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MEMORANDUM

TO: CalPERS Investment Committee

FROM: K&L Gates LLP

DATE: August 27, 2015

RE: Federal Monthly Report on Investment Policy - August 2015

While Congress was in recess for much of August, the SEC and CFTC were busy with key personnel changes and significant rulemakings that will likely be the subject of congressional discussion in the fall. In addition, the FHFA's recent move to increase GSE CEO compensation seems to have created momentum for potential legislative activity related to housing finance.

Derivatives

On August 5, the SEC held an open meeting in which it adopted rules and forms, under the Securities Exchange Act of 1934, providing for the registration of security-based swap dealers and major security-based swap participants. Additionally, the SEC proposed rules of practice to provide a process for a registered security-based swap dealer or major security-based swap participant to apply to the SEC to be permitted to continue effecting security-based swaps activities through associated persons subject to certain adverse legal actions, if doing so would be consistent with the public interest.

On August 13, the CFTC announced in a no-action letter that it would again delay implementation of proposed regulations to require foreign banking organizations that employ U.S.-based personnel who arrange or negotiate swaps with non-U.S. counterparties to comply in those transactions with certain Dodd-Frank rules related to financial protection, market efficiency, and price discovery. The latest CFTC no-action letter delays implementation until September 30, 2016.

Also at the CFTC, Democratic Commissioner Mark Wetjen announced his resignation on August 14. This comes a little over a year after Republican Commissioner Scott O'Malia announced his resignation from the CFTC, bringing to two the number of slots the President will now have to fill on the CFTC's five-member board. While it is not yet clear who the President will nominate to fill the two seats, Wetjen's departure increases the backlog of financial regulator nominees pending before the Senate.

Housing Finance

An important issue that has recently gained momentum is the potential opening for legislative activity that the FHFA, under the leadership of Director Mel Watt, seems to have created when it raised GSE CEO compensation from $600,000 to $3 million per year.

The political response was swift, with nearly unanimous House Financial Services Committee opposition and Senate efforts toward a hotline, which were later pulled back when the opportunity to accomplish other GSE reforms was realized. At end, the FHFA has essentially created the need for "must pass" legislation this fall, which could serve as a vehicle for the credit-risk transfer mandate included in Senate Banking Committee Chairman Richard Shelby's (R-AL) controversial regulatory reform bill.

As a result, the Senate is expected to work on legislation to limit GSE CEO pay, which will also include a mandate for increasing the volume and variety of credit risk transfers, possibly prevent the end of conservatorship without legislation, possibly prevent GSEs' guaranty fees from being used as "pay-fors," and demand further changes to Common Securitization Platform project to make it available to entities other than the GSEs.

Additionally, the FHFA announced new affordable housing goals that roughly conform to the proposed levels earlier this year, but are still lower than the pre-crisis levels. The current levels were set in 2012 and the new levels are effective for 2015-2017. For example, 24 percent of GSEs mortgages will be required in low-income areas, up from 23 percent. Of interest, the rule was accompanied by a report on the methodology the FHFA used to estimate the size of the affordable housing market.

Securities
At its August 5 open meeting, the SEC also adopted final rules requiring public companies to disclose the ratio of the annual total compensation of the chief executive officer to the median of the annual total compensation of the company's employees. The rule was required under the Dodd-Frank Act and has been controversial. Companies will be required to provide disclosure of their pay ratios for their first fiscal year beginning on or after January 1, 2017. The rules will be effective on October 19, 2015.

In response, House Financial Services Committee Chairman Jeb Hensarling (R-TX) indicated that the Committee will consider legislation (H.R. 414) this fall to repeal the provision. Prospects in the Senate are unclear, however. Although Senator Mike Rounds (R-SD) has also introduced repeal legislation (S. 1722) and recently affirmed his commitment to trying to move the bill forward, Chairman Shelby has not yet signaled whether the Banking Committee will take up S. 1722.

Debate over who will replace departing SEC Commissioners Luis Aguilar and Daniel Gallagher persists. The President had been expected to nominate corporate attorney Keir Gumbs to fill Aguilar's seat, but the potential nomination was met with criticism from Senator Elizabeth Warren (D-MA) based on Gumbs' apparent ties to corporate clients. As a result, the White House is vetting other candidates for Aguilar's seat. Nominations of replacements seem to be on hold at the moment but, once announced, they will likely be subjected to scrutiny from both sides of the aisle. Despite recent efforts by Democrats to urge Chairman Shelby to act on the backlog of financial regulator nominations pending before the Committee, reducing the backlog substantially does not appear to be at the top of the Senate Republican Majority's agenda for the fall.