

**Federal Investment Policy Report for the CalPERS Board
 March 2016**

I. Securities

1. **Brief Summary of Issue.** Policy developments related to the Securities and Exchange Commission (“SEC”), corporate board diversity and climate risk disclosure, SEC nominations, corporate governance, and the Public Company Accounting Oversight Board’s (“PCAOB”) budget.
2. **Developments Since Last Report.**
 - **Board Diversity.**
 - *Legislation.* Rep. Carolyn Maloney (D-NY) introduced H.R. 4718, the “Gender Diversity in Corporate Leadership Act of 2016” to require the SEC to establish a Gender Diversity Advisory Group comprised of representatives from government, academia and the private sector to study and report to the SEC and Congress on recommendations to increase gender diversity on corporate boards. The bill would also require the SEC to write rules to require public companies to disclose to shareholders the gender composition of their boards of directors and nominees to their boards of directors. H.R. 4718 has been referred to the House Financial Services Committee, which has not yet acted on it; and
 - *Letter to SEC.* Senate Banking Committee Ranking Member Sherrod Brown (D-OH) and House Financial Services Committee Ranking Member Maxine Waters (D-CA) led a bicameral group of Democratic Members of Congress in sending a letter to SEC Chair Mary Jo White urging the SEC to quickly seek public comment on the CalPERS-supported 2015 petition for rulemaking that sought to require public companies to provide more specific details about the diversity of their corporate boards.
 - **Nominations.** The Senate Banking Committee held the nomination hearing for Lisa Fairfax (a Democrat) and Hester Peirce (a Republican) to be SEC Commissioners. Committee Chairman Richard Shelby (R-AL) did not provide a specific timeline of when the full Committee would vote on the nominations, but said that he will try to move forward as soon as he can. If the full Senate confirms Ms. Fairfax and Ms. Peirce, the five-member SEC will have a full complement of Commissioners.
 - **Climate Risk.**
 - *Exxon Proxy Proposal.* The SEC’s Division of Corporation Finance informed Exxon Mobile that the company must include a climate change proposal in its shareholder proxy materials. CalPERS supported efforts to ensure that shareholders are permitted to vote on the proposal. If approved, the proposal would require Exxon to outline for investors how its profitability may be impacted by climate change and legislation designed to address it; and
 - *Legislation.* Rep. Matt Cartwright (D-PA) introduced H.R. 4792, a bill that would require the SEC to update its oil and gas mining industry guides and to work with the SEC’s Investor Advisory Committee on appropriate disclosures to include in the update. H.R. 4792 was referred to the House Financial Services Committee. An identical bill (S. 2716) has been introduced in the Senate by Senator Jack Reed (D-RI) and was

referred to the Senate Banking Committee. Neither Committee has yet acted on the legislation.

- **Universal Proxy.** SEC Division of Corporation Finance staff signaled that the division is considering recommendations about the use of universal proxy ballots in corporate board elections from the perspective of the shareholder. According to SEC staff, the Division of Corporation Finance is also considering whether the use of universal proxy cards should be mandatory. In addition, SEC staff noted that the appearance of universal proxy cards is also being considered. It is not yet clear when a recommendation will be made to the SEC or whether the SEC will adopt a universal proxy ballot rule.
- **PCAOB Budget.** The SEC approved a \$257.7 million budget and accounting support fee for the PCAOB for 2016. The PCAOB's 2016 budget, which represents a 3 percent increase over last year, will be funded largely by the collection of an accounting support fee totaling \$253.3 million. SEC Chair White and Commissioner Kara Stein voted in favor of the budget, while Commissioner Michael Piwowar voted in opposition.
- **SEC-related Legislation.** The House Financial Services Committee marked up and reported favorably to the full House the SEC-related bills below. No action to date has occurred in the Senate on the legislation.
 - H.R. 3798, the "Due Process Restoration Act of 2015." Introduced by Rep. Scott Garrett (R-NJ), H.R. 3798 would allow defendants to compel the SEC to seek sanctions by filing an action in federal court instead of an administrative action. The bill would also change the standard of proof in SEC administrative proceedings to "clear and convincing." H.R. 3798 passed the Committee by a vote of 32-25;
 - H.R. 4638, the "Main Street Growth Act." Introduced by Rep. Garrett, H.R. 4638 would require the SEC to approve or deny the application of a venture exchange within six months or the application would be deemed approved. H.R. 4638 passed the Committee by a vote of 32-25;
 - H.R. 4620, the "Preserving Access to CRE Capital Act of 2016." Introduced by Rep. French Hill (R-AR), the bill would reduce the Dodd-Frank Wall Street Reform and Consumer Protection Act's risk retention requirements for transparent and high performing single asset single borrower loans, qualified commercial real estate loans, and certain subordinated tranches of commercial mortgage backed securities. H.R. 4620 passed the Committee by a vote of 39-18;
 - H.R. 4139, the "Fostering Innovation Act of 2015." Introduced by Rep. Kyrsten Sinema (D-AZ), the bill would amend provisions of the Sarbanes-Oxley Act to provide a temporary exemption for low-revenue issuers from the internal control audit requirement. H.R. 4139 passed the Committee by a vote of 42-15; and
 - H.R. 4498, the "Helping Angels Lead our Startups Act." Introduced by Rep. Steve Chabot (R-OH), the bill would require the SEC to amend Regulation D to allow general solicitation and general advertising presentations to angel investor groups, among other groups. H.R. 4498 passed the Committee by a vote 44-13.

3. **Implications for CalPERS.**

- Efforts to provide additional information to investors about corporate board diversity and climate risk could provide CalPERS and other investors with additional information on which to base investment decisions to produce long-term shareowner value;

- The Division of Corporation Finance’s decision regarding the Exxon proposal could provide CalPERS and other investors in Exxon a better understanding of the company’s plans to address climate change; and
 - Possible SEC action concerning universal proxy ballots could create an opportunity for engagement by CalPERS with the SEC on the issue, given CalPERS’ view that proxy access is a fundamental shareholder right.
4. **CalPERS/Federal Representative Actions.**
- CalPERS Investment Committee Chair Henry Jones met with Ranking Congressional Member Maxine Waters on March 23, when he was in Washington D.C. for the CII Conference. General Counsel Matthew Jacobs also participated in the meeting. Mr. Jacobs also met with SEC representatives while he was in Washington D.C.
5. **Recommendations for Next Steps.** We will continue to:
- Monitor H.R. 4718, and press for the addition of ethnic to gender diversity in other potential legislative proposals;
 - Monitor the Senate Banking Committee’s possible vote on Ms. Fairfax and Ms. Peirce following their confirmation hearing;
 - Monitor possible responses to the Supreme Court’s stay of the CPP; and
 - Provide updates on other legislative and regulatory issues and recommend action by CalPERS, as warranted.

II. Derivatives

1. **Brief Summary of Issue.** Policy developments related to Commodity Futures Trading Commission (“CFTC”), including nominations and CFTC actions related to position limits and transatlantic efforts to harmonize derivatives rules.
2. **Developments Since Last Report.**
- **Nominations.** The White House announced the nominations of Chris Brummer (a Democrat) and Brian Quintenz (a Republican) to replace former CFTC Commissioners Mark Wetjen and Scott O’Malia. Mr. Brummer, a law professor at Georgetown University Law Center, has focused his academic work on investor protection, finance and global governance issues. Mr. Quintenz is the founder of Washington-DC based investment firm Saeculum Capital Management and previously served as a staff member for former Rep. Deborah Pryce (R-OH). The Senate Agriculture Committee is expected to take up the nominations in the near future. If the full Senate confirms Mr. Brummer and Mr. Quintenz, the five-member CFTC will have a full complement of Commissioners.
 - **Position Limits.**
 - *EEMAC Report.* CFTC Commissioner J. Christopher Giancarlo announced the withdrawal of a non-binding report issued on February 25, 2016 by the CFTC’s Energy and Environmental Markets Advisory Committee (“EEMAC”). Commissioner Giancarlo is the sponsor of the EEMAC. The EEMAC’s report, which recommended that the CFTC stop considering its position limits rules for commodities futures and swaps, was met with criticism from Sen. Elizabeth Warren (D-MA) when it was released; and

- *Letter to CFTC.* A group of Senate Democrats sent a letter to CFTC Chairman Timothy Massad urging the CFTC to quickly finalize its rules for speculative position limits, including aggregation position limits. The signatories to the letter include Ranking Member Sherrod Brown and Sens. Dianne Feinstein (D-CA), Maria Cantwell (D-WA), and Joe Donnelly (D-IN).
 - **Cross-border Harmonization.** The CFTC approved a substituted compliance determination for dually-registered central counterparties (“CCPs”) that are located in the European Union (“EU”), as well as a comparability determination concerning certain EU rules. The Commission’s action follows a recent CFTC-European Commission (“EC”) agreement to harmonize EU and U.S. regulations concerning CCPs. The CFTC stated that its staff and their European counterparts will continue efforts to ensure the agreed approach is applied consistently and appropriately.
3. **Implications for CalPERS.** Possible consideration of nominees to the CFTC could provide CalPERS and other derivatives market participants a greater sense of certainty as the CFTC pursues its 2016 regulatory agenda, including an expected position limits rulemaking and additional cross-border harmonization efforts.
 4. **CalPERS/Federal Representative Actions.** Ongoing monitoring of relevant legislative and regulatory developments related to the CFTC.
 5. **Recommendations for Next Steps.**
 - Monitor the Senate Agriculture Committee’s possible confirmation hearings for Mr. Brummer and Mr. Quintenz; and
 - Provide updates and recommend action by CalPERS, as warranted, including commenting on relevant rulemakings and legislative proposals.

III. Housing Finance

1. **Brief Summary of Issue.** Policy developments related to housing finance, particularly issues regarding the secondary mortgage market.
2. **Developments Since Last Report.**
 - **GSE Progress Report.** The Federal Housing Finance Agency (“FHFA”) released a report assessing the progress of Fannie Mae and Freddie Mac (the “GSEs”) toward meeting the performance goals contained in the 2015 GSE “Scorecard.” Of particular interest for CalPERS, the report provides an update on the GSEs’ ongoing efforts to develop the Common Securitization Platform (“CSP”). The CSP is being developed by Common Securitization Solutions (“CSS”), which is jointly owned by the GSEs, and will be implemented in two phases. According to the report, the FHFA anticipates that in the first phase Freddie Mac will begin using the CSP in the fourth quarter of 2016. The report notes that the FHFA expects to announce a specific date later this year. The also report indicates that the FHFA anticipates that both of the GSEs will begin using the CSP to issue single securities in 2018. Going forward, the report notes that the FHFA will continue to solicit stakeholder input on these initiatives “with the objective of improving overall secondary mortgage market liquidity while mitigating any risk of market disruption.”

- **FHFA Director Speech.** FHFA Director Melvin Watt delivered a speech in which he announced that the FHFA will be unveiling its decision to start a principal reduction program within the next 30 days. All indications suggest that the decision will allow principal reductions in limited circumstances for deeply delinquent, underwater loans. Those familiar with the discussions estimate the program to be limited and only target around 50,000 homeowners. A key component of eligibility for the write-down is likely to be a GSEs cost-benefit analysis that concludes the principal reduction would cost the GSEs less than a foreclosure. Any principal reduction program directed by the FHFA to the GSEs could be concerning for investors. During the same speech, Director Watt hinted at the work stream in place to develop a permanent Home Affordable Modification Program/Home Affordable Refinance Program (“HAMP/HARP”) (expiring this year) streamlined refinance program. Thus far, our industry contacts suggest that the permanent program that is currently under consideration would be limited to very high LTV loans, loans originated after the expiration of HARP/HAMP eligibility, available/activated in limited geographies going through temporary hardship, and loans already participating in HARP would not be eligible.
 - **GSE Reform Paper.** A small group of influential housing experts published a paper entitled, “A More Promising Road to GSE Reform.” This 11 page paper outlines an alternative approach to comprehensive GSE reform that would charter a new government corporation, make the government guarantee explicit, and ensure that the new entity only absorbs the catastrophic credit risk. In so doing, it would require the private market to absorb all expected credit losses. This paper is expected to be followed by a number of other proposals from think tanks and policymakers weighing in on alternative approaches to comprehensive GSE reform.
3. **Implications for CalPERS.** Changes to housing finance policy could impact market liquidity and stability thereby impacting CalPERS’ investment returns.
 4. **CalPERS/Federal Representative Actions.** Ongoing monitoring of relevant regulatory and legislative developments related to the secondary mortgage market.
 5. **Recommendations for Next Steps.** We will provide updates and recommend action by CalPERS, as warranted, including commenting on relevant rulemakings and legislative proposals.