MEETING

STATE OF CALIFORNIA

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

BOARD OF ADMINISTRATION

INVESTMENT COMMITTEE

OPEN SESSION

ROBERT F. CARLSON AUDITORIUM

LINCOLN PLAZA NORTH

400 P STREET

SACRAMENTO, CALIFORNIA

MONDAY, DECEMBER 14, 2015

9:00 A.M.

JAMES F. PETERS, CSR
CERTIFIED SHORTHAND REPORTER
LICENSE NUMBER 10063

APPEARANCES

COMMITTEE MEMBERS:

Mr. Henry Jones, Chairperson

Mr. Bill Slaton, Vice Chairperson

Mr. Michael Bilbrey

Mr. John Chiang, represented by Mr. Frank Moore

Mr. Richard Costigan

Mr. Rob Feckner

Mr. Richard Gillihan, represented by Ms. Katie Hagen

Ms. Dana Hollinger

Mr. J.J. Jelincic

Mr. Ron Lind

Ms. Priya Mathur

Ms. Theresa Taylor

Ms. Betty Yee

STAFF:

Ms. Anne Stausboll, Chief Executive Officer

Ms. Cheryl Eason, Chief Financial Officer

Mr. Ted Eliopoulos, Chief Investment Officer

Mr. Doug Hoffner, Deputy Executive Officer

Mr. Doug McKeever, Deputy Executive Officer

Mr. Brad Pacheco, Deputy Executive Officer

Mr. Matthew Jacobs, General Counsel

Ms. Kit Crocker, Investment Director

A P P E A R A N C E S   C O N T I N U E D

STAFF:

Ms. Cheryl Edwards, Committee Secretary

Mr. Jim Hurley, Investment Director

Mr. Mike Inglett, Investment Director

Mr. Paul Mouchakkaa, Managing Investment Director

Ms. Beth Richtman, Investment Manager

Mr. Wylie Tollette, Chief Operating Investment Officer

Ms. Laurie Weir, Investment Director

ALSO PRESENT:

Mr. David Altshuler, StepStone Group, LLC

Mr. Allan Emkin, Pension Consulting Alliance

Ms. Christy Fields, Pension Consulting Alliance

Mr. Michael Flaherman, University of California, Berkeley

Mr. David Glickman, Pension Consulting Alliance

Mr. Andrew Junkin, Wilshire Associates Consulting

Mr. Dillon Lorda, Pension Consulting Alliance

Mr. Michael Ring, Service Employees International Union Capital Stewardship Program

I N D E X

I N D E X   C O N T I N U E D

P R O C E E D I N G S

CHAIRPERSON JONES: I'd like to call the Investment Committee meeting to order. The first item on the agenda is roll call, please.

COMMITTEE SECRETARY EDWARDS: Henry Jones?

CHAIRPERSON JONES: Here.

COMMITTEE SECRETARY EDWARDS: Bill Slaton?

VICE CHAIRPERSON SLATON: Here.

COMMITTEE SECRETARY EDWARDS: Michael Bilbrey?

COMMITTEE MEMBER BILBREY: Good morning.

COMMITTEE SECRETARY EDWARDS: John Chiang represented by Frank Moore?

ACTING COMMITTEE MEMBER MOORE: Here.

COMMITTEE SECRETARY EDWARDS: Richard Costigan?

COMMITTEE MEMBER COSTIGAN: Here.

COMMITTEE SECRETARY EDWARDS: Rob Feckner?

COMMITTEE MEMBER FECKNER: Good morning.

COMMITTEE SECRETARY EDWARDS: Richard Gillihan represented by Katie Hagen?

ACTING COMMITTEE MEMBER HAGEN: Here.

COMMITTEE SECRETARY EDWARDS: Dana Hollinger?

COMMITTEE MEMBER HOLLINGER: Here.

COMMITTEE SECRETARY EDWARDS: J.J. Jelincic?

COMMITTEE MEMBER JELINCIC: Good morning.

COMMITTEE SECRETARY EDWARDS: Ron Lind.

COMMITTEE MEMBER LIND: Here.

COMMITTEE SECRETARY EDWARDS: Priya Mathur?

COMMITTEE MEMBER MATHUR: Good morning.

COMMITTEE SECRETARY EDWARDS: Theresa Taylor?

COMMITTEE MEMBER TAYLOR: Here.

COMMITTEE SECRETARY EDWARDS: Betty yee?

COMMITTEE MEMBER YEE: Here.

CHAIRPERSON JONES: Thank you.

The next item is the Executive Report, Chief Investment Officer Briefing. Mr. Eliopoulos.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Sure. Good morning, Mr. Chair. Good morning, members of the Investment Committee. I have just some brief remarks this morning. We have a full agenda before us today. And importantly, in today's agenda, we are concluding the calendar year review of our various constituent asset classes with the annual review of the real assets asset class today. And we have a series of agenda items reviewing real assets, this final and last review of the calendar year of all of the asset classes that make up CalPERS asset allocation.

As we turn our attention to real assets, I thought it would be helpful to provide some context around what has been really a protein asset class over the years, ever changing chameleon-like, as CalPERS has really tried to settle on and wrestle with real assets' role, our approach, and the constituent parts that make up what we know today as real assets.

What has not changed over this time period is the relatively modest proportion or percentage of real assets asset class in the overall asset allocation over the decades, ranging from five percent to ten percent of the total fund over this time period. And this is important, and not to be overlooked, as we have really come to define the role of real assets in consideration of the remaining 90 percent of the total fund we have just reviewed over the course of the past three months.

In the 1980s, 1990s, and early 2000s, the asset class that we now know as real assets was known as real estate. Its role, during that time period, was articulated as a diversifier for the total fund, much as it is today. It was made up mostly of core commercial real estate, mostly unlevered or very lowly levered, you know, 20 percent LTV or less. It evolved over these decades gradually.

Forestland, for example, was added under the real estate umbrella during this time period quite successfully in that era. Single family housing was added in the 1990s quite successful, until as we all remember, 2008. Then it evolved more suddenly or rapidly in the early 2000s. A new business model was, I think, thoughtfully added, the separate account model for the eight core commercial real estate partnerships.

An Opportunistic Program was allowed to develop. More leverage was allowed into the real estate policy and portfolio, as much as 80 percent loan to value, in some cases. And importantly, in the real estate policy itself, in addition to the diversification role, return enhancement was added as a twin goal of the real estate portfolio.

In 2007, real estate remained by itself as an asset class, but a new separate asset class was introduced into the asset allocation at that time, known by the acronym ILAC, inflation linked asset class and. At that time, it was composed of constituent parts, part public part private. It was composed of TIPS, or inflation protected securities and commodities on the public side. And for the first time, infrastructure was added as a private asset class into this new ILAC asset class.

Forestland was re-introduced to the fund at that time in 2007 as part of this asset class. In 2010, fast-forwarding three years, real assets was introduced as an asset class and really recombined these constituent parts, taking the private asset classes of infrastructure and forestland, adding it to real estate to make up the asset class that we now know as real assets.

At that time as well in 2002 importantly, a new but really old role was established for real assets which was to be a diversifier this time more specifically a diversifier to the equity risk that is inherent in the portfolio.

Well, we have, I think, appropriately today a very thorough review planned by the new head of real assets, Paul Mouchakkaa. And I think it's very appropriate and very timely to have Paul review the program, and as he will tell you during the course of his presentation later today, he is in the midst of preparing a new strategic plan for real assets that together with the Investment Committee will be reviewed and adopted next year, which is according to the timetable in our real assets policy that every five years this Committee will take up a look of the real assets strategic plan.

Paul is well aware of much of the short history that I just went through and described. But importantly, I think he brings a fresh perspective and fresh energy to the asset class, which I know our whole senior team welcomes, and appreciates, and we have tremendous confidence in him and his team's capabilities to take on what will be the next chapter in the asset class we know as real assets.

So with that, Mr. Chair, those are my comments.

CHAIRPERSON JONES: Okay. Thank you. We have a couple questions.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Ted, DTC has been in the news recently about its liquidity problem and its liquidity in the repo market. Has -- do you have any comments on that, and do you expect it to have any impact on our portfolio?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Boy, I don't have any comments for this public session. It is a topic that your senior team has been reviewing and considering.

COMMITTEE MEMBER JELINCIC: Okay. And Third Avenue Focused Credit fund obviously is having some problems. Does that have any impacts on either our private equity portfolio or the fixed income portfolio given that we're moving more into leveraged loans.

CHIEF INVESTMENT OFFICER ELIOPOULOS: I think specifically, in terms of Third Avenue, that's something that we will review. I wouldn't want to comment on the fly based on the newspaper articles that were published about Third Avenue over the weekend.

I think the topic of the roiling of the credit markets is one we're very much aware of and paying quite a bit of attention to.

COMMITTEE MEMBER JELINCIC: And do you expect it -- what kind of impact do you expect on the portfolio looking at your crystal ball?

CHIEF INVESTMENT OFFICER ELIOPOULOS: I think it's always dangerous to look into the future and make projections about it. But certainly the moves in the credit markets are ones that we're well aware of and are interesting.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Mrs. Mathur.

COMMITTEE MEMBER MATHUR: Thank you. I don't know if the audience is aware, but I just wanted to congratulate, Ted, for your leadership and the award that you were awarded by CIO Magazine, Best Public Defined Benefit Plan over $100 billion, that we and you together were honored with.

And I think they elucidated a number of the sort of strategic thoughtful long-term planning issues that we've been grappling with over the past couple of years that you've led us so ably with. So I just wanted to congratulate you for that, because I think it really says a lot about you and about our organization.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Well, thank you so much. And it's -- it really is a wonderful team that we collectively have here, and it's nice to be recognized.

CHAIRPERSON JONES: Okay. Thank you very much for those comments, Ms. Mathur.

Okay. Thank you, Ted.

Okay. The next item on the agenda is the action consent item, approval of the November 16, 2015 meeting minutes. Do we have a motion?

COMMITTEE MEMBER MATHUR: Move approval.

CHAIRPERSON JONES: Moved by Ms. Mathur.

VICE CHAIRPERSON SLATON: Second.

CHAIRPERSON JONES: Second by Mr. Slaton.

Questions?

Seeing none.

All those in favor?

(Ayes.)

CHAIRPERSON JONES: Opposed?

Hearing none. The item passes.

We then go to consent items for information. No request has been made to pull anything off. So we now will go to the next item on the agenda, Global Governance Policy Ad Hoc -- yes.

COMMITTEE MEMBER JELINCIC: On the consent item information, I wanted to raise a -- on the consent items, I don't particularly want to pull it off, but the -- we have some new policy violations. Now, they're reporting type violations, so it's no biggy, but I'm just wondering if, as a practice, when we have new policy violations, whether we ought to, in fact, pull that as a separate item and not necessarily just include it in consent?

So I want people -- you know, I'll throw that out to be thought about. I mean, if it's a violation, maybe we ought to just not bury it in consent.

CHAIRPERSON JONES: Okay. I think it's a good comment. We'll look at it, and see how we deal with it going forward, okay?

Okay. Mr. Slaton now on the next item on the agenda Global Governance Policy Ad Hoc Subcommittee. For that, I call on the Vice Chair of the Subcommittee, Mr. Slaton.

VICE CHAIRPERSON SLATON: Thank you, Mr. Chair. The Global Governance Policy Ad Hoc Subcommittee did meet on November 18th. We received a presentation on the most recent updates to the Global Governance Principles, including a study on Board tenure and the first draft of the introduction and purpose sections of the principles; an update to the legislative and policy guidelines for investments to include support for mandatory disclosure of corporate expenditures for charitable and political purposes.

The subcommittee discussed CalPERS Board representation on third-party organizations and referral of the issue to the Board Governance Committee.

Highlights of what to expect at the next Global Governance Policy Ad Hoc Subcommittee meeting. At the December meeting, staff will present its final recommendations to the Investment Committee on the Global Governance Principles, incorporating feedback received from the Subcommittee members; final recommendation to the Investment Committee on the update to the legislative and policy guidelines for investments; and a discussion and consideration of establishing a permanent subcommittee.

The next meeting of the Global Governance Policy Ad Hoc Subcommittee will be on December 14th, 2015 in Sacramento, California.

CHAIRPERSON JONES: Okay. Thank you, Mr. Slaton.

The next item on the agenda is the Item 6, Ms. Laurie Weir, on Annual Report to California legislature CalPERS Emerging Manager Five-Year Plan.

INVESTMENT DIRECTOR WEIR: Good morning, Investment Committee members. Laurie Weir, Targeted Investment Programs.

This agenda item requests Investment Committee approval to forward the year three report on CalPERS emerging manager five-year plan to the California legislature. The enabling statute requires CalPERS to submit an annual report by March 1st of each year through 2017 with a final report going to the legislature by January 1st, 2018.

This third year report covers from July 1, 2014 to June 30th, 2015. All but one of the workstreams in the plan is either complete, or work will be ongoing throughout the five-year reporting period. In several workstreams where the initiative has been completed, staff has engaged in additional efforts to make further progress and improvements. Most notably during this reporting period, CalPERS established a new industry leading Manager Transition Program.

Over the course of the next five years, the Manager Transition Program will commit up to $7 billion to transitioning managers to approximately 15 transitioning managers with continued commitment to emerging manager programs of approximately $4 billion. The combined capital commitments for Emerging and Transitioning Managers is up to $11 billion between now and June of 2020.

Other highlights of the year three report include: Establishing semiannual performance reporting for emerging managers in the total fund report; completed restructuring of global equity's Emerging Manager Program;

committed new capital 200 million to private equity and 100 million to real estate's Emerging Manager Programs.

Significant improvements were made to the Investment Office website, including enhanced information on Emerging Manager Programs, and continued improvements to our investment proposal submittal process.

CalPERS hosted a roundtable discussion in collaboration with the Women Equity Investor Network, and CalPERS hosted the New America Alliance 2015 national tour here at CalPERS Headquarters.

Staff participated as featured speakers at over a dozen conferences, and CalPERS was highlighted as a leader in investment with emerging managers at a White House meeting held by President Obama on the utilization of diverse asset managers.

The Investment Office held its first ever Emerging and Diverse Manager Day in October of 2014. And, of course, since that time, CalPERS hosted the second Emerging Diverse and Transition Manager Day September 9th of this year and that will be reported formally in next year's report to the legislature. These are just a few of the highlights of our efforts under the five-year plan.

Looking ahead, staff anticipates reporting on the final workstream to evaluate and establish criteria for new capital to Emerging Manager Programs in year four of the five-year plan. That ends my presentation. Happy to answer questions.

Thanks so much.

CHAIRPERSON JONES: Okay. Thank you for the report.

Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman. And I think Ms. Weir just answered one of my questions. And it had to do with -- I was glad to see the inclusion of establishing criteria for new capital. And I wanted to just kind of get a sense of how far along we were in getting these initiatives in place. So thank you for having us look forward to that in year four.

My question also had to do with, you know, just as we do our emerging manager's selection, and particularly around the more recent discussions around private equity. And I'm just curious as to, particularly with this asset class where we don't have necessarily long track records with managers, if we're going to try to streamline or at least make consistent criteria? Are we going to look at that somewhat differently or -- I guess, I'm just trying to get a sense of how we're looking at that within the context of this program.

INVESTMENT DIRECTOR WEIR: Sure. So I think you're referring to the selection criteria --

COMMITTEE MEMBER YEE: Yes.

INVESTMENT DIRECTOR WEIR: -- for emerging managers, am I right?

COMMITTEE MEMBER YEE: Yes.

INVESTMENT DIRECTOR WEIR: Okay. The selection criteria manage for emerging managers is largely the same as with any manager. Where it differs is we would typically see a robust institutional investment track record with an established manager. Where we typically don't have that with an emerging manager, what we do is we look very carefully, and we expect them to have established a track record with high net worth individuals, friends and family, foundation investments. We typically would not invest in a platform that does not have a demonstrable and attributable track record of some kind.

COMMITTEE MEMBER YEE: Okay. All right. That's helpful. Thank you.

CHAIRPERSON JONES: Okay. Thank you very much.

Ms. Taylor.

COMMITTEE MEMBER TAYLOR: I wanted to -- thank you, Mr. Chair. I wanted to thank you for the report. This is -- this is very good. And I'm extremely excited to see your work in establishing the diversity in the Emerging Manager Program. And it looks like it's very well entrenched in the program now. So I'm very happy to see that. And I'm very pleased to hear about the successes of the program, so congratulations.

INVESTMENT DIRECTOR WEIR: Thank you.

CHAIRPERSON JONES: Okay. Thank you.

Yeah. Before we entertain a vote on this item, we do have a request to speak on this item. Mr. Michael Ring if you'll come forward, take a seat at the -- on the -- on your right.

MR. RING: Good morning, Mr. Chair, members of the Board. Thank you for the opportunity again. Michael Ring with the Service Employees International Union. As you know, we have a couple hundred thousand participants in the fund. It's always a pleasure to have the opportunity to share a couple of words with you. You'll have to put up with me probably twice today, mostly on Laurie's subject matter. Sorry, Laurie.

So I just wanted to thank the CalPERS, the staff and the Board, for their leadership in this area. As you know, our President, Mary Kay Henry, released a letter, which many of you received in August, about the importance of diversity in the capital markets, in particular in the public pension fund world. And you guys are leaders in helping to reach some of the objectives that are laid out in the letter. And therefore, we look at ourselves as partners trying to join into the work that you're doing.

In particular, we appreciate the incorporation of diversity into all aspects of your work including in this space. In working with emerging managers, we really do believe that for funds that have a long-term horizon, like CalPERS, or to quote my friend Anne Stausboll, our funds in perpetuity, it's critical that we develop the widest talent pool possible in all areas of this work in order to successfully meet our goals, and that means having a very diverse base of people who manage assets. So thank you for the work you're doing and we look forward to continuing to partner with you in this and other areas.

CHAIRPERSON JONES: Okay. Thank you very much.

And I just want to echo the comments about thanking you for being a trailblazer in this space. And we continuously receive very positive comments from the work that you're doing in this area. So keep up the good work.

And with that, we'll now call for a motion on this item.

COMMITTEE MEMBER TAYLOR: So moved.

COMMITTEE MEMBER YEE: Second.

CHAIRPERSON JONES: Moved by Ms. Taylor, second by Ms. Yes.

Questions?

Seeing none.

All those in favor?

(Ayes.)

CHAIRPERSON JONES: Opposed?

Hearing none. The item passes. Thank you.

We now will move to Item 7a, Revision of Private Equity Program Policy, second reading.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you, Mr. Chairman. Good morning. Wylie Tollette, CalPERS Investment Office staff.

Item 7a is the second reading of the revised investment policy for private equity. As outlined in the agenda item, the edits to the private equity policy since the first reading are for clarification purposes only.

Following the first reading last month as well as suggestions from the Committee, staff has made several proposed edits. Those edits are outlined on the first page of the actual agenda item. In particular, you'll notice on page one of the policy, which is attachment one in your materials, proposed text red-lined under the strategic objectives section, this was a change suggested by Board Member Mathur last month.

Staff agrees these proposed changes are consistent with our overall effort to eliminate vague and untestable language from all the investment policies. I would emphasize that no changes to the benchmark or to the consideration of risk in our private equity program are being proposed with this policy.

The benchmark continues to be the FTSE U.S. two-thirds FTSE All World one-third plus 300 basis points lagged one quarter -- that's kind a mouthful --

(Laughter.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

-- as detailed in the Total Fund Policy, as we discussed at multiple workshops over the past year. Our portfolio priorities project is considering all of the benchmarks in the fund as it -- as we always do leading up to the next asset liability management exercise in 2017.

Risk is, of course, a dominate consideration within all of the asset classes. And I would highlight that Section B of the actual policy investment approaches and parameters on page two is almost exclusively about manager risk. Management of investment risk is also an appropriately and explicit part of the strategic objective of the total fund investment policy.

Next on page two of seven of the policy, there is some text highlighted in blue that was also proposed for removal, again with the idea that the language was vague and untestable. However, a member of the Committee has raised the question about whether to strike this language or keep the language in the policy. Staff is open to Committee direction on that element.

Finally, in the presentation of this policy last month, Mr. Jelincic raised a question around including specific policy elements on defined benefit plans and fee disclosure. Ted has some comments for the Committee related to those two topics.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Thank you, Wylie. So on these two topics, as we noted in our agenda, we'd be providing some discussion today. I think with respect to the defined benefit plan, whether or not to include a policy provision in our private equity policy with respect to the defined benefit plan of portfolio companies, private companies, the treatment of defined benefits plans, first of all, I just want to say I, and our team, share, you know, the policy concerns around defined benefits plans as a policy topic.

We think having considered it, rather than considering placing it in the private equity policy, we think the better avenue to address this concern is part of our -- is with our manager expectations work. And what we would propose upon direction from the Committee is that we would engage with our external partners in private equity to ask some questions as part of our manager expectation ESG work around how they treat the defined benefit plans, to the extent that they exist within the portfolio company universe that they have, and that we would report back as we will in our manager expectation work around the results that we find from those inquiries.

I think what we will find is that it really is a very fact specific and specific to portfolio company one by one inquiry, and it may be hard to generalize in just one sentence or two sentences in a policy what we find. But we think that work is important and will be a good level of inquiry and we'll report back regularly to the Committee.

Secondly, in terms of fee disclosure, that's certainly something we spend quite a bit of time on in private equity and in our workshop, and think it is a good concept to consider for the private equity policy going forward. We believe it's premature to craft language today. As we know, there is much evolving in private equity around fee disclosure. We ourselves at CalPERS will be receiving much information over the course of the year with the heightened disclosure that we're requiring.

ILPA, as we know, hopefully will ratify in January, just a month from now, the template that we've discussed so often. In addition, we expect there may be some regulatory activity over the course of the year. So it's all a long-winded way of saying, I think, next year, when we review the Private Equity Program and its policy, we think that would be an appropriate time to revisit whether or not there's more clarity around the policy language that would be appropriate at that time.

CHAIRPERSON JONES: Okay. Thank you. We do have a couple of questions on this one.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: On the defined benefit plan, I still believe we ought to write it into the policy. We ought to put the whole world on notice that we are not willing to de-fund private -- or defined benefit plans. Making it part of the expectations, we'll have a conversation with the GP, but it's not a constraint that exists, because it's not in the policy. So I'm very concerned about that.

You know, there's a certain hypocrisy in saying we will define our -- we will fund our defined benefit plan by de-funding yours. But I also can count votes and it's not there, but I find that disappointing.

I do have an amendment that I would like to make in the investment constraints. And I will take the guidance from the Chair whether to do that now or wait until further in the discussion.

CHAIRPERSON JONES: Yes. Why don't you wait till -- you know, and I'll call on you to make the motion.

I won't forget you.

COMMITTEE MEMBER JELINCIC: Okay. Just don't -- just don't call the question before I get a chance to make it.

CHAIRPERSON JONES: Okay. Yeah, we -- also, we have public speakers requests on this item. Okay. So with that, Mr. Lind.

COMMITTEE MEMBER LIND: Thank you. On the defined benefit plan issue, I certainly, as a recipient of a defined benefit pension plan, in the private sector, I agree with J.J. And maybe eventually I think we do need to get there as a matter of policy, but I support staff's sort of incremental approach on this, and think that putting it in the manager expectations work is a good first step. And we'll kind of see where that goes and how broad an issue it is, and look forward to hearing back on that.

I was the Committee member who in a briefing raised the issue about page two of seven point number four about the blue strike-out language. I believe that should remain there. I don't think it's vague. I think it's kind of important, especially with all of the focus on fees and transparency and aligning with limited partners interests and all of that. I just think it makes sense to leave that in.

So again, Henry, I don't know if you want me to make that as a -- save that as a motion for later or how you'd like --

CHAIRPERSON JONES: Save it.

COMMITTEE MEMBER LIND: Okay. Thank you.

CHAIRPERSON JONES: So we hear all the speakers and we'll come back to it. Okay. Thank you.

Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you. Well, I pretty much wanted to echo what Mr. Lind just said. I think your approach with respect to the manager expectations and starting by asking some questions is a sensible way to begin the conversation. I don't think we as a Committee have had a full-fledged -- or with staff have had a full-fledged conversation about this issue on defined benefit privatization of defined benefit plans and -- or the conversion of defined benefit plans. So I think that's very sensible.

On the fee disclosure, I think that's also a sensible approach to revisit that next year after we've had a little bit more time for some of these issues to settle in the marketplace, especially the regulatory environment.

With respect to Mr. Lind's suggestion on B.4, it is a bit of a deviation from the other items where it's just list the risk and not the potential mitigations. And I just think -- I don't necessarily disagree with him, but I think it's something we need to think about whether we want to consider listing mitigations for others, how exhaustive should that list be.

Maybe it's -- maybe it makes sense to have it just for one where we think there's really something to say about it, but -- so I guess I don't have a strong view, but I just wanted to think about it from a broader perspective.

Thanks

CHAIRPERSON JONES: Thank you.

Ms. Hollinger.

COMMITTEE MEMBER HOLLINGER: Yeah. Thank you.

I also agree with J.J. I think it's -- there's a potential conflict there. And the only thing I would want to -- I'd want to get input from fiduciary counsel that the -- and I understand your concern to want to put it in our manager expectations, but I would want just to hear from fiduciary counsel on that to make sure. By the way it's structured now, it's not diluting our fiduciary duty to our stakeholders.

CHAIRPERSON JONES: Thank you.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: This is not my amendment yet. On the strategic objective, I really think that maximizing risk-adjusted rate of returns belongs in that policy. I mean that is why we are in this asset class. You pointed out that Ms. Mathur suggested that it be dropped. I actually went back and looked at the transcript, and what she objected to was our desire to be a premier private equity manager was being put on the same basis as the risk-adjusted return.

I have no real desire to necessarily be the world's most desirable limited partner. In fact, I would tend to run the other way, but I think the maximizing risk-adjusted rates of return is what this asset class is all about. And so I think that that should be put back in.

And if, at some point, you want a motion on that, I will be happy to do it, but...

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you, Mr. Jelincic. Staff has no objection to continuing to include that risk-adjusted return language in the policy.

COMMITTEE MEMBER JELINCIC: Will the Chair direct them to include it then?

CHAIRPERSON JONES: I would like to have it in a motion, because I want to finish the discussion first.

COMMITTEE MEMBER JELINCIC: Okay.

CHAIRPERSON JONES: So now we have a request to speak on this item. Mr. Michael Flaherman from UC Berkeley.

MR. FLAHERMAN: Good morning. I'm Michael Flaherman. I'm a visiting scholar at UC Berkeley. I'm a former member of the Board, and I'm a beneficiary of the fund.

I have four things I wanted to speak on very quickly. The first is the DB issue. I want to call your attention to an important legal case on this issue that has arisen in the last couple of years, which the exact name I don't know, but its Scott Brass versus Sun Capital.

The essence of the case was that Scott Brass was a portfolio company of Sun Capital, and Sun Capital terminated the defined benefit pension plan. Scott Brass -- the Teamsters who represented the Scott Brass employees sued. And they argued that essentially the court, under ERISA, needed to look at Sun Capital and Scott Brass as essentially a conglomerate as one entity.

And the reason that that matters is that if you are viewed as a conglomerate, the assets of the parent, in this case, Sun Capital, but really the Sun Capital fund, meaning ultimately if you were an LP in Sun Capital, you would be liable for the unfunded liability of the pension plan.

It was litigated and the court found in fact that Sun Capital was liable. It was appealed. The court of appeal upheld the trial court. Sun Capital appealed to the Supreme Court, and the Supreme Court declined to take the case.

This, I think, is really important for this issue, because essentially there is a very strong precedent out there now that says that if a pension plan is terminated and there is an unfunded liability in the pension plan, the liability can be put back onto the LPs, which is you. So I think that puts the whole fiduciary issue in a very different light.

The second thing I wanted to bring up was to just support the comments that were made about the purpose of the program. I really think that the reason that you're in private equity is to earn a premium over public equity. And I think that the way that has been proposed to be rephrased -- although, it sounds like there's been a change of perspective on whether it needs to be rephrased is way.

But the way it's been phrased, actually it sounds like all you're really trying to do is sort of do infinitesimally better than public equity, but -- which I don't think is why you're in the business of being in private equity.

Third, on page two of the policy, it talks about leverage. And It says the increased volatility risk posed by the existence of non-recourse debt at the underlying investment level. So the policy only talks about non-recourse debt. There's significant recourse debt in your portfolio as well. And I think it's important actually that you recognize that, acknowledge it, and I also think actually that you should probably have a report brought back to you about the recourse debt. It's in the -- it's in the fund financial statements.

And lastly --

CHAIRPERSON JONES: Excuse me. We had put you up for three minutes, but I'm going to allow another two minutes, so --

MR. FLAHERMAN: Oh. Thank you.

Well, I'll take a moment just to explain what -- thank you. The recourse debt is a rapidly growing phenomenon in private equity where the GP pledges the commitments of all of the LPs as collateral, and goes out and gets a loan from a bank, okay? And these loans actually are called different things actually.

Subscription line credit is a very common name for them. You can see on the web the big banks marketing these to private equity firms, so you know it's out there just from that, but then you can see them in the fund financial statements.

The reason why it really matters in particular is because that will be -- the repayment of that will be called from you at the worst possible moment. It will be called from you in a financial crisis when liquidity is most precious. So I think that's an important issue that you want to pay attention to.

And then lastly, the fee transparency issue, I would voice support for the idea that requiring fee transparency is a good idea. I think it's actually kind of hard to argue against it. I mean, I understand the idea of a measured approach. But as just sort of a commercial matter, it seems to that it's sort of -- it's hard to argue that you'll make more money over time by letting people charge you undisclosed then you'll make by requiring them to disclose what they're charging you.

So those are my comments. Thank you very much.

CHAIRPERSON JONES: Okay. Thank you, Michael.

Mr. Lind.

COMMITTEE MEMBER LIND: Thank you. I was just trying to queue up for a motion. I don't know if it's the right time or not.

CHAIRPERSON JONES: Well, I had indicated that Mr. Jelincic would be the first to make a motion, since he held at my request.

COMMITTEE MEMBER LIND: I'll defer.

CHAIRPERSON JONES: Thank you.

(Laughter.)

CHAIRPERSON JONES: Okay. There you go.

COMMITTEE MEMBER JELINCIC: Okay. I'm on.

The -- I may have a second one if somebody else doesn't pick up the risk adjusted. On Appendix 3, which deals with the constraints. I would like to move that we add a provision that says, "CalPERS will not sign any new limited partnership agreements that does not require the general partner to disclose as part of the agreement any and all types of fees, carry, discounts, rebates, and any other forms of economic rent the general partner or related parties may charge".

CHAIRPERSON JONES: Okay. So that -- and you're moving -- modifying and then you're moving the whole policy for approval?

COMMITTEE MEMBER JELINCIC: I'm moving just this amendment.

CHAIRPERSON JONES: Okay. Yeah. So you -- are you going to go forward and approve -- move the whole policy?

COMMITTEE MEMBER JELINCIC: Well, I think ultimately we're going to have a motion to move the -- adopt the policy as amended.

CHAIRPERSON JONES: Yeah, but I don't think we can amend --

COMMITTEE MEMBER JELINCIC: Okay. Then --

COMMITTEE MEMBER MATHUR: Move the policy with the amendment.

CHAIRPERSON JONES: Yeah.

COMMITTEE MEMBER JELINCIC: Okay. I'll move the policy --

CHAIRPERSON JONES: With that amendment.

COMMITTEE MEMBER JELINCIC: -- with this amendment and recognizing subsequent amendments are coming.

CHAIRPERSON JONES: Okay. So it's been moved by Mr. Jelincic with the -- this policy has been moved with the amendments that he so identified. So do we have a second for that?

COMMITTEE MEMBER LIND: I would second it for a discussion.

CHAIRPERSON JONES: Okay. It's been seconded by Mr. Lind.

Mr. Lind.

COMMITTEE MEMBER LIND: And -- look, I get the sediment. We've had a lot of discussion around this. And I've talked to several Board members about it, but I think, as Mr. Flaherman described it as a measure -- as a measured approach I think is -- I'm comfortable with moving that way, but I'd be interested in hearing what other Board members think.

CHAIRPERSON JONES: Okay.

COMMITTEE MEMBER JELINCIC: Do I get to speak to my amendment at some point?

CHAIRPERSON JONES: Mr. Slaton.

VICE CHAIRPERSON SLATON: Okay. So this -- we're speaking on the amendment.

CHAIRPERSON JONES: Yeah.

VICE CHAIRPERSON SLATON: So I don't think there's anyone on this Board that is not in favor of full fee disclosure. If we had our druthers, that's exactly what we'd want, every fee, the way Mr. Jelincic described it. And maybe there's a few other ways to describe it, because people who do financial deals are pretty good at getting creative to say, well, this doesn't fall in those categories that were enumerated in your policy.

But that being said, I've come to the conclusion that we do not control the private equity market. It would be nice if we did, but we don't. So I think that staff's approach, kind of measured approach to this, to work with other partners, to work on the regulatory scene, to arrive at the same point that we're trying to arrive at I think serves us better, because I'm concerned that there may be some partners that we would like to do business with irrespective of this fee issue, and that we would preclude those transactions from taking place in the short-term.

So I think just -- I think we as a fund are better served by continuing to work on the issue, but not for this Committee to prescribe it at this moment in time, because I think it ultimately would be respective. So I'll be voting against the amendment.

CHAIRPERSON JONES: Okay. Mr. Costigan.

COMMITTEE MEMBER COSTIGAN: Thank you, Mr. Jones. So, Mr. Jelincic, I agree with you on transparency and disclosure. I guess the question I really have, Mr. Jones, is Mr. Jelincic you made a large motion on a number of items. It's whether or not we could go item by item, because I think Mr. Slaton raises some excellent points. But I do believe, or I'd like more staff direction, is which of the items in your large motion could we, in fact, do to move towards the goals, because I'd hate to almost see this go down in defeat, because I do think more information is important.

And I think -- do think from the standpoint that among our private equity partners, more disclosure. Even if you read among the placement agent items, I sometimes find the calculations to be rather amusing as I may raise in one coming up, that they seem to minimize the number of hours that they're working to make sure that they're disclosing as little as possible, and I would be more for transparency. But I am concerned that the way you made your motion it's kind of an all or nothing.

Thank you, Mr. Jones.

CHAIRPERSON JONES: Okay. Thank you.

Ms. Hollinger.

COMMITTEE MEMBER HOLLINGER: Yes. I also agree with full transparency, but one of my concerns is, as Mr. Slaton and Mr. Costigan suggested, that I don't want to price us out, make it so restrictive to deal with us that we lose this asset class in our portfolio, because I recognize that the outside returns that we've seen over the years goes to our ability to pay benefits.

So similar to Mr. Costigan, I'd like to see what staff feels they could do, because I also think the industry is getting pressure also on transparency, and I recognize this is evolution, not revolution. So as to what you feel you -- would be workable and wouldn't actually throw us out of the marketplace for this asset class.

CHAIRPERSON JONES: Okay. Ms. Taylor.

COMMITTEE MEMBER TAYLOR: So I also want to echo my co-board members. I do support very much transparency on these fees. And I also want to remind everyone that we're sort of in the forefront talking about this, and getting it out in the public. As Mr. Costigan and Mr. Slaton said, I'm concerned that we don't have control over the private equity. And I'm concerned that we would not be able to continue relationships with those folks. And I understand you want to wait until some of the legislation passes before we take a stance.

Maybe there is a way that we can word this differently so that we could include some sort of education or investigation into how we put this in our policy at a later date maybe. That would be my suggestion.

But again, I couldn't agree more, we need transparency on those fees. So I would be voting no on this particular -- the way it's worded. So maybe we can come up with something else.

CHAIRPERSON JONES: Okay. Mr. Jelincic, you wanted another --

COMMITTEE MEMBER JELINCIC: Yeah, I actually --

CHAIRPERSON JONES: Push your button.

COMMITTEE MEMBER JELINCIC: Okay. I actually want to speak to my amendment. This amendment does not limit the GPs from charging us whatever they want. This does not limit staff's ability to negotiate what kind of fees we're going to pay. All this amendment does is say before we enter an agreement, you have to tell us what kinds of fees you're going to charge us. It doesn't limit how much you charge us. It doesn't limit how we negotiate fee sharing. It only says you have to tell us what kind of fees you are charging.

Now, there may be some GPs who don't want to tell us what they're going to charge, and I have to question why we would want to enter into any agreement with somebody who says I'm reserving the right to charge you fees that I'm not going to tell you about.

So it doesn't prevent them from charging us. It doesn't prevent staff from negotiating. It only says we will not enter an agreement unless you agree to tell us up front the types of fees you're going to charge us. And because there are -- and recognizing Bill's point that they tend to have some pretty sharp lawyers. That's part of the reason I included any other forms of economic rent. It would be kind of hard to figure out some fee that doesn't fall under economic rent. So I would urge the Committee to vote for the amendment.

CHAIRPERSON JONES: Okay. Mr. Lind.

COMMITTEE MEMBER LIND: I'm going to offer a substitute motion, which would -- because I think I know where this one -- J.J. is going to go. So I'm going to offer a substitute, which is that we approve the policy with the following two amendments:

One, that we retain the language about -- around risk-adjusted rate of return and the strategic objective; and, then two, that we retain the blue-lined language under structural, which doesn't totally deal with what Mr. Jelincic is raising, but it at least keeps language in there that discusses fees and, you know, aligning interests with the partners.

COMMITTEE MEMBER MATHUR: Second.

CHAIRPERSON JONES: Okay. It's been moved by Mr. Lind and seconded by Ms. Mathur.

Discussion on the amended motion?

VICE CHAIRPERSON SLATON: Would you repeat that motion?

CHAIRPERSON JONES: Yeah, would you repeat it.

COMMITTEE MEMBER LIND: Okay. The motion is to adopt the policy with the following two changes:

Retaining the reference to risk-adjusted rates of return in the strategic objective; and then, secondly, retaining the blue-lined language under B.4, which talks about mitigating -- mitigated by among other things structuring fees, incentive payments, et cetera, et cetera.

CHAIRPERSON JONES: Okay. So it's been moved and seconded.

Discussion on the amendment?

Mr. Costigan, is this on the amendment?

COMMITTEE MEMBER COSTIGAN: I'm trying to figure out my question. Come back to me.

CHAIRPERSON JONES: Okay. Ms. Hagen.

ACTING COMMITTEE MEMBER HAGEN: Yes, I was wondering if we could hear from the staff perhaps on if there is a place in the policy where you might address what a couple of Board members have raised in our discussion. I agree with the recent motion, but I think what Mr. Jelincic is suggesting, and I agree, is that there be a little bit more specific language around, you know, as a matter of policy that we require disclosure. And while the language that Mr. Jelincic proposed sounded more to me like contract language rather than a policy -- I that's what folks are reacting to -- perhaps the staff can recommend some language or a location in the policy where we might be able to add that.

CHAIRPERSON JONES: Okay. And I am going to call on staff in a minute, as soon as I get through these Board members' questions.

Mr. Costigan, you're still up there, so what is your --

COMMITTEE MEMBER COSTIGAN: Okay. I'll tell you.

So this may be also a good one for staff. So one is what's -- in response to Mr. Lind's motion, what is it that is different that we don't already require, back to also Mr. Jelincic's motion?

So if he's going broadened, what do we currently require the managers to disclose to us, because, I mean, I think part of it is that level setting field. But I still have a bigger concern, and it will go to both motions, one is I don't understand even from the standpoint anybody that doesn't want to disclose this, we shouldn't be doing business with.

And from the standpoint that if Mr. Lind's is a first step, I would certainly hope Mr. Jones that we come back at a later date to ask for more disclosure on fees. But I would like at least a level set as to what Mr. Lind is proposing, what is different than our current policy?

CHAIRPERSON JONES: Okay. Mr. Jelincic, is this on the amended motion?

COMMITTEE MEMBER JELINCIC: Yeah. Yes, it is.

CHAIRPERSON JONES: Okay.

COMMITTEE MEMBER JELINCIC: The -- I would actually like to amend the amendment to put -- but what I want to do is put my motion back on the floor, because I really would like to see it come to a vote. It does not control the contract. It simply says you have to tell us before we sign the contract what types of fees you're going to charge. That's not contract language. That's policy language.

It doesn't limit what you charge us. It doesn't limit how you calculate it. It doesn't limit how staff negotiates fee spits. It simply says if you're going to charge us a fee, you've got to tell us about it.

And I would -- so I will amend -- move to amend the amendment, because I really would like a vote on that particular issue.

CHAIRPERSON JONES: Well, before we -- before I ask for a motion on the amendment of the amendment, I would like to have staff respond to the number of issues that were raised by how we separate some of these issues what may be included this time, what you may need more time to come back and give us an update on, et cetera, because a lot of issues were raised here.

And at the same time, I'd also like to have Andrew Junkin, our Board consultant, comment. And I know this is a private equity, but he is the Board's general consultant. I'd like to hear his comments too on this issue.

Mr. Eliopoulos.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Sure. So let me start with the easier two. In terms of the strategic objective change, and the section B.4 change to include the risk mitigation language, those are judgment calls by the Investment Committee. We don't think substantively including one or the other changes the way the program is operated at all. So it's healthy for the committee to weigh all of the policy implications as well as perceptions around what words you choose or not choose and come to conclusion one way or not to include that language or not. Substantively, it makes no difference in how the program is run.

I think on the question of fee disclosure, as I said in my original remarks, I think our approach would be to take the year and learn more about this laundry list of fees that have been alluded to here today and craft policy language, at that time, when we have the fullness of the year of experience of the disclosures that we're already receiving, and we have the year to see what regulations may or may not be imposed and we have some more experience.

I think the danger of crafting language on the fly here today is that it will prescribe the way that the program is operated. So if there is a word or two words or three words in the laundry list that have been added - I think of, for instance, the language around economic rent - staff is tasked with implementing the policy by its terms. And we need to make sure that we have a good understanding of the language.

I think what the -- what really is before the Committee is whether or not you'd like to take up drafting disclosure language this month in February or in one year. That's really the question. In terms of what we're actually doing, what the program is actually doing, I think as the Committee is well aware, we have already effectively implemented the requirement that our general partners disclose to us all of the fees that are, you know, generally described in the what we know as the ILPA template.

So we are asking for and demanding disclosure of all of the fees that the general partner is charging, not just to the limited partners, but as well as to the portfolio companies. I think the language that I heard verbally here today that would take more work is around the notion of any other arrangements that take economic rent away from the limited partners, things like rebates or discounts on service fees. That's an area that is evolving still in terms of disclosure practice and is not currently captured in the ILPA template today.

So really the choice between the Committee is to take up the codifying of these requirements this month or take it up a year from now. Our suggestion is that we take it up a year from now, but that's really up to the judgment of the Committee.

CHAIRPERSON JONES: Okay. Thank you.

Andrew.

MR. JUNKIN: Thank you. Andrew Junkin with Wilshire Consulting.

Even though Wilshire didn't provide an opinion letter, I feel sort of like an old hand at this. I've been around for the last two policy review projects. The last one Sort of felt like my baby, and so this one I feel involved in as well.

On the two issues that you're debating, which I think are great issues for this Committee to consider the risk-adjusted return issue and the fee issue, I'll address each of those. On the risk-adjusted return issue, to me it's clear. No one is talking about having a risk-doesn't-matter approach to private equity. That would be foolish, but risk-adjusted returns can mean many different things.

And if we're not going to specify how we're going to measure it, if we're going to use Sharpe Ratio, if we're going to use alpha, if we're going to use information ratio, we may end up driving three different sets of behaviors. And so if we're not clear about which one we use, I'm not sure you're going to fully understand all of the knock-on effects. So that may be -- that may speak simply to Ted's point about we may not want to address language like that on the fly.

Clearly, the benchmark that you have public equity. I won't say the whole mouthful that Wylie did earlier. Public equity plus 300 says we have to make more than just immeasurably more than public equity. That benchmark is not changing. If it were to ever change, you all would be the ones that would vote on it. And I would sit here and tell you do not change that benchmark below plus 300. At that point, I don't think private equity is worth it.

So I think there are some measurement issues with risk-adjusted returns. Maximizing also sounds like aspirational language. And I think I've just described some issues about how it's not testable. And early on in the policy review project, I think staff explained to the Board, we want to remove aspirational language and we want things to be testable. I think this contradicts that in some ways. Having said all of that, it's a good goal to have, right? Whether it's in the policy or not, this is how the program operates.

And it certainly is risk-aware. We spend tons of time talking about the risk of private equity when it comes to the asset liability workshop. And I'm going to -- this is precisely where the Investment Belief that risk is multi-faceted comes into play. When we try to say risk is only volatility, when it comes to private equity, we miss 90 percent of the risk. It's something that we can measure, but it's wrong, and that's a problem.

Fees. To Mr. Jelincic's original amendment before the subsequent amendment before the -- anyway. If the question is tell us all of the fees that you will charge us, or you may charge us, my fear is that you're going to get back a laundry list of every single private equity fee possible, and it becomes meaningless.

So I don't know how to address that. But again, I think that speaks to Ted's point about trying to deal with language on the fly. They might just check the box that says, yes, we may charge that, we may charge that, and you don't end up with anything useful.

I think driving towards fee transparency is critical, and it is something this organization is committed to. I just don't know that -- how to get the right language to deal with it.

CHAIRPERSON JONES: Okay. Thank you.

Okay. I think we're going to bring this to a close in a minute.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: I just want to make sure at some point I get a vote on my amendment to the amendment, which was the original amendment.

CHAIRPERSON JONES: No, he hasn't made it yet, because I -- we were talking to Mr. Lind's amendment.

Yeah. Did we get -- yeah, we got a second. Yeah, Priya seconded Mr. Lind's.

Okay. Mr. Costigan, is this to Mr. Lind's amendment?

COMMITTEE MEMBER COSTIGAN: Yes, I have a question.

CHAIRPERSON JONES: Okay.

COMMITTEE MEMBER COSTIGAN: I just want to make sure I know what I'm voting on. What will the language now say, for example, on strategic objective?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: I believe, Mr. Costigan, that it will say, "The program's strategic objective is to maximize risk-adjusted rates of return and enhance the equity return to the fund".

COMMITTEE MEMBER COSTIGAN: So we are going to strike just, "While enhancing the CalPERS position as a premier private equity investment manager, the program shall be managed".

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

That's right. That's my understanding of the proposed amendment.

COMMITTEE MEMBER COSTIGAN: Okay.

CHAIRPERSON JONES: Okay. Mr. Slaton.

VICE CHAIRPERSON SLATON: So it's getting a little confusing, I think. So what I'm wondering is, is -- I'd sure like to separate these things out. What I'd like to -- trying to figure out how many no votes do I have to make before I get back to voting the policy in as it reads today, as has been recommended by staff. Because I think for us to draft on the fly I think is a dangerous move. I don't think it's appropriate. We're not the ones who sit at the table trying to negotiate private equity deals. So I don't want to wordsmith from the dais.

So I guess what I'd do -- what, I have to make two no votes before we can get to another motion or would you --

CHAIRPERSON JONES: Yes.

VICE CHAIRPERSON SLATON: Are you entertaining another substitute motion?

COMMITTEE MEMBER JELINCIC: May I officer a way of simplifying this. Let's just divide the questions, and take the three amendments -- as separate votes, and then on the policy --

CHAIRPERSON JONES: No, I think what we're going to do, we're going to go ahead and -- unless you're making another substitute motion, go ahead and take a vote on Mr.

Lind's amendment. Okay.

COMMITTEE MEMBER JELINCIC: Let me ask if Ron's amendment gets adopted, is that adopting the policy as amended or what's it putting on the table?

CHAIRPERSON JONES: Yes, it's adopting the policy as amended by -- yeah.

COMMITTEE MEMBER JELINCIC: Okay. In which chase, I wish to move to amend the amendment -- or amend the substitute motion or whatever Ron has, to include the language that, "We will not sign any new limited partnership agreements that does not require the general partner to disclose as part of the agreement any and all types of fees, carry, discount, rebates, and other forms of economic rent that the general partner and/or related partners may charge".

CHAIRPERSON JONES: Okay. It's been moved by Mr. Jelincic?

There's no second, so the motion fails.

COMMITTEE MEMBER JELINCIC: Okay

CHAIRPERSON JONES: Now, we're back to Mr. Lind's motion. And it was moved and seconded.

So I'm going to -- you want --

COMMITTEE MEMBER LIND: Can I say one thing?

CHAIRPERSON JONES: Okay. Mr. Lind.

COMMITTEE MEMBER LIND: I just want to say one thing on behalf of my motion. I respectfully reject the notion that this is drafting language on the fly. This is restoring language that was in the previous policy, and the previous draft from last month.

CHAIRPERSON JONES: Mr. Slaton.

VICE CHAIRPERSON SLATON: Yeah. Mr. Lind, I was referring primarily to Mr. Jelincic's wording not yours. But I am persuaded by our consultant's view on this that I'm not sure this is where this belongs. So I think that the modification that just talks about enhancing the equity, you know, that's the overall strategic objective. The rest of it is the how to do it. And the how to do it doesn't belong in the opening paragraph. And in the other one, I think deleting the language is appropriate, because again I happen to always lean toward clarity of language. And all of these are risks that are identified without the solution being identified in the same spot. There is room to do it elsewhere, so I -- given that these are going to -- I'm going to vote against this. I'm hoping to get just the policy approved.

CHAIRPERSON JONES: Okay. So we're going to take a vote now on Mr. Lind's motion.

All those in favor say aye?

(Ayes.)

CHAIRPERSON JONES: Opposed?

(No.)

CHAIRPERSON JONES: So the item passes.

So let's be sure that we -- restate your motion to just be sure that there's communication about that motion. I want to hear it one more time.

COMMITTEE MEMBER LIND: All right. So the motion that I think we just adopted was, under strategic objectives and Wylie stated it how it would come out. If you would say again, Wylie?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Certainly. "The program's strategic objective is to maximize risk-adjusted rates of return and enhance the equity return to the fund".

COMMITTEE MEMBER LIND: And then the second part of it was under B.4, that the language -- and I'll go ahead and read it so it's clear. So after where it says limited partners, we retain the language that says, "...which may be mitigated by, among other things, structuring fees and incentive payments and other key aspects of the business relationship so as to better align the interests of the partners.

CHAIRPERSON JONES: Okay. So that motion passed. Okay. So -- and I think that there are a couple of follow-up items though that I'd like to direct staff that I heard, that we -- you need to come back to the Committee at a later date. And one of them was raised by the public speaker about litigation, regarding -- yes, so I would like you to research that issue and bring that back to the Committee.

And also --

COMMITTEE MEMBER HOLLINGER: Recourse debt.

CHAIRPERSON JONES: Recourse debt. Yeah, recourse debt. That's the other one dealing with the liquidity issue.

So if you could bring back those two clarifications regarding those two, that would be helpful as we go forward.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Thank you. Got them.

CHAIRPERSON JONES: Okay. So that -- you still want to speak. But the motion passes.

ACTING COMMITTEE MEMBER HAGEN: Yes.

CHAIRPERSON JONES: Okay.

ACTING COMMITTEE MEMBER HAGEN: I just had one comment after hearing from staff. Thank you for your recommendations and from our consultant. I just wanted to make one point that I think given the importance of this issue, I don't think that we can afford to wait a year to come back to this and revisit the fees issue. So I heard a reference at some point to February. And on behalf of the administration, I'd like to request February that we revisit that, rather than a year from now.

CHAIRPERSON JONES: And, Mr. Eliopoulos, what is the work schedule addressing that earlier than later?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Well, it would impact the work schedule. So right now what -- I think our preference is to take this up during the annual review of private equity and its policy in November. So don't currently have anything planned for February. I think the point I was making is we could either address it this month or at the next Investment Committee or next -- the next following annual review of private equity. So there's nothing currently planned in the workplan to take that up in February.

CHAIRPERSON JONES: So could you provide the Committee just some framework or the issue and timelines in February, not to complete the research and complete the necessary work that would be bringing back to us for any necessary action anything, but can you give us some guidelines about what you're going to be dealing with going forward in February?

CHIEF INVESTMENT OFFICER ELIOPOULOS: I'm not -- I'm not -- sorry, I don't understand that direction.

CHAIRPERSON JONES: In other words, you said you wanted to review it when the next annual report on private equity. And in order to get ready for that, there's a process that you're going to embark upon, right, to get to bringing this back to us next December. And I'm just saying if you could bring back some -- your thoughts about some timelines, and whether or not it could be done earlier than next December, maybe even in August or July.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Sure, I think we can contemplate that. I just want to make clear the point about the passage of time isn't so much about giving us more time to contemplate this issue or define the issue. It's really to let the experience move forward over the course of the year. As ILPA adopts its disclosure template in January, as we ourselves are receiving much more disclosure and transparency over the course of the year. And as perhaps regulatory actions are taken, I think we'll learn more by the passage of time. It's not that we'll be ignoring the topic or ignoring the issue or need more time to draft language, I think it's much more about having the time for the collection of this new data that we're already receiving to better inform a better policy a year from now.

CHAIRPERSON JONES: Okay. Unless the Committee have a different viewpoint, I'm going to direct staff to include it when they come back for the annual review in December, unless --

VICE CHAIRPERSON SLATON: Is it December or November?

CHAIRPERSON JONES: November. November. Yeah, November. So that's the direction. Okay. Thank you.

That concludes that item. Thank you very much.

Now, we'll move to the next item on the agenda, the -- Item 8, the Business Plan/Roadmap, Investment Office Roadmap Update.

(Thereupon an overhead presentation was presented as follows.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you, Mr. Chairman. Ted and I are pleased to provide the Committee with an update on the strategic planning efforts of the Investment Office as we do twice a year. This includes progress on our Investment Office five-year strategic plan, which we call the 2020 Vision. We'll discuss a few of the key initiatives within our 2015-17 roadmap, as well as some accomplishments from quarter one of this fiscal year.

And then finally, we'll actually provide an update on the close-out of the 2014-2016 roadmap with highlights around that.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: So this slide is familiar to the Investment Committee. We've seen it before, but I like how this pyramid illustrates the sort of relationship between the investment -- or the -- excuse me, the business plans of the different divisions within CalPERS and their relationship to the overall CalPERS strategic plan.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: So that large pyramid at the CalPERS level is supported by individual business plans within each of the programs, and this is the Investment Office Roadmap. As you can see, it starts at the top with the Investment Beliefs, that filters down into our Investment Office mission. That helps us define our roadmap or our business plan. And then that helps direct the core programs of the office, the 11 core programs focused on public and private assets, investment servicing, compliance, risk, performance reporting, total fund. And then finally that translates down into our ongoing work and our operating model priorities.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Five years ago, we -- actually, Joe Dear and Janine Guillot developed this from-to framework. And I continue to find this framework very helpful at examining how well the Investment Office is doing against our strategic priorities.

So when we started the 2020 Vision process last year, we pulled out the from-to statements that Joe and Janine devised back in 2009 and 2010 to basically assess how well we're doing against those things. And as you can see, we've made good progress on some of the elements. Risks are better understood as a key driver of the portfolio and our organization. We have greater total fund focus. We need to continue to drive that collaboration around cross-asset class approaches. We have an increased knowledge of the costs being incurred. It's not a perfect level of knowledge, but we have much better information around that, and we've made significant progress on our operating model in the systems and sort of the plumbing within the Investment Office.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: The gaps that we've identified where we still have work to do, as you can see those gaps highlighted in these two slides, those continue to really drive our resource allocation and our project priorities.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: The 2020 Vision was something that your senior Investment Office team helped build over the course of the last year and a half. And the key elements of that plan are highlighted here on this slide. It's really around simplifying the investment portfolio, our organizational structure, focusing on risk, cost and complexity, and improving a level of collaboration within the Investment Office to focus on the total fund decisions that make the most difference in the long-term rate of return.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Focusing in on the 2020 Vision, the -- excuse me. The refined strategic objectives are highlighted here. This is the mission and vision that we outlined and helped develop with your senior team. And you can see -- I'll read it quickly, because I think it's -- well, I think we're quite proud of it and I think it really helps direct the activities of the office. "To manage the CalPERS investment portfolio in a cost effective, transparent, and risk-aware manner in order to generate returns to pay benefits".

And the simplicity and clarity of that mission are very important. That's what we are focused on doing. And within the vision, we intend to operate with a focus on repeatable, predictable, and scalable portfolios and practices. We seek alignment of interests with our stakeholders, our business partners, and ourselves. We use clearly articulated performance, risk, and cost metrics. And finally, our business and investment activities are supported by a solid platform of effective risk management and controls. That's our vision.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

These are strategic objectives that really help sort of support the development of specific roadmap initiatives. These strategic objectives are actually supported by a total of 36 roadmap initiatives this year. And the majority of those are really cross-asset class, meaning they're representatives from multiple areas of the Investment Office to help drive progress.

They're led by 26 individual project leads. And we have over 130 staff within the Investment Office participating on these different initiatives. And that's in addition to their day-to-day core workload. So we're essentially -- one of the challenges with driving change is that you essentially have to re-pave the road while you're driving on it. And we believe we're effectively accomplishing that halfway through this particular roadmap.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: We also have created a small team that works effectively to manage the projects. With 36 individual projects, there's obviously going to be resource constraints and conflicts. And so managing that series of projects that -- those 36 initiatives, almost as if they were a portfolio, is something that we're now taking more time and focus around. And the projects -- the status of those projects, this program management effort within the Investment Office helps make sure that all those projects stay on track and reports effectively to our internal management Committee.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Here is our operating model. And this slide should look very familiar to the Investment Committee. What you can see, I think the key points here, is that the boxes that are in red are sort of what we think are our higher risk functions. Those are similar to what they were in May. We have made no changes since May in the overall risk levels of our different individual functional activities.

We do evaluate this on a quarterly basis to determine if any of our core functions need their risk levels assessed. We have a formal process within the Investment Office Operating Committee to vote and propose changes to the risk levels. We currently have seven high risk functions. You can see them listed on the slide. That's about 15 percent of the total 48. And we have 21 moderate risk functions.

We are, in fact, assessing, particularly the portfolio management private markets right now. We've recently implemented the PEARS system, which you'll hear more about, but we felt we needed more time and experience on that system before we felt like we could reduce the level of risk around that one in particular.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Here are the 36 projects that we mentioned. It's sometimes helpful, and we've taken this concept within our program management activities within the Investment Office, to divide them up into sort of what stages of a project's life they fall into. As you can see, several of them are in, what we could call, the concept phase.

And really, these are areas where there's additional research to be done. And the expected output from that is probably a recommendation to the Investment Committee, to our internal Investment Strategy Group to our internal Investment Office Management Committee, the IMC, or the Operating Committee.

We have 16 projects in, what I'll call, design phase. That's really where we've decided -- it's moved out of concept, and we now have an idea that we believe needs to progress, but we have to design how to support it.

And the expected output from that is a fully formed workplan and the beginning of implementation. And then finally, we have seven projects that are in the implementation or execution phase. And this is where we're actually building something, essentially doing the plumbing work. And the expected output there is a completed policy, system workflow, or strategy.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: One of the initiatives that I specifically wanted to highlight, and it's one that many members of the Investment Office are engaged in, is around the restructure of our ISG, our Investment Strategy Group, within the office.

This initiative is really designed to enhance governance, while improving the understanding and ownership of trust level investment risk and performance decisions. We've established four subcommittees to our ISG. And these are composed of -- led by senior level investment people, primarily our Managing Investment Directors.

And they really serve as the first line of review analysis and our due to present recommendations for actions and decisions to the ISG on key investment decisions facing the office. This includes the Trust Level Risk and Attribution Committee. And their job is to look back at our performance evaluating how well we did for the risks we took. Our Portfolio Allocation Committee, to provide an organized approach to making asset class rebalancing and tactical position decisions.

We also have the Governance and Sustainability Committee really to focus on integrating ESG considerations into all of our investment programs. And we believe you'll actually got a chance to hear directly from the members of that Committee at the January workshop when we meet next month.

And then finally, the Trust Level Investment Review Committee. And they're charged with really examining out of the investment opportunities that sort of fall outside of our core activities. So, for example, co-investment opportunities within private equity, those are things that are quick moving. They're outside of the core private equity program. And we felt like they needed additional oversight and review by a group of seasoned investment professionals. So this is part of the role of that committee. In addition, they'll be examining any of the open sort of manager spots that we have within our

100 -- our list of 100 managers.

If we have open spots, those are a shared resource that the office needs to consider, and then allocate. So we needed a committee to examine those opportunities to come forward with recommendations as to how we allocate those resources.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Some of the other 36 initiatives that we have on deck this year to address operating model risks specifically. The PEARS Project -- we've discussed the PEARS Project quite a few times with the Committee, but we have implemented phase one. And we're well ensconced in phase two. And really the goal of that is to enhance the investment monitoring, risk management, fee transparency, and operational risks and inefficiencies within the private equity -- our private equity investing activities.

And next strategic manager monitoring, you can see that up there. And this initiative continues to focus on aligning the interests and looking at the efficiency and consistency of our manager selection and monitoring process across the whole office to really try to drive consistency and transparency in those manager selection and monitoring activities.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Portfolio priorities is a project that the Committee has been engaged with at a variety of off-site workshops. The priorities are now being focused on translating basically our Investment Beliefs into the benchmark selection and portfolio construction activities of the office. You'll be hearing an update on that project also at the January workshop.

Portfolio measurement and attribution. The initiative focuses on providing timely, standard, analytic reports and analytics that measure performance, risk, and exposures within our portfolio. And the primary user of that information is that Trust Level Performance and Attribution Subcommittee that I mentioned a few slides ago.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Turning our focus to some of the quarter one accomplishments. Capital allocation. You can see that on our Investment Strategy Group restructuring, we've worked to better clarify the mission, the roles and responsibilities, and authorities of the ISG and two of the subcommittees. And we actually just voted on those at our ISG meeting last week.

The private equity legacy portfolio management and optimization. Really, we implemented key monitoring metrics to look at, what we call, legacy investments within our real assets and our Private Equity Program, and also interestingly enough, the tail-end of our Absolute Return Strategy Program. All of the legacy investments that we're working to wind down all live in that program. And they're watched and we use special metrics to examine that activity.

And then finally, liquidity operations. And really this has to do with the recent changes to the liquidity asset class, and enhancing the reporting and monitoring framework around liquidity.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: A few more quarter one accomplishments. The Investment Beliefs Integration Assessment. You may recall we came to the Investment Committee with some updates. And Roger Urwin helped us complete that work.

And the emerging manager five-year plan, as you can see, within this last quarter, as Laurie mentioned earlier, we hosted the Emerging Transition and Diverse Manager Day, as well as the Diversity and Investments forum.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Finally, since the last update in May, we went live with a system called Artemis, which is specifically used to address the asset allocation work and execution activity for the affiliates. We believe that this has dramatically improved the control environment and the efficiency around the management of the affiliate funds. And we're actually now looking at how to expand the use of Artemis to actually help us manage asset allocation within the total fund, the PERF.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: A few of the projects that closed out. We completed our carbon footprint. Within the global governance team, the principles and proxy voting. Sixty-nine percent of shareowners approved our shareowner proposals around proxy access, or 54 out of 78. So we're quite pleased with that hit ratio. We haven't given up. We're still working down that path and hope to see that percentage grow.

We completed pricing and valuation procedures for all asset classes within this last quarter. And finally, as you'll hear in April of next year, our INVO fiscal year 2014-15 cost savings totaled 217 million of both ongoing and one-time cost savings.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: We spent most of this brief presentation around our 2020 Vision, or basically four and a half years away. But we want to acknowledge that in line with being a long-term investor, we definitely have to look out further. And our Investment Committee Chair has been quite good about reminding us about the need to look out 20 years, and what the Investment Office might actually look like in 2035.

A couple of the key questions and considerations that the Investment Office is focused on are listed on this slide. And you can see technology, business model, market environment, physical location and talent. And really these are just a list sort of the areas that we think will likely -- we'll see change, some more than others.

And obviously, at this point, we're really just trying to figure out exactly what questions to focus on for looking at something like a 20-year vision. It's very difficult to sort of -- none of us have a crystal ball of how the world might work. There are many new technologies in existence or just starting to come into existence today that could, in fact -- affect the world of investment, the world of market settlement, the world of cash and liquidity management.

In particular, we think that an area for us to focus is on business model. And you've heard, we use a variety of approaches around investing, particularly in the private asset classes. And we can expect this consideration of new business models for investment in the private asset classes to take more than our 2020 Vision, or five years, to really flesh out and experience.

And we would honestly welcome feedback from the Committee on whether we're considering the right areas and questions for something like a 20-year vision. And we've reserved space in our business planning process to both consider these questions as well as Committee feedback on where to move.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Our next steps around our roadmap. We plan to continue to develop, manage, and report on those 36 initiatives I mentioned. We'll continue to finalize and really operationalize those ISG subcommittees that we think are so important to really create a total fund focus and improved collaboration between our asset classes and team on the total fund performance.

We continue to make progress on our 2020 Vision, and we've started work on identifying our next year initiatives. And finally, we'll continue discussions on the 2035 strategy.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: So in summary, our 2020 Vision has now been operationalized within our 2015-17 roadmap. The roadmap is off and running with 36 roadmap initiatives. And our 2035 strategy, the crystal ball, is at the very early stages of development.

So this concludes my presentation and I'm happy to take questions and feedback from the Committee.

Thank you.

CHAIRPERSON JONES: Okay. Thank you very much.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: On one of the slides, and I didn't notice which one it was, but you talked about PEARS and the fact that we're making progress on it. We're now in phase two. One of the questions I have asked about private equity is attribution analysis, how much of it is coming from leverage, how much is coming from killing defined benefit, how much is from, you know, dividend recaptures. You know, where is the money coming from?

And you had said earlier that, well, once we get PEARS we'll be able to do some -- you know, we'll be able to give some analysis. We mentioned -- I mentioned it briefly on the call. Can you talk a little bit about how PEARS is going to help us actually figure out where we're making money?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Yes, I can, Mr. Jelincic. PEARS essentially provides the sort of underlying portfolio level data that we think we would need to build an attribution model. It doesn't actually do the attribution math in terms of understanding where returns are coming from. You've highlighted some of the areas that returns could be -- you could attribute leverage, timing, what type of sector the portfolio companies are in, how much is sort of attributable to equity market beta and could be attained -- obtained cheaply in the public equity markets, for example.

But prior to the implementation of PEARS, it was difficult to have enough dis-aggregated portfolio level data to really do that attribution. As PEARS gets -- we're now in our 12th month of implementation. We do not yet have a full year of underlying portfolio company data in PEARS, but we're building it up. We believe we'll also start building up that core underlying foundational data that we'll need to build an attribution model on top of that. And, in fact, staff has started to examine different attribution models within the private equity space to determine sort of the current state of the marketplace.

So that's definitely one of our interests is to better understand and attribute returns in private equity.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

Very appreciative of this Investment Office Roadmap update and also the continued focus on ensuring that ESG considerations are going to be part of our investment decision making. I guess I wanted to just have some assurance, because I'm still feeling like it's kind of in this vague arena, and how to make that a little bit more real. And this may be the subject of our January discussion at the off-site.

But whether the Governance and Sustainability Committee -- I like the connection of the Investment Beliefs to the portfolio construction, and, you know, certainly having that guide that. But in terms of the incorporation of ESG, I'm still not sure for example how we can include ESG in a benchmark for any particular asset class. And I didn't know whether that was going to be part of the discussion in January.

I just wanted to see if, as we talk about integration, whether we could get a little bit more specific with respect to that particular arena.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

That's definitely a series of topics that we plan to cover in January. I don't know if we had planned, at this point, to specifically cover the topic of whether sort of tilting a particular benchmark with a sort of ESG element was an element of that, but that's a great question and a worthwhile discussion for the Committee to undertake.

Generally, we undertake benchmark changes or considerations in conjunction with our asset liability management exercise, but the topic is certainly worthy of discussion. And it's something that we actually will have some outside experts to give us some perspective on what's happening in the industry at the January workshop that we can hear from as to what other large plans are doing in that space.

COMMITTEE MEMBER YEE: Okay. Good. I think what I don't want to have is when we embark upon our next asset allocation process is to not be a little bit more, I guess, prepared on informed about how to consider those types of questions. So whether it be in the fixed income or global equities or whichever asset class.

Thank you.

CHAIRPERSON JONES: Okay. Thank you.

Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you, Mr. Chair.

Thank you for this presentation.

I want to sort of echo some of the comments of Mr. Jelincic. I think it is important work that we're progressing with the attribution analysis, both in terms of what's driving returns and what's driving the risk that we're taking in the portfolio and trying to ensure that we are only taking risk that is compensated. I think that is a really important piece of work, so I look forward to continuing to see that evolve over time.

You asked for feedback on the 2035 considerations. And I don't know if you're -- let me first ask you, are you planning to bring this back at some point at a workshop format or what is sort of your -- what are your next steps around the 2035 Vision or are you still thinking about it?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: You certainly can -- we certainly can consider a future workshop. As I said, we're at the very early stages of sort of thinking about a 20-year vision and how investing might be done in the year 2035, and which impacts. There's obviously going to be 1,000 changes that will impact CalPERS and the portfolio.

It really comes down to which of those changes are things that we think we need to -- we can and should be focused on now. Business model is sort of the first.

And that's certainly a topic that we can consider for a future workshop.

COMMITTEE MEMBER MATHUR: So that was sort of my second question is are these listed in order of priority, or are they just sort of --

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

They're really not, honestly. We have just started thinking about sort of the changes that we can begin to speculate about looking out 20 years. It certainly -- we're open to suggestion on that. Where do you think we should spend some time and focus?

COMMITTEE MEMBER MATHUR: Okay. Did you have something you wanted to --

CHAIRPERSON JONES: Anne.

CHIEF EXECUTIVE OFFICER STAUSBOLL: Thank you, Mr. Chair. Anne Stausboll. I just thought I'd mention in terms of the timing and the process, that we're coming up on the end of our current strategic plan, which was a five-year plan to end June 30, 2017. So we're starting to gear up now for the next strategic planning process. So one thing that we've been talking about is how to think about these issues that Wylie talked about and create a framework around that, and then try to integrate that into the upcoming strategic planning process.

COMMITTEE MEMBER MATHUR: Terrific. Thank you.

CHIEF EXECUTIVE OFFICER STAUSBOLL: If that's helpful. Thank you.

COMMITTEE MEMBER MATHUR: If I could, Mr. Chair. I just had one more thing I wanted to add.

CHAIRPERSON JONES: Sure.

COMMITTEE MEMBER MATHUR: So in terms of actually providing you feedback on this, I note under market environment that you do note climate change, but I think there are other long-term systemic risks that we would want to consider I think as we were thinking about 2035 and beyond.

So I think we need to have a more expansive conversation about what some of these systemic risks might be. And if we are going to talk about prioritization, you know, physical location is listed on here. And I think maybe that and talent should be combined, because in a way they are -- they are -- they're talking about sort of the same thing, how are our people working, where are they working, how are they executing their job, do we have the right resources in the right places?

So I guess those are my two sort of preliminary comments, but I welcome the opportunity to sort of have a more robust discussion about this.

Thank you.

CHAIRPERSON JONES: All right. Thank you, Ms.

Mathur.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Thank you.

CHAIRPERSON JONES: Yes and to expand on that, I think the workshop idea is a great one. And, you know, as Anne mentioned, it's going to be part of your strategic planning. So we can begin that process of, first of all, educating, and then get into some deeper discussion in terms of priorities and what these elements really mean going forward.

And I think it's important that we all recognize that there's no crystal ball to tell us exactly what's going to happen in 35 years, but I think we need to start the planning process, because there are some things we already know about 20 years from now. We're going to still have to pay benefits, you know.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: That's right.

CHAIRPERSON JONES: That's a given. And as Ms. Yee indicated, the climate issue, we know that's a long-term strategy that people are beginning to talk about how to deal with that, and how that's going to affect our investment strategies going forward.

So those are some of the things that I think we can have this educational dialogue about in developing that process.

Thank you.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Thank you, Mr. Chairman. So what we'll take there is we'll work within our team to calendar that for the -- and get that on our Investment Committee calendar for some point.

CHAIRPERSON JONES: So that's my direction on that item. And I won't have to repeat it at the end of this meeting. Okay. Thank you very much.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Thank you.

CHAIRPERSON JONES: Okay. So now we go to the next item is 9, which is Real Assets Annual Program Review.

(Thereupon an overhead presentation was presented as follows.)

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Good morning. This is Paul Mouchakkaa. I'm Managing Investment Director for the Real Assets Unit. I'm joined by three members of the real assets team, Beth Richtman, Mike Inglett, and Jim Hurley to the far left.

I want to start off by saying real assets is really a new categorization for CalPERS. It's really the consolidation or amalgamation of three programs. One program that is long tenured, large, and established in real estate; one that is developing nascent and relatively small in infrastructure; and, one that I think Mr. Eliopoulos described as fits the chameleon role in forestland, which is actually quite long tenured, but is also quite small.

What we have done in the past eight or nine months since I joined CalPERS is we're working very hard to integrate these three programs in how we manage and make investment decisions. And, in essence, we've taken a few steps in that progress. And some are still in progress.

First, in July of this year, we reorganized the real assets unit functionally across all three programs. Whereas in the past, they were divided with infrastructure and forestland on one side and real estate on the other.

We felt that given the talents of the team, this would provide a lot of knowledge transfer, but also importantly provide consistent investment decision making for the real assets category or asset class.

Second is we're working on defining one role for the real assets component of the CalPERS fund. If you see on one of the slides that was provided, there's roles for each of the three programs on slide number six, and there's a tremendous amount overlap when you look at it highlighting items such as diversification to equity risk, stable cash flow, and inflation hedging. So we will be working to have one role to sort of cover the whole real assets component.

And third, we will be providing one strategic plan for the real assets component coming in the spring of next year. It's just about that time, as Mr. Eliopoulos mentioned in his beginning points.

The other component that is providing, what I would call, some guiding principles to our unit were hit upon by Wylie in his last presentation regarding Vision 2020. First and foremost, we are looking to focus on repeatable, predictable, and scalable strategies and business models for real assets. Secondly, we are working very hard to reduce the complexity, and therefore, the number of investment managers that we partner with. Just important to remind the Committee that this program is executed primarily by using external managers. And third, we are also working hard to integrate ESG as much as we can in the early stages of where we are in real assets.

We're not there. And if I had to -- I'll sort of delve in now just to give a sort of a headline or highlight of each of the three programs and where we are, and then I'll get into the belief matrix on slide number three.

So starting first with real estate, as I mentioned, which is kind of this longer tenured, established, and large program, the goal today is to stay on course. Really, the results are in over the last five years that the strategic plan has undertaken back in 2011 has provided exactly what we asked for in terms of its role of diversifying equity risk and providing stable cash flow.

Secondly, performance has been strong over the past five years in the real estate component. The strategic portfolio has been the key driver of the more recent performance -- strong performance, I should say. On the other side of it is, it is still a restructured program. If you were to go back seven years ago, as Ted mentioned, it really doesn't even resemble what the portfolio is today. And adding to that is the market dynamics have been quite challenging. There's a lot of other investors that are chasing the types of assets we want to invest in.

Moving on to infrastructure, those same competitive dynamics are at play as well. And our goal is to stay disciplined, but at the same time try to increase the deployment, which is not an easy thing to do, because those two things can be at odds with one another.

Lastly, in forestland, this is a program that is under review in terms of its fit with real assets and more importantly it's fit with the fund. As I mentioned, those guiding principles of Vision 2020 of predictable, repeatable, scalable strategies will really help be the prism or lens that we use to evaluate that program.

The last two concluding comments I'll make before turning to the Belief matrix, and they are somewhat repetitive, is we do -- we have had strong performance in the last three to five years, particularly in real estate and infrastructure. The forestland component has been challenged, and that has been -- that will be touched upon in terms of its underperformance.

And in the second part, is that we will be bringing a new strategic plan in the new year, that will cover all of these three programs for the Board.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: So turning to slide 3, which is the Belief matrix, Tom McDonagh presented this last year. And I thought he made a very lucid observation. And one of them was that if you were to score this program five or six years ago, it would have looked like a plate of marinara sauce. There would have been a lot of red.

And what you saw last year was a tremendous amount of progress in that a lot of it was yellow with a -- what we have shown here I'd like to highlight three big observations for the Investment Committee.

First, on Belief number 10, we have shown improvement. On that area, we believe that that's been driven by the integration of the organizational unit of real assets, bringing knowledge transfer and consistent investment decision making, and providing that sort of level of expertise that we have at the program levels across real assets. So we believe we made -- we sort of turned the corner there.

The second observation I would make, which really hone in on Beliefs number 6 and 7, relate to the competitive dynamics in the market today. It is very difficult for us to maintain our asset allocation. We've been below it, mostly driven by the pricing, and the fact that there is a lot of people chasing the same number of assets that -- or same types of assets that we would like to pursue, but we need to maintain that discipline.

The third observation I would make really hone in on ESG integration and expense reduction. With respect to ESG, there are a few observations I would make.

First, the manager expectations project has been a key area that has been woven into the real assets approach to investing. And it really covers now from the very beginning of a relationship to the ongoing maintenance of that relationship. And what I mean is it's part of the search, diligence, contracting, and monitoring of our investment managers that we select. We're only in the early stages of that, but that we believe is an important element to bring into our portfolio.

Second, we added infrastructure assets that are in our -- many of our separate accounts to be benchmarked into terms and measured for their efficiency in their carbon footprint. This joins now with some of the real estate assets, which have been benchmarked and monitored for the past few years.

The other element that I mentioned is expenses, which is also a key area of focus for real assets. And we have been on two fronts working to evaluate new business models and fee models to explore, and potentially implement. And on the other front, we have been actively liquidating legacy portfolios which have generally tended to have higher fee models.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: So I don't want to -- I know it's a very long presentation, so I will not be touching every slide.

(Laughter.)

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: But I wanted to move ahead to slide number 7, which is the program investment philosophy. Really, the vast majority of the program, as I mentioned in the rule, is to be invested in high quality, well located assets. I like to think of it as assets you want to hold through business cycles and less of those assets that are premised on timing or trading. And that tends to align with Beliefs numbers 1 and 2 in our program.

The execution in which we do that is primarily through separate accounts, and we seek to partner with highly reputable and market-leading investment managers to do that. This model, as Ted mentioned, in his introductory comments, from our point of view, allows CalPERS to gain better governance, greater alignment, more transparency, and cost efficiency, and will allow us to move towards having fewer and larger external manager relationships for the program, again aligning ourselves with the Vision 2020 principles.

So what does the Real Assets Program look like today?

And I'll touch upon it here. And as I mentioned, we're currently -- or as of June 30th, which these numbers are presented at about 10 and a half percent of the funds assets, or $32 billion. That's one and a half percent below its target allocation. We have unfunded commitments of approximately 11 and a half billion dollars. I want to highlight that given that the vast majority of those commitments are in separate accounts, they can be actually revoked. And so they're not -- the full amount that you see there is not actually a full contingent liability for the system.

What's it made of today?

We have 58 external managers. Again, that's as of June 30th. That's 60 commingled funds, 45 separate accounts, two operating companies, and two direct investments.

And the geographical exposure of the real assets portfolio is roughly 86 percent is in the United States, with 14 percent outside, and nearly a quarter of our program is invested here in the State of California, mostly in the real estate sector.

So with that, I will pass the presentation over to Mike Inglett who's an Investment Manager, and he will cover performance, characteristics, and the market environment for the programs.

Thank you.

INVESTMENT MANAGER INGLETT: Okay. Thank you, Paul.

In the investment review section of the presentation --

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INVESTMENT MANAGER INGLETT: -- I will discuss each of the three programs that make up real assets. We will begin with real estate. This will be on page 12 of the slide deck. Like Paul mentioned, we're not going to go through every page, but we're going to hit on some highlights.

So in regards to a market overview, the commercial real estate capital markets are competitive and pricing is robust. Cap rates are at or near historic lows. As for fundamentals, they are solid and continue to show improved income growth and lower vacancies across all the sectors.

Because of this unique environment, investors need to be especially disciplined and selective at this point in the market cycle.

Now, I'll discuss some real estate performance.

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INVESTMENT MANAGER INGLETT: We'll move on to page 13 in the slide deck. For the fourth consecutive year, CalPERS real estate has outperformed the benchmark. During the past year, the CalPERS real estate net returns were 13.5 percent compared to the real estate benchmark returns of 12.4 percent.

The strategic portfolio produced a 15.9 percent return, and was real estate's primary driver for the performance over the benchmark. The base portfolio, which is a segment of the strategic portfolio, had a noticeably strong return of 21.6 percent for the fiscal year.

Now, we will turn to slide 16 and I'll go over some of the Real Estate Program characteristics.

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INVESTMENT MANAGER INGLETT: So real estate's total NAV is 27.5 billion. This is 9.1 percent of the total fund, and it slightly below the target of 10 percent.

As of June 30th, we had 50 external managers. The real estate portfolio consists of 52 commingled funds, 40 separate accounts, and two operating companies. The separate account vehicles account for approximately 70 percent of our NAV.

Geographic exposure is 88 percent domestic, and 12 percent international. Turning to slide 17.

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INVESTMENT MANAGER INGLETT: There are a few additional real estate characteristics I'd like to go over.

So as you can see, there are four charts on this slide. I'm going to concentrate on just two of them. First, please turn your attention to the chart in the upper right called strategy. The strategy is made up of

81 percent in strategic portfolio. And this consists of base, domestic tactical, and international combined to make our strategic portfolio, and then 19 percent in our legacy portfolio.

Now, if you'd move down to the bottom right side of the page, we can go to the chart entitled risk category. The risk category shows that we roughly have 50 percent of our assets in core, and 50 percent of our assets in non-core. The non-core is made up of value-add and opportunistic combined.

We will now turn our focus on the infrastructure program, so if we could turn to slide 21.

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INVESTMENT MANAGER INGLETT: In regards to infrastructure market overview, we face both challenges and opportunities. Some of the challenges include, one -- number one I want to point out is that assets that fit our role are in high demand, and we face stiff competition for these assets as Paul alluded to earlier. Number two is research shows a significant need to build infrastructure in the U.S., but the reality is it has not translated into many live investment opportunities for us.

Some of the opportunities that we see, I'll go over a couple main ones here. The first one is the global transition to clean power. And the second one is select geographic locations like Australia are privatizing their infrastructure.

Now, I will discuss infrastructure's performance. If we could turn to page 22 in the slide deck.

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INVESTMENT MANAGER INGLETT: For the fourth consecutive year, the CalPERS infrastructure returns have outperformed the benchmark. During the past year, the CalPERS infrastructure net returns were 13.2 percent compared to the infrastructure benchmark returns of 3.9 percent.

As you can see on the chart, infrastructure has had strong returns across all periods. Turning to slide 25, I will discuss some of infrastructure's portfolio characteristics.

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INVESTMENT MANAGER INGLETT: Infrastructure's total NAV is 2.2 billion. This is 0.7 percent of the total fund, which is slightly below the one percent target. As of June 30th, there were eight external managers. The infrastructure portfolio consists of eight commingled funds, two direct investments, and three separate accounts. The NAV is broken out with roughly 50 percent in commingled funds, 25 percent in direct investments, and 25 percent in separate accounts.

The geographic exposure is 60 percent domestic, and 40 percent international, with the majority of the international exposure in Canada and the United Kingdom.

Turning to slide 26, there are a few other additional infrastructure characteristics I'd like to highlight.

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INVESTMENT MANAGER INGLETT: Once again, there are four charts. I'm going to concentrate on two of these. If we could turn our attention to the chart in the upper right called risk category, this shows that 33 percent of our NAV is in, what we call, defensive assets, 47 percent is in defensive plus, and 20 percent is in extended.

Now, if you'd move down to the bottom left side of this page to the pie chart titled sector, 91 percent of the sector is exposed in three primary areas, power is 50 percent of the NAV, transportation is 28, and energy is 13.

We will now turn to page 31 to discuss the -- briefly discuss the forestland program.

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INVESTMENT MANAGER INGLETT: The total NAV is 2.2 billion, about the same as infrastructure. It is 0.7 percent of the total fund and is slightly below the one percent target. The program is made up of two managers, one manager is domestic, which is 82 percent of the NAV, and the other manager is international, which is 18 percent of the NAV. The international holdings are primarily in Brazil, Australia, and Guatemala.

The CalPERS forestland returns underperformed the benchmark. During the past year, the CalPERS forestland net returns were negative 0.3 percent, compared to the benchmark of 10.6 percent. The performance has been challenging, the program has been underperforming, and the program is currently under review. We will provide recommended direction when we present our real assets strategic plan in the spring of 2016.

That concludes the investment review section. I'll now hand it off to Jim Hurley, who will cover real assets organization chart, the upcoming strategic plan, and he'll provide a strategic project update.

Thank you.

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INVESTMENT DIRECTOR HURLEY: So if we could turn to page 39. This is -- page 39 reflects our current organizational structure. The team has 58 professionals, which is unchanged from the prior year, year '13-'14. During this year, '14-'15 the team hired or promoted six professionals. We currently have three open positions.

If we could go to page 42 --

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INVESTMENT DIRECTOR HURLEY: -- the team has been very busy on a number of initiatives. Page 42 has some key initiatives that I want to just touch on very quickly. On the first initiative, real assets Investment Committee integration. With the prior structure, there were two separate investment committees, one for infrastructure and one for real estate.

Effective July 1, we integrated those two committees into one Real Assets Investment Committee. There's eight members on that committee. There's folks from infrastructure, real estate, asset allocation, and we also include the head of private equity.

There are or -- there is an open invitation to legal and ICOR. And the Board consultants attend each applicable investment committee agenda item.

On the second initiative, asset class staff organization, the prior organization had separate portfolio management and new investment groups for infrastructure and real estate. We've merged those groups, those four groups, into two groups both reporting directly to the Management Investment Director and that was effective July 1.

On the third initiative, working with the operations group, we've implemented a new valuation procedure for the real estate assets. So effective July 1, all real estate assets are valued on a quarterly basis. And there's procedures that are implemented and in the process of being refined to ensure those are quality valuations. And then finally, as Paul discussed, we're proposing to bring one integrated strategic plan to you in the spring.

And with that, I'll turn it over to Beth who has a few comments on ESG and emerging managers.

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INVESTMENT MANAGER RICHTMAN: Beth Richtman, Real Assets.

In the last year, we've made progress on the integration of sustainable investment considerations into real assets investment processes, namely on three fronts. First, we've documented our manager expectations -- our manager expectations across all of real assets laying out key expectations for sustainable investment practices pertaining to diligence, selection, contracting, monitoring, and managing.

Second, we have become a founding signatory to GRESB infrastructure, measurement, and benchmarking platform. Real assets will begin utilizing this tool and surveying our infrastructure assets with this new platform in 2016.

Adding the GRESB infrastructure tool deepens the benchmarking already being done in real assets on real estate investments through the GreenPrint program. Thirdly, as you know, the Responsible Contractor Policy was enhanced this year.

Looking forward. With the benefit of better data coming from our measurement tools, real assets will be evaluating options for energy efficiency and cleaner energy sourcing for our assets, and also looking at how to push out the best sustainability practices at our assets further across the portfolio and into the different asset types.

Moving on to emerging managers.

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INVESTMENT MANAGER RICHTMAN: We are three years into the program for real estate. The program is off to a good start. As you heard in an earlier agenda item, the Manager Transition Program was established earlier this year. Real estate looks forward to utilizing this program for graduating high performing emerging managers as appropriate into further mandates.

And now back to Paul to discuss expenses.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Thank you, Beth. There we go.

I'll touch upon expenses. You see before you a table with a lot of numbers. I think the headline on this is progress has been made, but there's more work to be done. And what you see is roughly $630 million in total program expenses on real estate. And as I mentioned before, since we execute the program through external managers, the vast majority of that 609 million is paid to external managers.

The breakdown of that 609 million is roughly $177 million in base asset management fees, and approximately $432 million in paid or accrued profit sharing payments.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Going forward, as I mentioned, as the headline more work needs to be done. We'll be evaluating new business models and looking for even better aligned fee structures to enhance the cost efficiency of this program. I will say it has moved in the positive direction, as I said, when we talked about the belief matrix over the past five years since the adoption of the new strategic plan.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Moving on to the next table of numbers, the story is very similar for infrastructure, the only difference being, as I touched upon, it's a much -- it's a developing and growing program. Roughly, total expenses amounted to $67 million dollars with the vast majority of 63 million being paid for external management, 22 million in the form of asset management fees, and approximately 40, 41 million in the form of profit sharing payments paid or accrued.

Again, new fee models, new business models are being explored. And going forward, we will sort of look at this on a more holistic basis for real assets. So when you kind of smush these two tables together, there's roughly $700 million in total expenses, with 672 million being paid to external management.

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MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: So taking us home, slide 50 of 50, I'd like to sort of reiterate three key messages. And as I touched upon, real assets is really this consolidation of these three programs in various stages and histories and whatnot. And so each have -- are in sort of different forms or stages. And with real estate, we will continue, as I mentioned, to focus on high quality income producing assets that fit the role.

In infrastructure the goal is to balance the need for deployment, but still maintain the discipline. And as both Mike and myself mentioned, the forestland program is under review for its fit.

ESG and program expenses are also a major focus. We will evaluate results of our benchmarking exercises and data. I don't actually want to take the word -- they're not exercises. These are actually really important components in terms of the portfolio management of our group.

On the expenses side, we'll be evaluating different business models and new fee models to better align ourselves -- to even better align ourselves going forward. And then the last two points I would make, and I'll -- we'll open it up to questions are really the focus for real estate or real assets I believe is really described very well in the role.

And with private asset classes, it's very hard to benchmark how you perform. And so therefore, our role is really the guiding post. And the more we focus on it, it really provides a lot of information for our Investment staff in terms of how we pursue our structures, and how we pursue the types of assets that we want to invest in to provide a defensive portfolio and the types of assets that we will want to hold through business cycles.

And with that, I am -- we're all happy to open it up to questions.

Thank you.

CHAIRPERSON JONES: Okay. Thank you very much. We do have several questions, but we're going to take a 10 minute break and then reconvene and take the questions, and then we'll move to consultant's review after that.

Okay. Thank you.

(Off record: 11:12 AM)

(Thereupon a recess was taken.)

(On record: 11:21 AM)

CHAIRPERSON JONES: We'd like to reconvene the Committee meeting, please. So we'll ask the Committee members to return to the auditorium

Okay. Let me see. Yeah, we are going to reconvene. I was looking around and where are they?

(Laughter.)

CHIEF INVESTMENT OFFICER ELIOPOULOS: Call the Sergeant at Arms.

CHAIRPERSON JONES: Yeah, right. We have to get the Sergeant at Arms

Okay. But we do have several questions. I'm going to go ahead and start with Mr. Costigan, since he's here.

COMMITTEE MEMBER COSTIGAN: Thank you, Mr. Jones. Thank you for the excellent report.

So I just have some questions actually regarding slide -- well, it's the program expenses. So just some clarification. So on 199 of 315, or 46 of 50, why do you account in 2013-14 for the 87 million? Why do you put multiple years of fees on that one?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: The reason for that was there was a catch-up done that year in terms of the total amount of accrued profit sharing. It's highlighted -- I believe, there's a footnote.

COMMITTEE MEMBER COSTIGAN: It's footnote number 3, but that doesn't quite highlight. So why is there a catch-up provision?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: No, no. Excuse me. It's not a catch-up provision related to the traditional explanation of an incentive fee model. It's that several years have passed since the new strategic plan, and it had basically implemented probably about two or three years worth of incentive fees that were accrued, and lumped into that one year, because it was the first time.

COMMITTEE MEMBER COSTIGAN: Okay. I see Wylie wants to answer, because that's even more confusing. Why would we wait three years to pay something?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

There was a change in accounting practice last year that we worked with the Chief Financial Officer around. Effectively, we -- historically, we did not accrue profit sharing around our Real Estate Program until the last three years of a partnership, with the thought that -- this is the old accounting practice -- with the thought that performance could turn around and then we would have to reverse out any fee that we accrued if performance fell.

Last year, again, working with the CFO, in June of 2014, we changed that practice to essentially accrue fees as they are earned based on the current performance. So essentially, we went from a last three years policy to a whatever the performance is this year. If the partner has earned a fee, we accrue it. That required a catch-up for about from -- actually, back from 2011 through 2014 of multiple years of incentive fees in order to basically catch the accrual up. This actually hit the books in last year's consolidated annual financial statements.

COMMITTEE MEMBER COSTIGAN: Because I have a question then on timber. But from the standpoint then for a more accurate representation on fees, are we going to see a fee increase? How do I -- the problem is it looks like there's a substantial reduction, when, in fact, there isn't. So if I'm looking for a comparison between '13-'14, where did we land from a fee perspective?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: What you see in the profit sharing accrued in the column fiscal year '14-'15 would be the change for the year. And so therefore, as of today, we have it in one of the notes at the very bottom. The total profit sharing liability today is approximately 1.1 billion, which is close to the addition of what you see in fiscal year '13-'14, and what you see in fiscal year '14-'15.

Since it's an accrual, it is a moving target and changes year to year. And so the total liability is a little over a billion dollars today.

COMMITTEE MEMBER COSTIGAN: Okay. Then on infrastructure and forestland, I just want to make sure I understand this correctly. On the slide that shows performance, we actually have a net 10 years where we've underperformed the benchmark, is that correct? I can't find the slide.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: For forestland?

COMMITTEE MEMBER COSTIGAN: Correct.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA:

Twenty-eight.

COMMITTEE MEMBER COSTIGAN: 31 of 50.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: There we go. I was there.

COMMITTEE MEMBER COSTIGAN: Okay. So we've underperformed, correct?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Correct.

COMMITTEE MEMBER COSTIGAN: Okay. So I don't understand -- and I just don't -- I struggle with the whole fee aspect. How is it then on the slide that talks about the fees that were paid back here to --

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Forty-eight.

COMMITTEE MEMBER COSTIGAN: -- 49, infrastructure and forestland -- so we have profit sharing paid 12 million, profit sharing accrued 29 million, and asset fee 20 -- So they've underperformed for 10 years, and yet when I look at the -- so help me just to understand this slide. What part --

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: It's including infrastructure and forestland, and infrastructure has had very strong performance. And therefore, that -- the accounting for the infrastructure and forestland program is combined. And so therefore, what you're seeing is --

COMMITTEE MEMBER COSTIGAN: So we should break this out then, because --

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: We would have to break it out.

COMMITTEE MEMBER COSTIGAN: Because again -- then

I would -- because you have two managers on the forest side. And what I don't see is what we've paid those managers in fees or how they have done on an asset that under 10 years has underperformed.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Understood.

COMMITTEE MEMBER COSTIGAN: So, Mr. Jones, if we could get that at our next meeting, it would be great, because, again, this slide is skewed, because on the flip side, it shows then not the value of benefit that you're getting on the strong performance of infrastructure.

Thank you, Mr. Jones.

CHAIRPERSON JONES: Sure. Okay.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Some observations and a couple of questions. I really like forestland. It's a asset that's long-dated, where we can control the cash flows, because you simply don't harvest when it's down. But on the other hand, as we look at it, unless we get into the Pacific northwest and the northeast, I'm not sure that we will ever come anywhere close to tracking the industry. And if we're not going to move there, then I think we need to look at getting out of it.

I want to commend the discipline that you've shown in not chasing this market.

On slide eight, which is the index -- the benchmarks, for real estate policy benchmark, obviously, we have underperformed that significantly. Can you tell me how the benchmark is different than what our portfolio looks like?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Well, the real estate benchmark is called the ODCE Index. It's a combination of roughly 22 or 23 what's called open-ended funds. These funds are domestic only. So that's one area where we have exposure outside of the United States. In addition, they represent I think the total gross value or -- is about 170 billion and the NetValue is around 140 billion, which, you know, compared to the size of our real estate portfolio, is relatively small as a benchmark.

But it does take into account leverage, and it does take into account fees paid to managers. And when you run the historic data for the NCREIF ODCE, it does -- the results, or the output, of that information does tend to match, to some extent, the role in which we talk about.

But notwithstanding that, in any private asset class, it is quite challenging in terms of benchmarking ourselves. And so where we have differences, it's very hard to always compare yourself to any of the private asset class benchmarks, in terms of what's the make-up of them.

As I said, it's 23 managers or 23 funds. I believe the top four funds are over half of the index. And so therefore, it's hard for us to always directly compare as you might in a public world where the index might be a greater representation. As I said 150 billion, 140 billion is not even -- it's roughly two and a half percent of the investable universe just in the United States.

COMMITTEE MEMBER JELINCIC: And the composition?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: It's about 39 percent office, 24 percent apartment, 19 retail, and 14 industrial. And the other four percent is in self-storage, hotel, data centers, and other specialized types of real estate.

COMMITTEE MEMBER JELINCIC: And how do we look in terms of the asset distribution compared to that?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: So we're currently overweight in retail. You can see it on -- I believe on one of the slides here, if you'll bear with me. We're overweight in terms of retail overall, and we're underweight in terms of apartment and office as of today. And we have housing exposure in our legacy portfolio, which wouldn't be reflected in the benchmark.

COMMITTEE MEMBER JELINCIC: Okay. And then on slide 13, it's -- it shows the time sensitivity of performance. It's great when '08 and '09 fall off your comparison.

On slide 45, which was the -- in the emerging managers section, we've gotten an IRR calculation. Is that calculation -- is the cash flow front-loaded, back-loaded, because that's obviously a key to IRRs?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Those are just on realized investments, so they would be gross. And we've had, I believe, four actual properties. So these are not manager level or fund level. They would be property level and they've been very strong in this market.

COMMITTEE MEMBER JELINCIC: So those cash flows would tend to be back-loaded.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: They would have been more back-loaded given that they were generally short three-year holds.

COMMITTEE MEMBER JELINCIC: Okay. And then the -- I think -- I forget who mentioned it that we're now going to quarterly evaluations of the real estate portfolio. I assume we are not doing full appraisals every quarter. It would tend to get a little expensive. How are we doing that and what kind of quality controls are we putting in?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Wylie Tollette, CalPERS staff.

The new process -- the new evaluation process involves Altus, which is the manager that we've contracted with for a number of years to provide guidance on selection of external appraisers throughout the world. And they recommend appraisal firms to us and have done that for a number of years.

The new process we put in place this year also asks Altus to coordinate a quarterly evaluation process, where we actually will take the manager's evaluations for three quarters of the properties each quarter. And then one quarter of the properties, we will pursue an independent appraisal, as we always have.

So over the course of a year, every property is independently appraised at least once on a rolling quarterly basis. And then three quarters of the properties we actually will examine. Altus will first receive and then examine and challenge, if necessary, the manager's valuations. And through that process, we're achieving a quarterly valuation process without incurring the full expense of a full quarterly independent appraisal.

COMMITTEE MEMBER JELINCIC: And we have been basically booking all of the appreciation and depreciation in one quarter, so --

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: That's right.

COMMITTEE MEMBER JELINCIC: And I assume that will change now?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: That's right. Starting with this quarter, what you'll see is the -- any change in valuation will actually occur ratably throughout the year. So that was actually one of the primary motivations that we had for moving to this new quarterly valuation process is that you essentially had to sort of do the math in your head for an entire year, because the benchmark is also updated quarterly.

And we wanted to try to not fall as far behind the benchmark so that we could understand changes in the marketplace, both sort of on the -- on an overall real assets basis as well as within local markets. And this new quarterly evaluation process gives us more information to try to detect those changes and understand the nature of the portfolio.

COMMITTEE MEMBER JELINCIC: And I assume -- but assumptions are dangerous -- that we will look at their quarterly evaluations versus what kind of appraisal we get, so that it's sort of a check to see if they are consistently high, consistently low, or the deviation is random?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Yes, that's right. And that's one of the advantages we feel we actually will get from this new process is we actually will get both the managers and appraisal -- assessments of the real estate marketplace every quarter and can use those as a counterpoint to one other.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you, Mr. Chair.

Forgive me if some of my questions are repetitive. I was a little bit late coming back.

A couple of things. One is I really appreciate the work on the GRESB benchmark for infrastructure and the manager expectations project. I think those are both really important steps forward in terms of achieving a more sustainable portfolio.

Can you talk to me a little bit more though about how you are integrating long-term systemic risks and opportunities into the investment decision making and risk management? And let me just cite a couple of examples that maybe you could think about.

One is sea level rise. I mean, there have been -- I know we tend to be in sort of the highest quality markets, a lot of them are on the coast. You know, there's -- Seattle is projecting that some of its neighborhoods will be under water by 2050, which is not that far off from where we are today. We also see nationally demographic changes, an aging population. And just curious whether any of those are sort of influencing the decisions we're making or moving forward, or how we manage our current portfolio?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: We do have a matrix that we have built into our due diligence that takes into account the types of risks that you highlighted. And so we -- particularly when we look at a separate account structure, whereby we're investing in one -- you know, one asset at a time, we can have managers fill out that matrix or questionnaire in order to get some assessment on some of the particular issues.

Beth, I don't know if you want to highlight a couple of the elements in that matrix?

INVESTMENT MANAGER RICHTMAN: Sure. Yes. Definitely long-term risks like climate change and sea level rise, but also resource scarcity are called out specifically as items that we want managers or staff to look at, depending on the nature of the asset and who's doing the due diligence.

Additionally, tools like GRESB and the recent sort of SASB standards that are emerging do call out look -- basically making sure managers and asset owners are looking at these type of risks. So it's becoming more part of industry practice to do so.

COMMITTEE MEMBER MATHUR: Okay. Thank you. You also noted, I think it was you Paul in your comments, that we don't have very much global exposure. I mean, we have exposure to Canada and the UK. But beyond that, we have very little exposure globally. Can you talk a little bit more about what's driving that? Is it really the currency issues or more on-the-ground regulatory concerns or other concerns?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Well, we do have, across real assets, about 15 percent. It's a $32 billion program. On a relative basis, that may not be high, and especially when you paint across, you know, what is the global opportunity set. What we're doing though is we're evaluating that exact question as part of our strategic plan. And we'll be bringing some parameters around what we believe will be the focus of the international component of real assets going forward.

COMMITTEE MEMBER MATHUR: Okay. And I assume -- I don't mean to harp on currency, but I assume currency is part of the concern. I mean, I've certainly seen in India, the currency has had a significant impact on returns there. So just -- will part of your strategic review also include any recommendations around how to manage currency, whether that might make -- influence how you deploy capital?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: I would say it more or less is influencing the strategy. Today, we take a more granular perspective and look at, either if it's a direct deal or if it's a program, to more or less look at it on a case-by-case basis.

But one of the challenges with respect to international investing is we do live in the biggest backyard, and we're a U.S. dollar denominated fund.

At the same time, we're investing in tangible assets, real assets. And so therefore, the complications around investing international need to be taken into account. And that is part of the formation, including the currency aspects that are helping inform our strategic planing.

And I think on one of the slides that Jim Hurley went over, we talked about the strategic plan update. And the last bullet on the slide talks about roundtables that we've engaged with various industry leaders around the globe with really on the public side, the private side, global big managers, boutique type managers to gain a lot of perspective on the questions that you're bringing up.

COMMITTEE MEMBER MATHUR: And then one final question, if I might, Mr. Chair. I know with respect to infrastructure, one of the things that we hear as -- you know, the competitive marketplace for good infrastructure projects that meet our criteria is that there are other managers or other pools of capital out there that might have different criteria than we have in terms of -- particularly in terms of the return expectation that they're requiring.

And as we're moving forward with this benchmarking, sort of, conversation about how -- what is the appropriate benchmark, I guess what I'm thinking about in my head is do we really want to measure ourselves against the marketplace or against what we need, in order to have real estate -- or real assets be contributing to our portfolio in a meaningful way in terms of both the return and risk aspects, which I see as sort of two different things. There's one sort of the relative performance, which, yeah, we always want -- you always want to be the best, delivering the best returns, but is that really the right way for us to look at ourselves or do we really want to be thinking about, okay, what do we require -- what's the right level of return to merit the types of risks that we're taking, et cetera. Just, I'm sure you all are way ahead of me on that, but thank you.

CHAIRPERSON JONES: Okay. Ms. Hollinger.

COMMITTEE MEMBER HOLLINGER: Yeah. Appreciate the presentation and all the work and planning that went into it.

I just had a question. What is going in the -- into the evaluation of whether or not it makes sense to retain our forestland portfolio?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: I think the real test, and Wilshire can -- talks about it in their letter to some extent, is does it meet the criteria of allowing us -- in terms of the actual implementation of it, does it match up with the role that we're trying to achieve?

And then in addition to that, given the principles of Vision 2020, is it a model that we can scale up? Because at $2 billion today, it is -- it's somewhat -- in the grand scheme of the fund, it doesn't have, you know, an enormous impact. It now has an enormous impact in terms of real assets. But is it something that we can scale up and does it pass the test of being a repeatable type of model and type of asset class that we want to continue to invest in? That is really the focus of the evaluation.

COMMITTEE MEMBER HOLLINGER: And if it wasn't, would we look to divest it or just -- it would stay --

just retain what we have?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: We would bring that forward in the direction that we talked about in the strategic plan. I think it's too early to know.

COMMITTEE MEMBER HOLLINGER: Thanks.

CHAIRPERSON JONES: Ted.

CHIEF INVESTMENT OFFICER ELIOPOULOS: I was just going to say, there's really two parts to that. One in the strategic planning sense of whether or not to keep the current investments within the forestland portfolio, divest them, sell them down, lessen them, eliminate them, that's one inquiry. But the other spot that this Committee would consider it is at the asset allocation level, because it is part of our asset allocation. So it would also have to come to this Committee for consideration of its part in the total fund.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: We did -- while we did get the fees broken out that Mr. Costigan had asked for with respect to timber -- or forestland, excuse me, and infrastructure. I'm happy to share that if you --

CHAIRPERSON JONES: Would you just send that to the Committee, because it was one of my follow-ups, but now scratch it off. So since you have it, provide it to

Committee.

Thank you.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Of course. Thank you.

CHAIRPERSON JONES: Okay. So, Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

I wanted to just applaud the work around the implementation of the sustainable investment practice guidelines, and obviously recognizing that real estate is a unique asset class where you have, you know, physical assets where probably these guidelines are much more easily applied.

My question really concerns whether there -- maybe to Ted and to Wylie. Are there things that are instructive about this asset class that may be applied to others. And I'm particularly focused on the manager expectations and the due diligence around the sustainable investment practice guidelines when we are looking at ESG factors?

CHIEF INVESTMENT OFFICER ELIOPOULOS: I think yes. And part of the manager expectation process is that there are similar inquiries going on for -- in fixed income and public equity and private equity, but they rhyme with each other rather than be specific, given the different nature of each of the asset classes. So we hope that the answer to that will be yes as we get the information back, and then make sense of it and compare across asset classes, as well as within each asset class.

But it's a new experiment that we're running. I've called it a pilot project for the year, so this is the first time in real assets and the other asset classes that we're doing this survey and assessment. So I think the real answers we'll see at the end of the year, and we'll be bringing that back to the Committee and see what's instructive across the different assets classes.

COMMITTEE MEMBER YEE: Okay. Great. And then I'm -- I'll await the consultant's report, but on the forestland issue, certainly scaling up is something to take a look at. But what was it about the -- I guess the environment at the time of the original prospectus that made us think this was going to be a good investment? I mean, was there -- I mean, was it the demand in the regulatory environment? And I think it's what's changed that's really -- or is it just because it's been such a limited investment?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Yeah, I think, theoretically, the forestland is a very attractive component asset to our asset class and our asset allocation. Theoretically, it has a link to inflation. It includes a component of income generation, and it has attributes that are very attractive to asset allocation team in looking at it, which would lead you to want to design and implement a program in forestland.

I think in practice, now that we have some time and experience with it, scale -- scale and scaling it is a real issue, and trying to come to terms with whether or not we're willing to sort of wait out the lumpiness of when assets will become available, and what business models then we would own these assets in and what structure. Certainly, the current business model that we hold our southeast timberland holdings poses some real challenges.

So it's more in practice than in the theory. The theory, I think, continues to make sense from asset allocation standpoint. The practice side of it leads us to question whether or not it's something that we can scale and repeat positive performance over a long period of time.

COMMITTEE MEMBER YEE: Thank you.

CHAIRPERSON JONES: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: When I look around the room, there's probably only three people who remember this, but, you know, 15 years ago, we had $2 billion in forestland, and the fund was much smaller, and it was a very profitable investment.

It got really expensive, and we said we're taking our money off the table. And then we got back, we decided we're going to do souther hardwood for whatever reason. But there is some real value to the asset.

On the -- if I can follow up on Priya's question, the foreign versus domestic real estate. We sold a whole bunch of commingled legacy accounts. Did that have a significant change on our U.S. versus international exposure to real estate?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Yes, it did. Now, the sale is not fully closed. We announced a buyer for the funds that we put in the secondary market. And so knowing the full exposure, we'd be able to provide once we get through whatever funds actually close and transfer in that secondary sale, but it should lower our international exposure.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Okay. Thank you. There are no further questions and thank you very much for your presentation.

We now will move to 9b, consultant's review of Real Assets Program from Pension Consulting, Wilshire Associates Consulting, and StepStone Group, LLC.

(Thereupon an overhead presentation was presented as follows.)

MR. LORDA: Good morning. Dillon Lorda, Pension Consulting Alliance. I'm joined by my colleagues Christy Fields and David Glickman. We are collectively your Board consultant for real estate, and have been since 2009.

Since that time, we have seen dramatic improvements in the real estate portfolio and have seen many improvements in the real estate unit or now the real asset unit. There is still ground to cover. As Paul mentioned, there are many improvements that are driving towards the 2011 objectives, namely through greater exposure to income producing assets, and reduced investment in highly leveraged opportunistic strategies.

Part of this is due to the fact that staff has incorporated diverse opinions and investment perspectives into the decision-making process. Staff has utilized this along with better portfolio management and risk analytical tools to make more holistic decisions.

It's our opinion that these decisions have helped reduce the overall risk profile of the portfolio, and simultaneously delivered strong nominal and relative returns.

We think that overall, both the portfolio and staff are better positioned today to withstand the next correction in the real estate market. We're not sure when that correction will come, as market conditions are currently quite strong at the space market level, with strong demand for real estate across property types driving rents upwards. Concurrently, capital markets are pushing prices above the peaks reached into 2007.

Under these conditions, it's difficult for staff to identify and acquire assets that are, as Paul described them, long-term hold assets at prices that are accretive to your overall performance. Both your managers and staff have been quite disciplined and patient in the deployment of capital under these conditions, and we're supportive of the measured pace at which they're approaching the market.

Staff is also very deliberately taking steps to move towards the 2020 objectives and the Investment Beliefs as you've identified them.

MS. FIELDS: CalPERS Investment Beliefs have been integrated into many parts of the RAU operations and investment decision making --

CHAIRPERSON JONES: Excuse me, would you identify yourself?

MS. FIELDS: I'm sorry. Christy Fields, PCA. My apologies -- into -- so Investment Beliefs being incorporated into the RAUs, operations and decision-making process. I won't flips to it, but on page nine of our materials, we do provide some examples of ways in which the RAU is working within the framework of the Investment

Beliefs established by the Board. And I won't speak to all of them. I think they've been covered quite well, but I do want to draw your attention to two of them.

First, number 7, calPERS will take risks only where there is a strong belief that the system will be rewarded. As has been highlighted in staff's presentation and Dillon's comments, the real estate portfolio has been significantly de-risked over the last seven years, and new capital is being deployed in lower risk, lower volatility investments.

Domestic and international tactical investments with higher risk return profiles are still being considered for a small portion of the portfolio, but those are being evaluated within the framework of Investment Belief number 7, and that is with the intent in a careful assessment to understand the CalPERS is being appropriately compensated for the attendant risks. That's not always been the case and that represents a marked improvement in the investment process.

The second Investment Belief I'd like to point you to is number 9, risk is multi-faceted and not fully captured through measures such as volatility and tracking error. This belief is nowhere more true than in real estate or perhaps private equity, as Andrew mentioned earlier.

Real estate has a disparate set of risks associated with physical property, with joint venture and development partners, with leverage, with market cycles among others. And many of these risks are very difficult to distill into discrete quantitative measures.

That said, staff has continued to meaningfully improve risk management in the real estate portfolio through their process, through the analysis, and through reporting.

If we turn just two pages ahead, there's a SWOT analysis that I'll touch on briefly. Among the strengths which are now many, at this point in the portfolio's evolution, we note in particular the direction of the Board via the Investment Beliefs, the significant reduction of risk in the portfolio, and the fact that you now have an experienced an MID in place who can add great stability to the leadership of the unit.

Among the opportunities, we know the making of continued progress towards the objectives of the 2011 strategic plan, and relatedly to the revisiting of that plan in the spring of next year.

Also, while there's been good progress to date on ESG initiatives in the RAU, there is still opportunity for more progress, and staff is focused on these.

Finally, with the portfolio de-risked and better aligned with the role of the asset, staff can now turn their attention to proactively identifying opportunities that are well aligned with the role of the -- of the RAU.

Among the weaknesses, we note that the installation of the new real asset portfolio management tools will continue to take time, and that the RAU needs to integrate Investment Beliefs and ESG initiatives in a more disciplined manner.

The understanding of the importance of these matters is evident with staff. It's more of a time and resource management issue to continue to further all of these initiatives concurrently with the day-to-day investment activities.

Lastly, relative to threats, we highlight again the competitive market that CalPERS faces in the pursuit of quality real estate investments that meet its risk and return objectives. We support staff and their continued discipline focus on building a defensive portfolio to hold through the market cycles.

That concludes our comments, and we're available for questions at this point.

CHAIRPERSON JONES: Yes. Okay. Thank you for your presentation. Oh, wait a minute. We've got -- you want to -- let's go to questions, then we'll go -- go ahead, Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Yeah. This is on SWOT, you know, which is 11 of 19, 221 of the iPad. The weaknesses, can you expand a little bit on those, particularly the first, second, and four one?

And then just to warn you, so you can think about it, in the threats, the difficulty of sourcing new strategic partners.

MS. FIELDS: So I think some of these will be blended into the discussion that follows with the review of the strategic plan that's coming, but they're things that we've started to discuss, particularly around the issue of offshore investing and whether that becomes a -- remains the same or becomes a larger part of the program, and what that means for having people only based here in Sacramento trying to understand these markets and their attendant risks.

The reliance on external managers, that is certainly an intrinsic part of this program. Many of your base partnerships are -- this is kind of a -- both a strength and a risk of the portfolio. You have some very strong dedicated and scalable partners in this program, so you're naturally very reliant on some of these managers.

And speaking to the associated threat, finding talented managers who can be dedicated to CalPERS investment objectives and for whom CalPERS capital is a good and appropriate fit for their own organizations is not super easy. So that's where that comment comes from.

MR. GLICKMAN: There's also an issue with some of the managers who've had great success and who are in different actuarial cohorts than they were when that success was created. And whether those firms, several of which are pretty much captive to CalPERS - you're their only client - whether they'll be able to transfer the kind of same skills and grow their people in order to sustain a relationship for the next 20 years between them and CalPERS. That's something that requires a lot of attention, and a lot of monitoring, and is yet to be determined whether or not the next generation of management in those partners will be as strong and competent as the generation that has provided the extraordinary results.

COMMITTEE MEMBER JELINCIC: So the reference to, you know, some of whom were captive to CalPERS really is a reference to the fact that we have some who are going to retire on us relatively soon?

MR. GLICKMAN: It's something that over the next 10 to 15 years will have to be dealt with to make sure the transitions continue to provide strong talent who are incented and aligned with you.

COMMITTEE MEMBER JELINCIC: Okay. So -- but the problem is not that they're captive, it's that they are aging out or -- you know, before we quit paying benefits, they're not going to be around. I mean, is that really what you're --

MR. GLICKMAN: Yeah, I think that's true. When you have larger institutional managers for whom succession and training is done on a match larger scale, it's a different set of parameters than if you have what are smaller firms that are dependent on two or three key people.

COMMITTEE MEMBER JELINCIC: And can you comment on the staff compensation limits?

MR. GLICKMAN: You are one of the largest owners and managers of commercial real estate in the world. If you were spun-out just in real estate 180 degrees away from what you've just described, you would be in the top two dozen firms. The compensation system that's in place here is much, much different than the compensation systems among firms with whom you compete actively for assets.

The kind of profit sharing or participation that's available in private companies or in larger publicly held investment managers is very, very different than yours. And so there will always be, with this business model, some tension and some challenge in recruiting as many top-flight people as you would like to have compared to some of the ODCE managers or some of the opportunity fund managers.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Yeah, thank you. Yeah, we have just a comment. I hear you making reference to some of the same issues that Ted and Wylie talked about in terms of our 20-year vision, and it ties right in. What business model are we going to have? We know we're going to have this asset for a long, long time. And as you suggest, that when we're internationally investing and where is our interest in having our own people on the ground in these countries to get -- to have our best interests at hand.

So it's the same thing and I'm glad to hear that we're talking about it in all of our assets.

Ms. Priya -- Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you. I was also going to ask a question about the captive managers, because I think this is an issue, managers who only or predominantly do work for CalPERS. It's an issue not only in this asset class, but it's been an issue also in private equity. And the tradeoff has been that we are able to negotiate lower fees, et cetera, in exchange for sort of helping to start up these companies. And we've seen that as advantageous.

But I think this long-term question of the sustainability of that model is really worth exploring across the entire asset class. I think it's probably already been thought about quite extensively in private equity, but it sounds like something we need to have sort of a -- what -- how do we -- if we do start these types of companies, or help them to start, how do we grow them or what is the lifecycle of these relationships?

And so maybe that's something we need to think about across the entire portfolio and not just real assets.

CHAIRPERSON JONES: Okay. So who's next, Wilshire or StepStone?

MR. ALTSHULER: David Altshuler, StepStone.

Good afternoon. We were appointed as consultant for infrastructure to the Board starting in March of this year. So the comments that we have and the -- our experience with the program is somewhat limited from an annual review perspective. But I should note that -- and it goes to some of the organizational changes that have been implemented across the real asset group over the past several months.

Our visibility into the program, into investment thinking, due diligence, how staff contemplates policy Investment Beliefs is far deeper than it had been in the past, and I think has therefore given us, like, I think a lot of visibility into the program. And our ability to participate in Investment Committee meetings review and sit and listen to how staff, both the real estate and the infrastructure and risk and private equity team members, are discussing the asset class I think is very exciting, and for us, I think, helps us serve the Board better.

So I just wanted to start off by saying, even though it's been a relatively short amount of time, I think we've jumped right in.

I wanted to make a few remarks there are highlighted in our letter to you, and they echo comments that were already made, as well as some questions that have been raised by you. First off really is the market. I'll -- I don't want to beat a dead horse, but conditions are competitive.

I think what's important to note about infrastructure and maybe it's a little different than real estate, is that part of the competition has really been driven by the fact that it's a very desirable asset class from a long term -- in the context of a long-term liability structure.

You have increasing allocations to it from real estate, from fixed income, from private equity, and all over the world. So there is just an increasing amount of capital coming into this space, and it is all targeting what is by definition a limited set of assets.

So the fact that there's so much interest I think is not necessarily a bad thing. I think it reflects well on the asset class, but then it become a challenge for CalPERS to manage, because some of the advantages that CalPERS has being a very prominent investor, having a lower cost of capital than some other investors even being a U.S. dollar denominated investor are shared by other groups. And I can just tell you from experience there are a lot of offshore investors that are willing to put capital in the United States almost at any cost to be able to own high quality infrastructure assets. So that's a very high barrier to entry.

I think I'm excited about the strategic planning process, because I know that staff is very interested and engaged in trying to understand ways that CalPERS can be competitive in the market. And I think that will go to areas around diversification by geography. That's already started with, as you know, a very large commitment to an Australian manager. It was the first for the program or whether it's assessing other types of risks that CalPERS may be in a better position to manage and find fit with the program and its objectives.

You know, despite the fact that the market is tight, the program has been active in putting capital to work. There were, I think -- and this extends, you know, before our time, but 1.5 billion of commitments to new managers and accounts. And I should note also that these are not managers that are seated by CalPERS or only serving CalPERS. These are very well known, very reputable, top-tier international managers that are now working with CalPERS on a -- in the context of these accounts on an exclusive basis. And so I think that there has been activity and it should be noted.

You've heard about the performance. I won't go too much into it, other than to note that in addition to exceeding the benchmark, approximately 80 percent of the portfolio is invested in defensive and defensive plus assets. And so while outperforming the benchmark, the program is still, from a risk perspective, well within the program guidelines and the objectives.

I've touched on some of the program organizational changes. It's very early on to talk about the integration of real estate and infrastructure into a cohesive real assets unit, but I think that to some of the points made earlier, the focus really has been on creating consistency in investment discussion, investment decision making. And I think that it is always helpful to have views from outside the direct team that has been involved and has backgrounds in originating these types of investments.

And so it's a bit early on to assess the effectiveness of the reorganization, and it's still ongoing, but that's something that we're very actively following and involved in and we'll continue to keep you all updated on the progress there.

And maybe finally, I'll just touch on a few of the Investment Beliefs, which, you know, I've said this before to the Board. I think that the asset class itself is a very good fit in general with CalPERS Investment Beliefs as a long-term asset class focused on delivering income and stable returns over time.

I think that the -- as you've heard from staff, the focus on some of the internal and external initiatives around environment and government -- environment and governance and so forth are very positive. I think the question will be how to monitor these developments over time. I think to a question asked earlier, how can you predict how these assets will performed given climate change and so forth? Those are things that we really don't know, but I think the access to research, the access to managers that CalPERS has, I think the path forward is really continuing to press them on to providing responses to this -- to these questions.

From a risk standpoint, as I mentioned, I think -- and this is Investment Belief 7, I think the program has been very deliberate at focusing on risk. This goes to not only the types of investments that have been made but the number of deals that the program was not successful in bidding on. You're all aware of the discipline that staff has demonstrated, and I think that that really speaks to the importance of risk, and we've seen this in the discussions. There's a lot of very active discussion about that.

The account structures that CalPERS has negotiated, I don't want to say they're totally unique, but they are unusual in the market. And I think to Investment Belief 8, they are very much focused on cost and cost management. As lower returning asset class, costs always matter, but they matter a bit more to -- when you're dealing -- when you don't have that expectation of outsized returns.

And to Investment Belief 10, as we've discussed, I think the focus of this reorganization really is on streamlining an investment process, creating efficiency there. And I think that that should be positive. So I'm happy to take any questions.

CHAIRPERSON JONES: Okay. Thank you very much.

Yeah. I have a question on the PPP,

public-private partnerships. I think everybody is in agreement that the need is there. And a lot of the funds and plans are sitting on a lot of dry powder, and they're not able to allocate those assets to get the long-term returns that we need.

And in your notes, you mentioned that it's going real well internationally, but in the states it's way behind or marginal, if you may. And even some states are sponsoring legislation to deal with it. And even the U.S. government is talking about private-public partnerships.

What other workstreams do you believe are necessary to cross that hurdle of getting these three pieces together to begin to be able to allocate funds to this asset class and get the returns that we expect?

MR. ALTSHULER: It's a great question. And we did include the reference to P3s in the activity somewhat deliberately in the letter, because I think it's a question we get a lot. And there's a lot of -- it's one of these areas where there's a lot of interest, and especially in the U.S. in trying to participate.

I think in terms of workstreams, there's actually been a fair amount of discussion. And I think that I'm not sure of -- other than continuing to -- with the roundtables that CalPERS had done in the infrastructure areas across the asset classes, I think that was incredibly informative for the market in general to understand what kind of risk CalPERS is willing to accept, what the role of the program is, what its cost of capital is.

But I think quite honestly one of the challenges right now is we don't have a long track record of successful execution of these projects in the U.S. And if you look from a political point of view, and these are highly politicized projects, they take political will to push them forward, there's a lot of risk for people leading agencies and local governments to choose a P3 model when they could continue to use a traditional public finance model.

And so I think that as -- there have been projects that have been announced projects that are nearing completion. I think as the track record of successful P3s starts to build out, and you have examples of projects that have been completed on time, on budget, et cetera, and delivering outcomes to the public, and to investors, I think that there will be increased willingness to go down that path.

Another issue, quite frankly, though is really just some of the financing structures have not accommodated pension capital in the capital structure. And there's been a lot of discussion about that. There's been -- this summer there was an announcement from the Obama administration about a new form of bond that will sort of look like a private activity bond, but will manage some of the limitations around that. That lower cost of capital financing and the ability to put equity into deals like that is critical, because that's where the value is.

And so I think that really on those two fronts as you start seeing more activity and maybe more opportunity around the financing structure, there will be, I think, a better fit for P3s with pension capital.

CHAIRPERSON JONES: Okay. Thank you.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: In some ways, this is a follow up on Henry's question. In the U.S., we have this tax-free financing. And that's obviously a real barrier to participation. I've noticed that we're more successful overseas. Is the tax-free financing sort of a U.S. phenomenon or does it exist in the rest of the world.

MR. ALTSHULER: It is very much a U.S. phenomenon, and it is the single most important factor that is -- has informed the financing of public infrastructure in the U.S. So yeah, it is unique. There are governments outside the U.S. do not have access to that kind of low-cost financing.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Okay. Thank you.

No further questions. Thank you.

Next, Wilshire.

MR. JUNKIN: I think that will be me. Andrew Junkin with Wilshire. So it seems like just from some comments already, most of you could probably give my presentation for me, so I'll probably keep it pretty short.

You know, I think big picture, our view on forestland as an asset class is it's really a wonderful asset class for pension funds. It is a long lived asset. There is a tie to inflation. There is some control, as Mr. Jelincic noted, over when you harvest, so that you can time the sales to be more economical, and the whole while the trees are growing.

In addition, for you all, you know, forestland can align with your Investment Beliefs in unique ways that others don't. I mean you almost have your own carbon offset program, right, with a forestland program. And sustainable practices are both good for the investment, but also good for the environment.

However -- you knew this was going to come -- it's hard to invest in forestland at your size. And back to Controller Yee's question earlier about how did this sort of come to pass?

My recollection on the timing is this was 2007 on the purchases. A prior CIO obviously -- two prior, who had a vision to really have this be a significant part of the portfolio. And so it wasn't just intended to be these two purchases. But then 2008 rolled through and there was plenty of other things to focus on. And building out a forestland portfolio at the time really kind of dropped to 95th on the priority list. And so it's just held these two assets for a very long time.

So getting it implemented is a challenge at your size. And this is the price of being the nation's largest public pension fund, not all asset classes are accessible to you in easily implementable ways, no matter how much you like them.

So I think I've given this same presentation for a few years. I'm not going to dig into all of the reasons for the underperformance. I think those are pretty well known. But I think -- and we've talked to Paul about this -- for the strategic plan, you're getting to a point where you really either have to commit to this asset class and scale up, and that could take maybe a decade or more, or it may be time to get out.

Now, that's not to say you'd have a -- I don't really want to say a fire sale on timber. That sounds inappropriate --

(Laughter.)

MR. JUNKIN: But you don't want to rush for the exits necessarily. You'd want to maximize the value, if that's what you choose to do. But having two very different assets, leads to performance that you may not really enjoy, as we've seen over the past five years. And without someway to build out of well diversified portfolio in terms of geography and wood types, it's going to be a challenge I think on an ongoing basis.

So I'll stop my comments there. I'm happy to take any questions. Our letter sort of stands on its own, and it should look pretty familiar over the past several years.

CHAIRPERSON JONES: Yeah. No further questions. Like you said, you've presented that viewpoint a number of times.

MR. JUNKIN: Yeah, I have.

CHAIRPERSON JONES: So okay thank you for -- and that concludes the report on the consultant's review of real assets. So thank you very much for your presentations.

And we will move to the next Item, 9c, Responsible Contractor Policy Program Annual Update.

INVESTMENT DIRECTOR WEIR: Good afternoon. Laurie Weir, Targeted Investments. I'm pleased to present the Responsible Contractor Program Annual Report for the '14-'15 Fiscal Year.

CalPERS has a deep interest in the condition of workers employed at CalPERS-owned assets. To that end, CalPERS takes considerable effort to assure the payment of fair wages and fair benefits based on local market conditions subject to fiduciary principles.

The RCP seeks to secure the condition of workers without adverse effect on investment returns, access to investment opportunities, or significant costs. The RCP policies provide an important risk management function in the identification and mitigation of labor risks across the real estate and infrastructure portfolios.

The RCP policies support Investment Belief number 4 to create long-term value through the effective management of financial, physical, and human capital. Effective management of human capital increases the likelihood that companies will perform over the long term and manage risk effectively.

The policies also support Investment Belief number 3 related to engagement with interested stakeholders which we do in the administration of this policy on a regular basis. For the '14-'15 reporting year, managers reported a combined 99.49 percent compliance with the policy. CalPERS investment managers paid approximately $1.4 billion to responsible contractors during the reporting period.

And that ends my presentation. I'm happy to answer questions.

Thanks very much.

CHAIRPERSON JONES: Thank you very much for your presentation.

Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Ms. Weir, I just want to congratulate you on the compliance. That's awesome. So the program is working very well. I'm very happy to see that, and it's great to see it's integrated into our program, like -- as well as it has been. Thank you so much.

INVESTMENT DIRECTOR WEIR: Thank you.

CHAIRPERSON JONES: Okay. Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: The same questions I ask every year. What do we do in terms verifying and testing the data that we're getting?

INVESTMENT DIRECTOR WEIR: So the policy establishes an interwoven set of roles and responsibilities between the managers and the contractors and staff and labor stakeholders in administering and monitoring this policy.

Importantly, managers are responsible for their and their contractor's compliance with the policy. Managers are taking their responsibilities for seriously as evidenced by the dedication of their time and their staff time, heightened reporting requirements, and their outreach and engagement with labor representatives to administer the policy.

The policy states that a pattern of noncompliance with the policy may result in termination of that manager. And I -- you've asked the question and I've said a couple years, that's a pretty high standard. I'm going to get to a more specific answer to your question in just a moment.

Further evidence of policy compliance is that over the past several reporting periods, no formal complaints have been received that allege failure to pay fair wages and benefits. It has been and will continue to be staff's goal to engage with labor representatives and managers in very positive efforts to assure that managers are aware of responsible contractors for bidding opportunities, and that fair wages and benefits are paid on CalPERS-owned assets.

The way certification works is that contractors and subcontractors, and when managers contract directly for work, managers self-certify that they have paid fair wages and benefits based on their local market conditions. As contractors and subcontractors self-certify, those certifications are rolled up to the managers, and the managers review and carefully assure that they confirm and believe that fair wages and benefits have been paid.

The managers in turn inform staff, through a annual survey process, of the compliance of their contractors and subcontractors. Staff does not review specifics unless complaints are brought under the policy. And so we do take some comfort in the fact that we have not had formal complaints under the policy for several program years running.

COMMITTEE MEMBER JELINCIC: And I would -- Ken will kill me, even though he's retired, if I don't point out that it's kind of difficult to file a complaint when you don't know about the opportunity and can't get a list of the properties covered.

INVESTMENT DIRECTOR WEIR: Importantly, the policy sets forth that our managers and labor engage directly with one another on the administration of the policy. When labor requests a list of assets, managers under the policy are obligated to provide that list of assets. And so we do believe that labor is receiving information on CalPERS assets from the managers. I hope that's helpful.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON JONES: Okay. Thank you.

No further questions. Thank you for the report, Laurie on that.

We do have a request to speak on this item. Michael Ring from SEIU.

MR. RING: Hello, everyone, again, Chairman Jones, Board. Thank you for the opportunity. Michael Ring with SEIU's Capital Stewardship Program.

I have a statement to share from some of our leaders, and my colleague Marguerite Young, who many of you are familiar with who helped run this work for us.

So we greatly appreciate the work of the staff to support risk management of the real estate portfolio. As you know, we represent janitors and security officers who work at the buildings that CalPERS owns in major U.S. markets. We have established a responsible contractor rating program in recent years to fulfill our duty under the policy to provide the fund and its partners with lists of responsible contractors.

For the first time last year, we were in the position of downgrading a contractor, Universal Protection Services, UPS, from a green to yellow caution rating across California markets. You may recall that the workers -- that workers testified to your Board about some the issues involved with you UPS in your May investment Committee meeting.

I'm happy to report that just last night we were able to restore UPS to a green status, and we much appreciate CalPERS diligent and thoughtful engagement on this matter. On other fronts we have grown relationships over the past year with several of your managers, including CommonWealth Partners, GI Partners, and CIM, and appreciate their commitment to the highest standards in this industry.

The contracts for janitors in nearly all markets where SEIU represents members expire over the course of the next 12 months. Many contracts on the east coast expire on New Year's Eve, and our California contracts are up in May.

Even with the union, nearly 40 percent of SEIU janitors earn less than $15 per hour. Our hope is to bring all of our workers over this threshold throughout the next contract cycle.

We are also looking to raise standards for all property services workers who do not have the benefit of a union. Here in California, we are investigating legislation to curb workplace violence against women in our industry. We are looking also at legislation around enforcement of wage theft, SB 588, and identifying opportunities to expand green cleaning and operations.

The RCP is one of CalPERS strongest human capital management tools. As the fund looks ahead to how to incorporate tools to the manage labor risk and to address the long-term value of sustainable labor practices, we encourage you to link the RCP to these efforts and to build upon its foundation.

And we thank this fund and the staff for all your great work and leadership in helping develop this really groundbreaking human capital management strategy known as the Responsible Contractor Policy.

Thank you very much both on behalf of our beneficiaries in the fund and the workers we represent in the industry who are helping to ensure that your buildings have the value that they merit. Thank you very much.

CHAIRPERSON JONES: Okay. Thank you, Michael, for sharing your views with the Investment Committee.

We have a question. Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

I want to just say to Laurie, thank you for all your work on this. This is really a great policy. I think Mr. Ring kind of highlighted a couple things I wanted to just see if we could try to help facilitate, if not already, and that is if there are labor complaints that don't necessarily bubble up through the manager or labor kind of context. Is there kind of a single point of contact that is here in CalPERS to receive them, and can we be sure that that's really well known?

We've had issues with the underground economy for a long time in the state. And I think even for as much as we try to coordinate with the various State agency stakeholders on those, the one issue that's always become -- that's been the common among complainants is that they don't know where to go.

And so I just want to be sure that is really clear and visible and highlighted, otherwise the policy really is not going to reach those that probably are subject to the most egregious violations.

INVESTMENT DIRECTOR WEIR: I really appreciate your comment. I think it's a good point to the end of making it clear that, A, we have a policy, we have dedicated staff for the policy. In our Investment Office website improvement process, we established a portion of the website that is dedicated to the Responsible Contractor Program policies, it includes our list of all of our active managers under the policy their key contact people and the method to contact our managers, as well as to know that we -- that you can communicate directly with CalPERS Investment Office and CalPERS staff.

You know, Carrie Douglas Fong's name has been mentioned before this Board in the past. I'll mention it again. She's an extraordinary outreach person and she has done everything within her power sitting within the confines of the Investment Office to make it known that this policy exists, and that there are active staff engaging in administering the policy.

I think this is something that we can continue to look at. And as we find ways of improving the communication about the fact that the policy exists, we will certainly endeavor to do that and report to the Board on those efforts.

COMMITTEE MEMBER YEE: That's great. Thank you so much.

CHAIRPERSON JONES: Thank you. No further questions. Thank you, Laurie.

Okay. Let's move then to Item 10, Proposed Revisions to the Real Estate -- Real Assets Policy, First Reading.

INVESTMENT DIRECTOR CROCKER: Thank you, and good afternoon. Kit Crocker, Investment Office staff.

Item 10a is the first reading of a proposed interim revision to the real assets investment policy in the form of a new Attachment D.

The sole purpose of Attachment D is to incorporate into the investment policy the limits and constraints currently contained in the real assets delegation. This interim step is part of a broader effort to streamline, clarify, and align investment policies across the Investment Office. It makes no change to current authorities, limits, or constraints.

The full migration of the real assets policy to the new format is being deferred until next year to take place in conjunction with the development of the new strategic plan for real assets.

So as this is an information item only for today, with that, I will ask if there are any questions.

CHAIRPERSON JONES: Okay. Seeing no further -- no questions. Thank you very much for the presentation.

So that moves us to summary of Committee direction. And we've already talked about the two on the private equity and also mentioned that you will be providing us the information in response to Mr. Costigan's question of breaking out forestland and infrastructure data.

So I had no other -- no further direction. Ted, did you have any that you --

CHIEF INVESTMENT OFFICER ELIOPOULOS: Just one, which is near and dear to the Committee Chair's heart, that we'll also look at the strategic planning cycle and the workshop cycle to include visioning exercise for the long term.

CHAIRPERSON JONES: And I'm glad I mentioned that.

(Laughter.)

CHAIRPERSON JONES: Okay. Thank you. Okay. So what we will -- oh, no requests to speak, so we're going to break, and when we return and reconvene, we will be reconvening into closed session. So we're going to break for lunch. And so that's the end of the open session. Thank you very much.

(Thereupon California Public Employees' Retirement System, Investment Committee meeting open session adjourned at 12:38 p.m.)

C E R T I F I C A T E OF R E P O R T E R

I, JAMES F. PETERS, a Certified Shorthand Reporter of the State of California, do hereby certify:

That I am a disinterested person herein; that the foregoing California Public Employees' Retirement System, Board of Administration, Investment Committee open session meeting was reported in shorthand by me, James F. Peters, a Certified Shorthand Reporter of the State of California, and was thereafter transcribed, under my direction, by computer-assisted transcription;

I further certify that I am not of counsel or attorney for any of the parties to said meeting nor in any way interested in the outcome of said meeting.

IN WITNESS WHEREOF, I have hereunto set my hand this 16th day of December, 2015.

James F. Peters

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