

Investment Compliance Program Annual Review

August 15, 2016

Executive Summary

- Investment compliance core functions established since the inception of the program in FY 2011-12 are now mature
- ICOR led several key strategic initiatives during the FY 2015-16 that further aligns INVO with its Target Operating Model:
 - Investment policy revision project (Phase II)
 - Divestment compliance functional realignment
 - Development and integration of ODD programmatic functions
- ICOR is a key component of the CalPERS Five-Year Compliance Plan* adopted in June 2015

* Page 6 in agenda item 5a, Attachment 1 presenting the 2015-17 Enterprise Compliance Plan to Risk and Audit Committee on June 16, 2015

Review Outline

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Legend: Investment Beliefs Map

<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="background-color: #003366; color: white; text-align: center;">1</td><td>Liabilities</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">2</td><td>Long-Term Horizon</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">3</td><td>Stakeholders</td></tr> </table>	1	Liabilities	2	Long-Term Horizon	3	Stakeholders	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="background-color: #003366; color: white; text-align: center;">4</td><td>Three Forms of Capital</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">5</td><td>Accountability</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">6</td><td>Strategic Allocation</td></tr> </table>	4	Three Forms of Capital	5	Accountability	6	Strategic Allocation	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="background-color: #003366; color: white; text-align: center;">7</td><td>Risk Reward</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">8</td><td>Costs Matter</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">9</td><td>Multi-faceted Risk</td></tr> </table>	7	Risk Reward	8	Costs Matter	9	Multi-faceted Risk	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td style="background-color: #003366; color: white; text-align: center;">10</td><td>Resources/Process</td></tr> <tr><td style="background-color: #003366; color: white; text-align: center;">↑</td><td>Alignment Changes or Improvement</td></tr> </table>	10	Resources/Process	↑	Alignment Changes or Improvement
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Program Role, Governance & Oversight

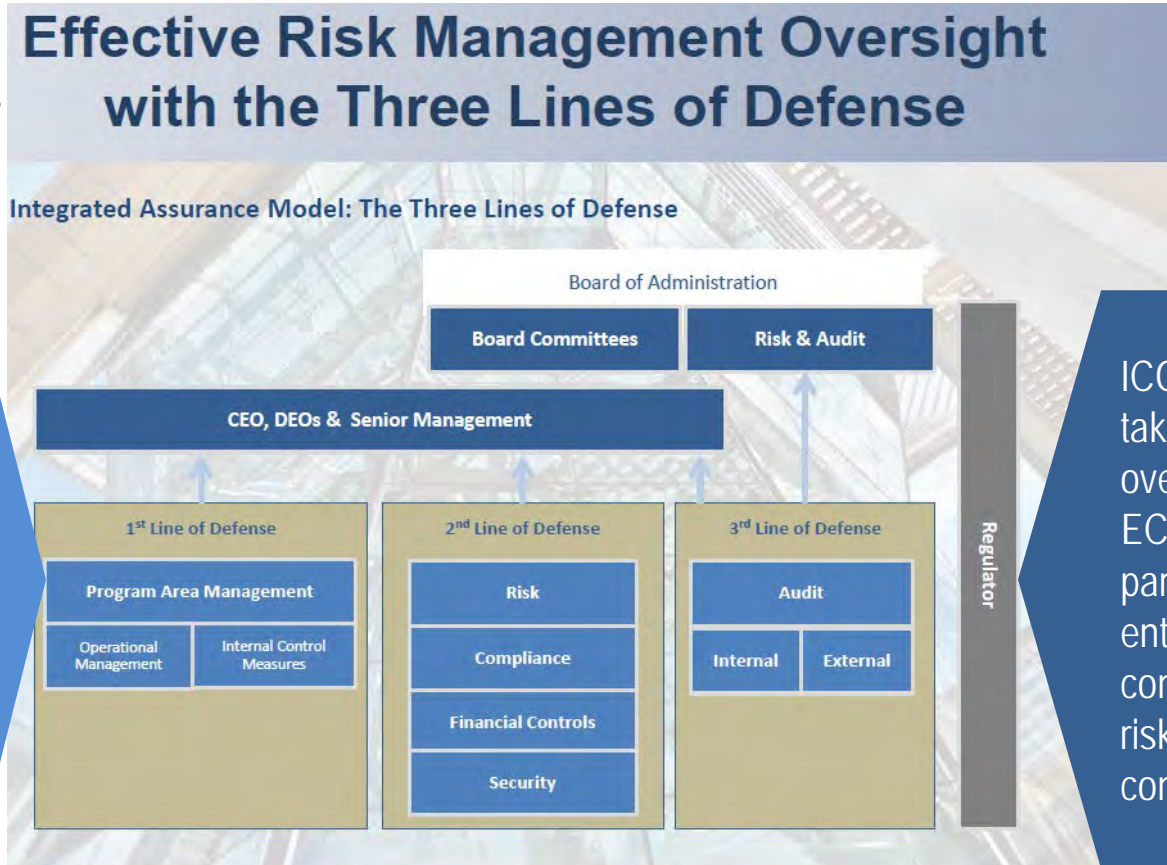
Core Function Capabilities

- ICOR functions are modeled on best practices employed by SEC-registered investment advisers
- Role is to ensure that INVO maintains ongoing compliance with regulatory and investment policy requirements
- ICOR staff, in concert with INVO senior management, seeks to promote a culture of compliance

Program Role, Governance & Oversight (continued)

CalPERS Enterprise Compliance Framework

Key Point: ICOR plays an integral role in the “Three Lines of Defense” of Defense”



ICOR, as an embedded compliance function, is part of the “1st line of defense” as well as independent check and balance on the investing functions

ICOR activities take place with oversight from ECOM and ICOR participates on enterprise-wide compliance and risk governance committees

Program Role, Governance & Oversight (continued)

Investment Compliance Program Responsibilities



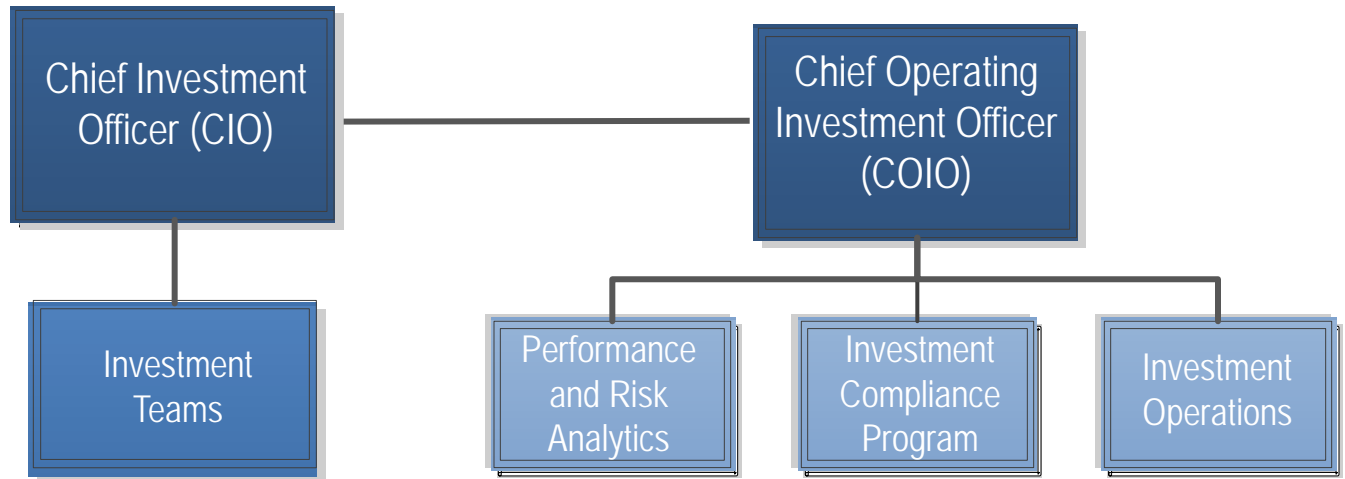
Business Model

Organizational Alignment

Investment Teams Supported by Dedicated Functional Groups

Key Point:

Risk taking, and risk monitoring and control functions, are separate



Team-Oriented Approach with Support Areas that act as Key Internal Partners While Maintaining Clear Segregation of Duties

Investment Compliance Core Functions

Function	Selected FY 2015-16 Accomplishments and Milestones
Surveillance, Testing & Reviews	<ul style="list-style-type: none"> • Enhanced compliance controls in BlackRock Aladdin and Charles River systems supporting Global Fixed Income and Global Equity portfolio management • Partnered with ECOM to enhance the external manager Form 700 review and communication process
Policies & Procedures	<ul style="list-style-type: none"> • Policy revisions completed for the Total Fund and all Asset Class Policies <ul style="list-style-type: none"> ○ Resulted in a substantial reduction in number of investment policies, standardization and clarity of policy language, and increased efficiency for ongoing maintenance activities • Developed framework and implemented new Investment Policy Procedures and Guidelines as part of the policy revisions project
Education & Training	<ul style="list-style-type: none"> • Organized and administered enhanced investment compliance training for Investment Office staff <ul style="list-style-type: none"> ○ Bifurcated curriculum into core (ethics and conflicts of interest) and elective training tracks ○ Piloted elective training to review the impact of Dodd-Frank on the private and public asset classes
Regulatory Research & Engagement	<ul style="list-style-type: none"> • Designed and implemented compliance rules for securities trading systems of public markets asset classes to monitor thermal coal divestments in light of California Senate Bill 185 (De León) • Reviewed and tested applicable PERL requirements and remediated gaps

Strategic Initiatives

Operational Due Diligence (ODD) Implementation

- Significant progress implementing external manager ODD reviews:
 - Private Equity: ODD required for all new funds
 - Global Equity and Fixed Income: Manager ODD required for new investment relationships
- FY 2016-17 initiatives:
 - Real Assets: Further integration of ODD
 - Design and pilot new process for risk-based compliance testing of CalPERS partnership agreements



Strategic Initiatives (continued)

Initiative	Manager Review & Monitoring Functionalization	Divestment Functional Realignment	Investment Policy Revision Project
Accomplishments (Through End of FY 2015-16)	Developed baseline standards and implemented manager monitoring tools and processes for each asset class	Assumed oversight, administration, and reporting responsibilities for all CalPERS-related divestment initiatives	Aligned the various asset class investment policies with the new total fund framework, resulting in a substantial reduction - approx. 49 to 19 so far - of the number of investment policies, standardization and clarity of language, and efficiency for ongoing maintenance activities

Appendices

Appendix 1: Investment Compliance Training

Mandatory Annual Investment Compliance Training Curriculum

Core Module (2012 – 2015 Topics)

Ethics	Conflicts of Interest	Transparency
<ul style="list-style-type: none"> Statement of Incompatible Activities for Officers/Employees Staff Ethical Decision-Making Policy CalPERS Restricted Contact Policy Attorney Client Privilege 	<ul style="list-style-type: none"> FPPC Form 700 Filing CalPERS Gift Policy Placement Agent Policy and Regulation Personal Trading Regulations CalPERS Restricted List Process Contracts Related Disclosures 	<ul style="list-style-type: none"> Employee Confidentiality Policy Public Records Act Portfolio Holdings Disclosure Policy Records Retention

Additional Core Focus Areas (2012 – 2015)

Elective Module Tracks

Industry Compliance Topics	CalPERS Compliance Topics	2015	2016
<ul style="list-style-type: none"> Derivatives & Counterparty Risk Operational Risk & Operating Events 	<ul style="list-style-type: none"> Approval of Outside Employment Post-Employment Restrictions Using the Ethics Helpline Bagley-Keene Open Meeting Act Role of Stakeholders at CalPERS Protocols and Guidelines for CalPERS Board Communication with Staff Undue Influence Policy External Investment Resource Conflict of Interest Prohibition of Honorarium 	<p>Dodd-Frank: Public Markets</p> <ul style="list-style-type: none"> ✓ Expansion of Antifraud Provisions ✓ Volker Rule ✓ Enforcement Cases Studies <p>Dodd-Frank: Private Markets</p> <ul style="list-style-type: none"> ✓ SEC Examination Approach for Advisers to Private Funds ✓ SEC Focus Areas for Advisers to Private Funds 	<p>Public Markets Asset Classes:</p> <ul style="list-style-type: none"> ○ Fiduciary Duty Concepts (TBD) <p>Private Markets Asset Classes:</p> <p>PE Academy Pilot Partnership:</p> <ul style="list-style-type: none"> ✓ Conducting and interpreting Operational Due Diligence Reviews ✓ Conducting and Interpreting Form ADV reviews