk Management and the Information Technology Services Division are continuing work efforts tied to the Security Roadmap Project. The Security Roadmap is an ongoing multi-year effort that will ensure CalPERS technology and information will remain secure against constantly changing landscapes of threats. This project includes prioritized yearly initiatives and deliverables focused on implementing the latest preventative measures. For the FY 2014-15, the \$2.6 million related to phase III of the project would include the cost of two project managers and consulting hours to oversee and complete the Enhanced Enterprise Identity System. The project would also provide consultant program management support services to the two priorities for the coming year which are Data Loss Prevention and Security Information and Event Management controls.

[4] Business Intelligence

\$1.0 million

Funds are required to support the Business Intelligence program which leverages data and information to support decision making. With new information technology resources, CalPERS will be able to deliver certain Business Intelligence results, such as data integration between sources, data warehousing, and business-focused analytics. The funding will establish the base infrastructure and formal governance of the Business Intelligence Program. The Business Intelligence program is focused on making information accessible for better decisions on which CalPERS may act upon with confidence, supporting the ability to use advanced analytics to conduct health and other planning research.

[5] Human Capital Management System (HCMS)

\$1.2 million

Funding for the HCM system supports the e-performance and e-compensation functions within the Human Resources branch. This funding will automate many of the processes utilized by both Human Resources and the Financial Office to provide an integrated payroll and position control database information and streamline reporting.

[6] PeopleSoft Financials eProcurement Module

\$500,000

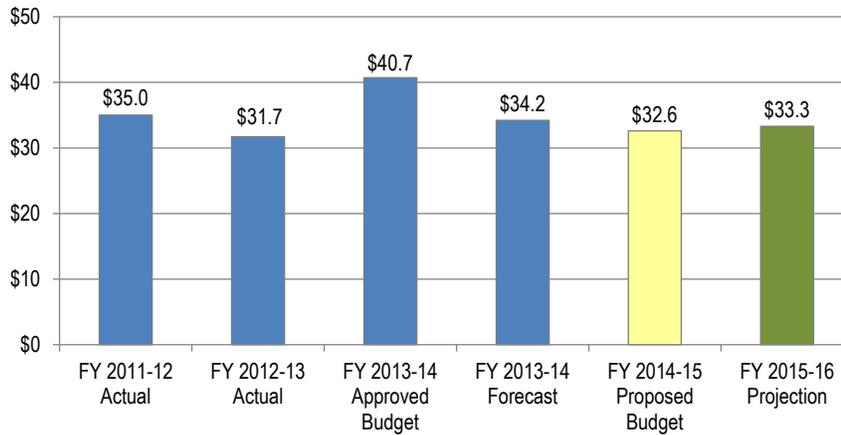
Funding is required to support the recent integration of the current CalPERS procurement system called WeBuy into the PeopleSoft Financials system e-Procurement module. This recent integration requires one year of support for two PeopleSoft Financials consultants who will provide knowledge transfer to existing staff on the maintenance and operations in the new systems platform.

[7] Enterprise Migration to SharePoint

\$500,000

SharePoint is a content and document management program utilized to support the Business Plan objective to implement an Enterprise Content Management system to centralize data content and improve content structure in addition to establishing a governance process to improve Internet usability. Funding is requested to augment staff resources to complete the migration to the new SharePoint platform for the remaining program areas in the CalPERS organization. Funding will also be utilized for training on the new technologies deployment as well as advanced web content management skills.

Headquarters Building Costs Trend
(in millions)



The Headquarters Building Costs Budget of \$32.6 million consists of operating expenses (utilities, engineering services, janitorial security, etc.), and non-operating expenses (structural improvements, staff moves, insurance, etc.).

Operating expenses in the FY 2014-15 Proposed Budget of \$18.3 million are relatively unchanged from FY 2013-14 Approved Budget.

Non-Operating expenses include owner improvements of \$7.1 million for data wiring improvements (\$2.5 million), electric underfloor distribution (\$1.5 million), master space plan with tenant improvements (\$1.6 million), and other miscellaneous improvements. Building Improvements of \$3.0 million include a remodel in the Lincoln Plaza North break room (\$0.8 million), radio and emergency response repeater replacement (\$0.5 million), and waterproofing (\$0.3 million) and other standard building maintenance costs. Furniture and fixtures of \$3.4 million include furniture, cubicle walls and labor for staff moves. Non-Operating expenses in FY 2014-15 of \$14.3 million have decreased by \$8.0 million from the FY 2013-14 Approved Budget as reconciled below:

(\$3.1)	Owner Improvements - Savings due to 1800 3rd Street renovations postponed.
(2.7)	Telecommunications - Funding being moved from Headquarters Building Costs Budget to Information Technology Services Branch's Operational Budget
(2.6)	Building Improvements – Completion in FY 2013-14 of Americans with Disabilities Act (ADA) federally required restroom modernization and Leadership in Energy and Environmental Design (LEED) improvements needed for recertification.
0.7	Engineering Services - Increase to Colliers engineering staff salaries.
(0.7)	Operating Other - Various decreases in cost for items such as waste removal, electrical, on-site child care center, and general maintenance
0.4	Miscellaneous - Net effect of all other changes
(\$8.0)	Total Change

F. Headquarters Building Costs

(in thousands)

	FY 2012-13 Actual	FY 2013-14 Approved Budget	FY 2014-15 Proposed Budget	Budget to Budget	
				\$ Change Incr / (Decr)	% Change Incr / (Decr)
Operating:					
Utilities	\$2,940	\$2,936	\$2,765	(\$171)	(5.8%)
Engineering Services	2,454	2,772	3,519	746	26.9%
Janitorial	2,984	3,063	3,096	33	1.1%
Landscaping	789	815	814	(1)	(0.2%)
General Maintenance	2,076	1,554	1,560	6	0.4%
Security	2,084	2,302	2,309	8	0.3%
Property Mgmt & Administrative Fees	1,030	1,152	1,225	73	6.3%
Café Plaza	459	359	359	-	0.0%
Front St. Parking/Warehouse	401	404	655	251	62.1%
EOC (Sun Center) ¹	501	354	487	132	37.4%
Operating Other ²	1,458	2,245	1,520	(725)	(32.3%)
Total Operating	17,177	17,957	18,309	352	2.0%
Non-Operating:					
Owner Improvements ³	7,023	10,145	7,064	(3,081)	(30.4%)
Building Improvements ⁴	2,867	5,625	2,994	(2,631)	(46.8%)
Telecommunications ⁵	2,435	2,708	-	(2,708)	(100.0%)
Furniture & Fixtures	1,545	3,356	3,356	-	(0.0%)
Building Insurance	674	886	930	44	4.9%
Total Non-Operating	14,543	22,719	14,343	(8,376)	(36.9%)
Total Expenses	\$31,721	\$40,676	\$32,652	(\$8,024)	(19.7%)

¹ Emergency Operations Center (EOC) includes utilities, janitorial, security, landscaping, generator maintenance

² Includes ongoing expense categories that individually equal less than \$300K annually such as electrical, HVAC, plumbing, general maintenance, waste removal, property taxes, child care center, parking garage

³ Non-Operating Owner Improvements include CalPERS operational enhancements and support for the movement of divisions, units, and/or staff within

⁴ Non-Operating Building Improvements are improvements made to the building structure or common areas

⁵ Telecommunications budget is now reflected in Information Technology Services Branch operations budget authority

G. Investment External Management Fees

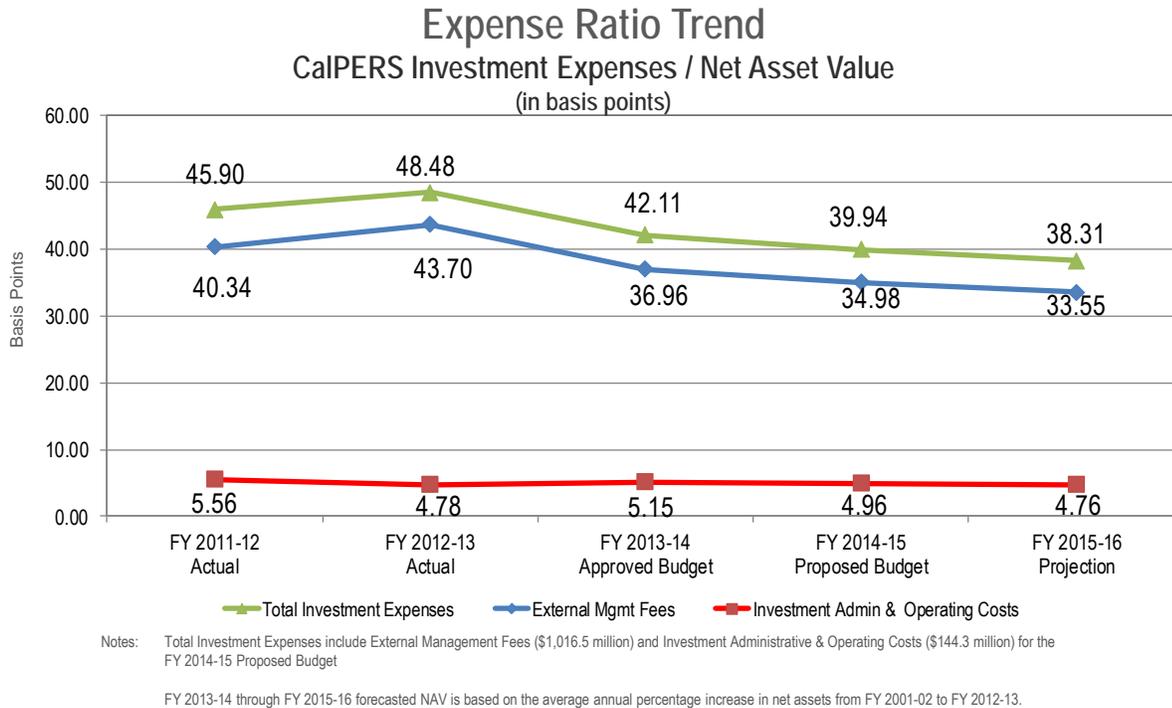
	(in thousands)				
	FY 2012-13 Actual	FY 2013-14 Approved Budget ¹	FY 2014-15 Proposed Budget	Budget to Budget Change	
				\$ Incr / (Decr)	% Incr / (Decr)
Global Equity	\$36,303	\$35,099	\$40,911	\$5,812	16.6%
Fixed Income	7,043	7,200	5,329	(1,871)	(26.0%)
Real Assets	201,944	194,871	201,944	7,073	3.6%
Absolute Return Strategy	60,708	68,000	60,708	(7,292)	(10.7%)
Private Equity	476,150	494,167	476,149	(18,018)	(3.6%)
Corporate Governance	38,382	39,174	26,413	(12,762)	(32.6%)
External Mgmt - Base Fees	\$820,530	\$838,511	\$811,455	(\$27,056)	(3.2%)
Global Equity	\$46,217	\$48,300	\$64,689	\$16,389	33.9%
Fixed Income	5,698	4,500	5,698	1,198	26.6%
Real Assets	270,624	65,017	71,329	6,312	9.7%
Absolute Return Strategy	55,026	64,000	55,026	(8,974)	(14.0%)
Corporate Governance	18,095	9,642	8,288	(1,355)	(14.0%)
External Mgmt - Performance Fees	\$395,660	\$191,458	\$205,030	\$13,571	7.1%
Total External Mgmt Fees	\$1,216,190	\$1,029,969	\$1,016,484	(\$13,485)	(1.3%)

¹ Investment expenses per FY 2013-14 Midyear Budget approved by CalPERS Board of Administration on December 18, 2013

The FY 2014-15 Proposed Budget of \$1,016.5 million is made up of \$811.5 million for External Management Base Fees and \$205.0 million for External Management Performance Fees which is an overall decrease of \$13.5 million or 1.3 percent from the FY 2013-14 Approved Budget. Total External Management Base Fees are decreasing by \$27.1 million or 3.2 percent from the previous FY 2013-14 Approved Budget. Global Equity costs are projected to increase due to higher portfolio values. Fixed Income and Private Equity costs are being projected to decrease due to CalPERS Investment Office insourcing of analytics efforts and the negotiating of more favorable contract terms. Corporate Governance portfolio management fees are expected to decrease due to a shifting of assets toward more cost effective Global Equity assets.

External Management Performance Fees of \$205.0 million for FY 2014-15 Proposed Budget is expected to increase by \$13.6 million or 7.1 percent over the FY 2013-14 Approved Budget of \$191.5 million. This expectation in higher performance fees is anticipated to be higher Global Equity and Real Asset returns offset by decreases in Absolute Return Strategy and Corporate Governance.

[1] Expense Ratio / Basis Point Trend



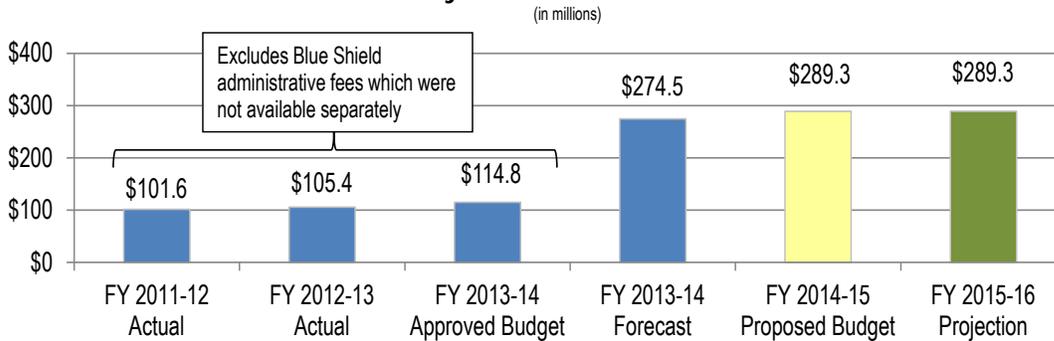
Basis Points Trend

The expense ratio measures the cost to maintain the funds and is determined by dividing the investment expenses by the dollar value of the assets under management (AUM). The ratio reflects investment expenses against the fluctuating value of the portfolio. The above chart shows the comparison, or ratios, of the External Management Fees and the Investment Administrative and Operating Costs to the net asset value (NAV) of the AUM by fiscal year.

The slight increase in basis points in FY 2012-13 Actual External Management Fees from the previous FY 2011-12 Actual reflects an increase in the performance fees as Real Assets outperformed its benchmark. Real Assets include investments related to real estate, forestland, and infrastructure.

The anticipated ratio of the FY 2014-15 Proposed Budget total investment expenses of 39.94 basis points assumes a downward trend in the ratio as staff negotiate more favorable portfolio management terms. There is a positive downward trend for both External Management Fees and Investment Administrative and Operating Costs relative to the NAV.

Third Party Administrator Fees Trend



Third Party Administrator Fees cover plan administration, recordkeeping, marketing, and participant communication services for the CalPERS Self-Funded Health Program, Long-Term Care Program, and Supplemental Income Plan Program. Establishing strong partnerships to support delivery of health and pension services continues to support our focus on improving long-term health and pension benefit sustainability for our members.

Total Third Party Administrator Fees for the FY 2014-15 Proposed Budget are \$289.3 million, an increase of \$14.8 million or 5.4 percent over the FY 2013-14 Forecast of \$274.5 million. The increase is driven by the Self-Funded Health Program and is offset with \$1.2 million in savings from the CVS Caremark Pharmaceutical provider.

(in millions)

	FY 2012-13 Actual ¹	FY 2013-14 Approved Budget ¹	FY 2013-14 Forecast	FY 2014-15 Proposed Budget	Forecast to Proposed Budget	
					\$ Change Incr / (Decr)	% Change Incr / (Decr)
Self-Funded Health Program ^{2,3}	\$ 73.2	\$ 77.0	\$ 236.7	\$ 249.9	\$ 13.2	5.6%
CVS Caremark Pharmacy	9.9	13.6	13.6	12.4	(1.2)	(8.8%)
Subtotal Health	83.1	90.6	250.3	262.3	12.0	4.8%
Long-Term Care Program - Univita	18.8	20.7	20.7	23.2	2.5	12.1%
Total Health	101.8	111.2	271.0	285.5	14.5	5.4%
Supplemental Income Plan - ING	3.6	3.5	3.5	3.8	0.3	8.6%
TOTAL	\$ 105.4	\$ 114.8	\$ 274.5	\$ 289.3	\$ 14.8	5.4%

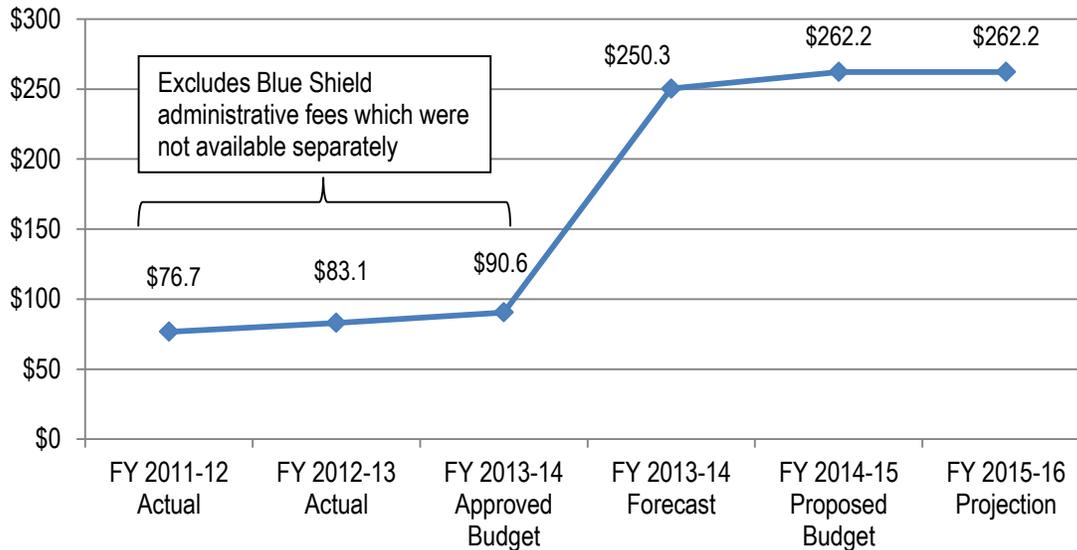
¹ Excludes Blue Shield administrative fees which were not available separately for FY 2013-14 Approved Budget and FY 2012-13 Actual

² Excludes Kaiser global capitation system which does not capture administrative fees separately

³ Includes Anthem Blue Cross, Blue Shield, Health Net, Sharp Health Plan and United Healthcare

Self-Funded Health Program

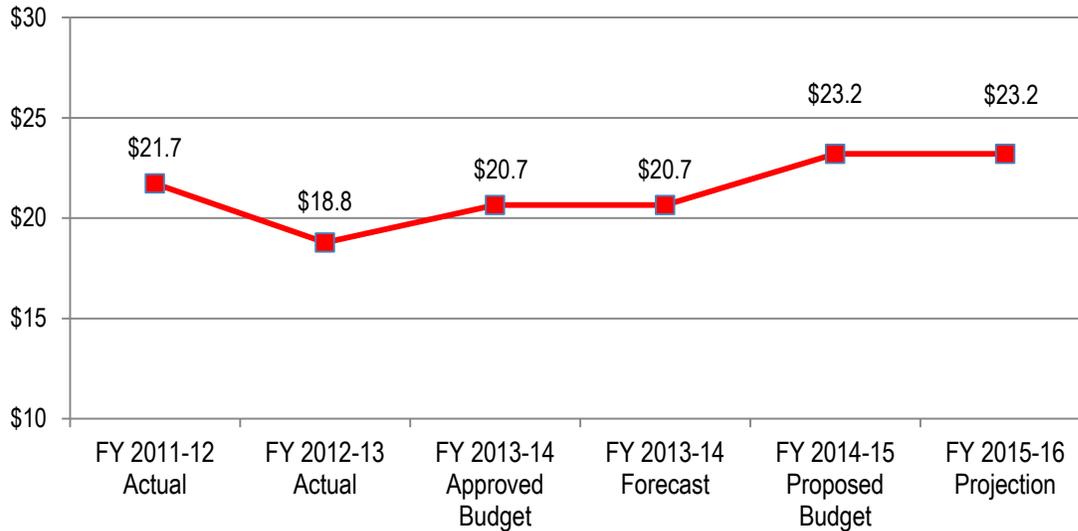
(in millions)



The Self-Funded Health Program provides health coverage to more than 1.3 million members and their families enrolled in CalPERS health plans which include all active and retired California State employees, as well as active and retired employees of local agencies and school districts. Effective January 1, 2014, health coverage providers were expanded to include Anthem Blue Cross, Blue Shield, Health Net, Sharp Health Plan and United Healthcare.

The FY 2014-15 Proposed Budget of \$262.3 million represents an increase of \$11.9 million or 4.8 percent due to anticipated increases in the new number of self-funded health plans for the full 2014 calendar year.

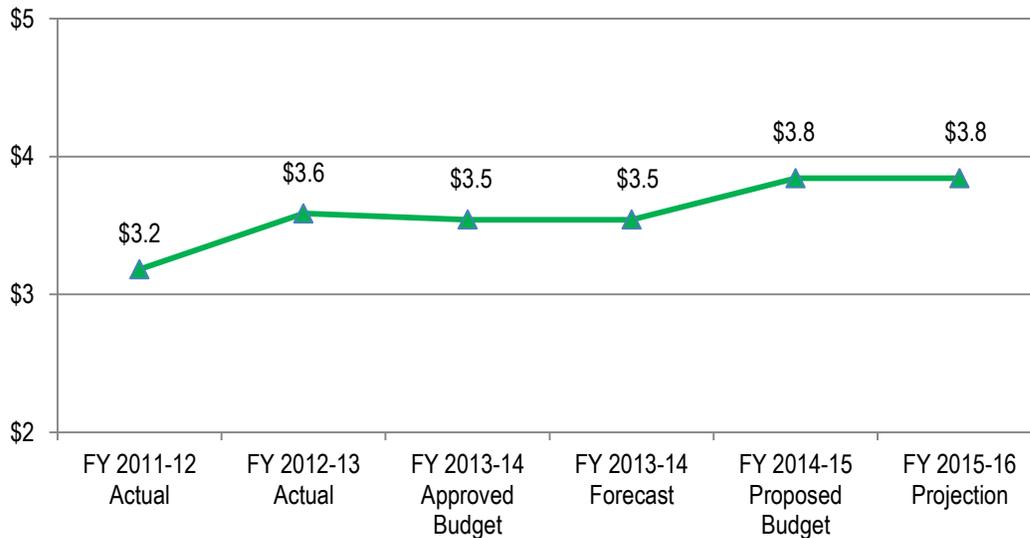
Long Term Care (in millions)



The Long-Term Care Program, as administered by Univita, provides comprehensive long-term care personal non-medical assistance, including care at home, adult care centers, assisted living facilities, and nursing homes. Administrator fees include underwriting costs, billing/banking, care advisory services, claims administration, reports, and customer service.

The Proposed Budget of \$23.2 million for FY 2014-15 represents an anticipated increase of \$2.5 million or 12.1 percent from the \$20.7 million FY 2013-14 Forecast. This is also an increase of \$4.4 million or 23.4 percent from the FY 2012-13 Actual Costs of \$18.8 million. Increases are due to the recent re-opening of enrollment for this program which is anticipated to attract new applicants.

Supplemental Income Plan (in millions)



The Supplemental Income Plans (SIP) program provides deferred compensation and defined contribution plans for employees of participating public agencies, schools, and the State of California. The ING Group is the third party administrator responsible for providing recordkeeping and administrative services for the SIP Program.

Fees are anticipated to increase by \$0.3 million or 8.6 percent from the FY 2013-14 Approved Budget/Forecast of \$3.5 million to the total FY 2014-15 Proposed Budget of \$3.8 million. The increase is due to an anticipated increase in assets under management.

I. Administrative Budget by Fund Source

Fund	FY 2012-13 Actual	FY 2013-14 Approved Budget	FY 2014-15 Proposed Budget	Budget to Budget	
				\$ Change Incr / (Decr)	% Change Incr / (Decr)
Administrative Budget					
Public Employees' Retirement Fund (PERF)	\$ 297,661	\$ 354,196	\$ 353,115	\$ (1,081)	(0.3%)
Public Employees' Contingency Reserve Fund (CRF)	26,230	28,947	27,130	(1,817)	(6.3%)
Public Employees' Health Care Fund (HCF)	16,882	28,351	22,835	(5,516)	(19.5%)
Long-Term Care Fund (LTCF)	2,011	5,012	3,429	(1,583)	(31.6%)
Annuitants' Health Care Coverage Fund (AHCCF)	1,938	2,036	2,092	56	2.8%
Deferred Compensation Fund (DCF)	1,423	2,189	2,198	9	0.4%
Judges' Retirement Fund (JRF)	1,329	1,113	1,154	41	3.7%
Judges' Retirement Fund II (JRF II)	845	905	939	34	3.8%
Legislators' Retirement Fund (LRF)	389	365	372	7	1.9%
Replacement Benefit Custodial Fund (RBF)	8	9	9	-	0.0%
Subtotal	\$ 348,716	\$ 423,123	\$ 413,273	\$ (9,850)	(2.3%)
Reimbursements ¹	2,961	2,086	1,825	(261)	(12.5%)
Total CalPERS	\$ 351,677	\$ 425,209	\$ 415,098	\$ (10,111)	(2.4%)

¹ Amounts received by CalPERS for services rendered. These reimbursements are actuarial valuations prepared for public agencies that qualify for reimbursement, cost of photocopies/postage related to the Public Records Act requests, annual employer conferences, and administrative assessments for employers' delinquent payroll

J. Total Operating Costs Summary

	(in thousands)			
	FY 2013-14 Approved Budget	FY 2014-15 Proposed Budget	\$ Change (Decr) / Incr	% Change (Decr) / Incr
Total Operating Costs				
Actuarial Office	7,102	7,636	534	7.5%
Benefit Programs Policy and Planning	30,794	25,928	(4,866)	(15.8%)
Customer Services and Support	101,375	94,647	(6,728)	(6.6%)
Executive Office	5,913	4,693	(1,220)	(20.6%)
Financial Office	25,256	23,469	(1,787)	(7.1%)
General Counsel	27,688	25,177	(2,511)	(9.1%)
Investment Office ¹	143,636	144,262	626	0.4%
Office of External Affairs	12,587	12,663	76	0.6%
Operations and Technology	134,560	125,807	(8,753)	(6.5%)
Other ²	20,674	31,385	10,711	51.8%
Subtotal	\$ 509,584	\$ 495,665	(13,919)	(2.7%)
Enterprise Projects Budget	33,288	27,908	(5,380)	(16.2%)
Headquarters Building Costs	40,676	32,652	(8,024)	(19.7%)
Investment External Management Fees	1,029,969	1,016,484	(13,485)	(1.3%)
Third Party Administrator Fees³	274,488	289,291	14,803	5.4%
CalPERS Total Budget	\$ 1,888,006	\$ 1,862,000	\$ (26,006)	(1.4%)

¹ The Investment Office now includes the investment related operation costs previously displayed in the Investment Expense Budget

² Includes Central Administrative Services (Pro-Rata), projected 2 percent Governors Budget increase to salaries, and merit salary adjustments

³ Includes Self-Funded Health Program Fees, Long-Term Care Fees, and Supplemental Income Management and Custodial Fees