

Federal Investments Report for CalPERS Board September 2016

- I. *Oppose H.R. 5424, the “Investment Advisers Modernization Act of 2016” (Rep. Hurt)***
1. **Brief summary of issue.** Developments related to H.R. 5424, the “Investment Advisers Modernization Act of 2016.” Introduced by Rep. Robert Hurt (R-VA), the bill would revise certain requirements for investment advisers and create an exemption for private equity funds from various books and records requirements.
 2. **Specific changes/developments since last report.** H.R. 5424 was introduced on June 9, 2016. The House Financial Services Committee reported the bill favorably to the full House on June 16, 2016. The bill is scheduled for a House Floor vote during the week of September 5.
 3. **Implications for CalPERS.** A reduction in required disclosures by U.S. private equity fund managers could hamper CalPERS’ ability to effectively monitor its fund managers. Additionally, provisions of the bill would reduce reporting requirements that could adversely impact investor protections and the assessment of systemic risk.
 4. **CalPERS/Federal Representative Actions.** Sent a letter in June 2016, to House Financial Services Chairman Jeb Hensarling (R-TX) and Ranking Member Maxine Waters (D-CA) in opposition to the bill.
 5. **Recommendations for Next Steps.** Transmitted the Hensarling-Waters letter to House Majority Leader Kevin McCarthy (R-CA) and Minority Leader Nancy Pelosi (D-CA) in advance of Floor consideration of the bill. Although H.R. 5424 is expected to pass the House, it is not anticipated that the Senate will take up the bill.
- II. *Oppose H.R. 5311, the “Corporate Governance Reform and Transparency Act” (Rep. Duffy)***
1. **Brief summary of issue.** Developments related to H.R. 5311, the “Corporate Governance Reform and Transparency Act.” Introduced by Rep. Sean Duffy (R-WI), the bill would require the registration of proxy advisory firms and the management of conflicts of interest, among other things.
 2. **Specific changes/developments since last report.** H.R. 5311 was introduced on May 24, 2016. The House Financial Services Committee reported the bill favorably to the full House on June 16, 2016.
 3. **Implications for CalPERS.** The bill would establish an entirely new, but largely unnecessary and burdensome regulatory regime for proxy advisory firms and would negatively impact investors that utilize proxy advisory services.
 4. **CalPERS/Federal Representative Actions.** Included CalPERS’ perspective about H.R. 5311 as part of a letter to Chairman Hensarling regarding the discussion draft of the Financial CHOICE Act in July, 2016.

5. **Recommendations for Next Steps.** Continue engagement with House Financial Services Committee leadership and staff, and consider possible engagement with other Members of Congress to help advance CalPERS’ objective of defeating the bill.

III. *Oppose H.R. 5429, the “SEC Regulatory Accountability Act” (Rep. Garrett)*

1. **Brief summary of issue.** Developments related to H.R. 5429, the “SEC Regulatory Accountability Act.” Introduced by Rep. Scott Garrett (R-NJ), the bill would require the Securities and Exchange Commission (“SEC”) to consider the costs and benefits of its regulations and to conduct a review to determine whether existing regulations are “outmoded, ineffective, insufficient or excessively burdensome.”
2. **Specific changes/developments since last report.** H.R. 5429 was introduced on June 9, 2016. The House Financial Services Committee reported the bill favorably to the full House on June 16, 2016.
3. **Implications for CalPERS.** The imposition of additional cost-benefit analysis would divert scarce resources from the SEC’s core mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation.
4. **CalPERS/Federal Representative Actions.** Sent letter to Chairman Hensarling and Ranking Member Waters in opposition to the bill.
5. **Recommendations for Next Steps.** Continue engagement with House Financial Services Committee leadership and staff, and consider possible engagement with other Members of Congress to help advance CalPERS’ objective of defeating the bill.

IV. *Support H.R. 4718, the “Gender Diversity in Corporate Leadership Act” (Rep. Maloney)*

1. **Brief summary of issue.** Developments related to H.R. 4718, the “Gender Diversity in Corporate Leadership Act.” Introduced by Rep. Carolyn Maloney (D-NY), the bill would promote gender diversity on corporate boards.
2. **Specific changes/developments since last report.** The House Financial Services Committee has not yet acted on H.R. 4718, and Rep. Maloney is seeking additional Republican cosponsors for the bill. Rep. Lynn Jenkins (R-KS) is currently the lead Republican cosponsor.
3. **Implications for CalPERS.** Additional corporate disclosure beyond gender about board skills, experiences, race, and ethnic diversity can help CalPERS and other investors determine whether boards have the appropriate mix of qualities to manage risk, achieve long-term business objectives, and avoid the adverse consequences of “group think.”
4. **CalPERS/Federal Representative Actions.**
 - Sent letter to Rep. Maloney in June 2016, expressing support for H.R. 4718 and requesting that the scope of the bill be broadened; and
 - Identified members of the House Financial Services Committee with whom to potentially engage about H.R. 4718.

5. **Recommendations for Next Steps.**

- Continue engagement with Rep. Maloney’s office; and
- Decide whether to engage other members of the House Financial Services Committee to help advance CalPERS’ objective of broadening the scope of the bill.

V. *Securities and Capital Markets*

1. **Brief summary of issue.** Policy developments related primarily to the SEC, including investor protection issues such as investment adviser rules, stock buybacks, and disclosure effectiveness.
2. **Specific changes/developments since last report.**
 - **Investment Advisers.** The SEC adopted a final rule to amend a number of its Investment Advisers Act rules and the investment adviser registration and reporting form. The final rule requires investment advisers to provide additional information about their separately managed account business, including certain data concerning the use of derivatives and borrowings in such accounts. The final rule will also facilitate streamlined SEC registration and reporting for private fund adviser entities that operate a single advisory business. Additionally, the final rule requires advisers to maintain additional records regarding the calculation and distribution of account performance information. The rule will become effective 60 days after publication in the Federal Register, which has not yet occurred. Investment advisers will be required to be in compliance with the rule by October 1, 2017.
 - **Stock Buybacks.** Sen. Tammy Baldwin (D-WI) sent a letter to SEC Chair Mary Jo White in response to the SEC’s request for comment on the agency’s Regulation S-K concept release. Sen. Baldwin states that the “SEC must reform its disclosure regime to provide more transparency, information and details about stock buybacks on a more frequent basis.”
 - **Disclosure Effectiveness.** As part of the Disclosure Effectiveness Initiative, the SEC announced that it is requesting public comment on disclosure requirements in Subpart 400 of Regulation S-K, which includes disclosures related to management, certain securities holders, and corporate governance issues. After publication in the Federal Register, which has not yet occurred, the public will have 60 days to comment on the request. Comments are expected to assist the SEC in its study of Regulation S-K, as required by the Fixing America’s Surface Transportation (“FAST”) Act.
3. **Implications for CalPERS.**
 - The SEC’s efforts to require investment advisers to report additional information could provide the SEC and investors a better understanding of the risk profile of each adviser and the asset management industry as a whole.
 - Sen. Baldwin’s efforts related to stock buybacks could give policymakers, CalPERS and other investors the information needed to better understand the impact of stock repurchases on the U.S. economy.

- The SEC’s request for public comment will continue to provide investors and other market participants the opportunity to provide input on Regulation S-K, which could help to inform the SEC’s work to ensure that disclosures provide investors the information necessary to make informed investment and voting decisions.
4. **CalPERS/Federal Representative Actions.**
- Prepared for testimony of Anne Simpson at a hearing scheduled for September 9, 2016, entitled “Corporate Governance: Fostering a System that Promotes Capital Formation and Maximizes Shareholder Value” before the House Financial Services Capital Markets and Government Sponsored Enterprises Subcommittee. Ms. Simpson was invited to testify by Ranking Member Waters.
 - Prepared for Dan Bienvenue’s visit to DC in September 26-27, 2016, to continue strategic engagement with key Members of Congress and regulators about capital markets issues and other CalPERS priorities; and
 - Worked on CalPERS’ DC stakeholder engagement list, which includes the SEC, other regulators, Congressional Committees of jurisdiction, and key Members of the California delegation.
5. **Recommendations for Next Steps.** We will continue to:
- Monitor possible House Financial Services Committee markup of the Financial CHOICE Act, which contains H.R. 5424, H.R. 5311 and H.R. 5429;
 - Address any outstanding issues from the Subcommittee hearing;
 - Continue preparations for Mr. Bienvenue’s visit;
 - Work to further CalPERS’ objective of obtaining a seat on the SEC’s Investor Advisory Committee; and
 - Provide updates on other legislative and regulatory issues and recommend action by CalPERS, as warranted.

VI. *Derivatives Reform*

1. **Brief summary of issue.** Policy developments related primarily to the Commodity Futures Trading Commission (“CFTC”) regulation of derivatives, including the foreign persons exemption and the regulation of swaps and central counterparties (“CCPs”).
2. **Specific changes/developments since last report.**
 - **Foreign Persons Exemption.** The CFTC issued a proposed rule amending requirements for persons located outside the U.S. that would qualify for an exemption from registration as a futures commission merchant, introducing broker, commodity trading advisor, or commodity pool operator. The proposed rule would remove the clearing requirement for commodity interest transactions if the entity is acting on behalf of persons located outside the U.S. or an international financial institution. Public comments are due by September 6, 2016.

- **Swaps.**
 - *De Minimis Exception Report.* CFTC staff issued a final report about the swap dealer *de minimis* exception. The report provides the final results of a CFTC staff study about the possible impact of increasing or decreasing the threshold that requires swap dealers to register with the CFTC. The current \$8 billion threshold is set to decrease automatically to \$3 billion in 2017 unless the CFTC takes action. CFTC Chairman Timothy Massad has not indicated whether the CFTC will allow the lower threshold to take effect, though he signaled that the agency is “considering all options, including a rule making.”
 - *Massad Statement.* CFTC Chairman Massad issued a statement in which he described the CFTC’s past and future regulatory activity related to central clearing, oversight of swap dealers, trading and reporting. Regarding central clearing, he indicated that the CFTC is working with international regulators to address resiliency requirements and to engage in recovery planning. Chairman Massad also noted that the CFTC is participating in international resolution planning for central counterparties. In addition, he stated that the CFTC is focused on harmonizing its rules with those of international standard-setting bodies in a number of areas, including data reporting standards, and the oversight of swap dealers and swap execution facilities.
- **CCPs.** CFTC Chairman Massad issued a statement in response to the publication of documents that were released by the Committee on Payments and Market Infrastructures of the Bank for International Settlements and the International Organization of Securities Commissions, which consider risk management and recovery practices of CCPs, and CCP resolution planning. In his statement, Chairman Massad emphasized that these issues are “high priorities for the CFTC,” and indicated that the CFTC has been working with major clearinghouses on reviews of their resolution plans and rule changes.
- 3. **Implications for CalPERS.** The CFTC activity related to the foreign persons exemption, central clearing, oversight of swap dealers, trading and reporting, and CCPs could address potential risks in the derivatives markets. Moreover, the CFTC’s *de minimis* exception report could prompt the CFTC to act on the threshold thereby providing greater clarity to derivatives market participants.
- 4. **CalPERS/Federal Representative Actions.** Ongoing monitoring of relevant regulatory and legislative developments related to the derivatives markets.
- 5. **Recommendations for Next Steps.** We will provide updates and recommend action by CalPERS, as warranted, including commenting on relevant rulemakings and legislative proposals.

VII. *GSE Reform*

1. **Brief summary of issue.** Policy developments related to the secondary mortgage market.

2. **Specific changes/developments since last report.**
 - **GSE Stress Tests.** The Federal Housing Finance Agency (“FHFA”) released a report detailing the results of the annual stress tests of Fannie Mae and Freddie Mac (the “GSEs”). The report provides updated information about potential ranges of future financial results of the GSEs under a “severely adverse economic scenario.” According to the report, under such a scenario, the GSEs could need to draw between \$49.2 billion and \$125.8 billion from the Treasury Department.
 - **GSE LLPAs.** FHFA Director Melvin Watt responded to a letter from a group of housing industry and advocacy organizations that requested the FHFA to substantially lower or completely abolish loan-level price adjustments (“LLPAs”). Director Watt noted that the FHFA’s review of g-fees in 2014 and 2015 concluded that the g-fees and LLPAs charged by the GSEs struck the appropriate balance between safety and soundness and liquidity in the housing finance market.”
 - **New Refinance Option.** The FHFA announced a new streamlined refinance option for high loan-to-value (“LTV”) borrowers and extended the Home Affordable Refinance Program (“HARP”) through September 2017. The new option will offer liquidity for certain borrowers who are unable to refinance through the traditional program as the result of high LTV ratios. This new program differs from the current HARP requirements because there are no cut-off dates for eligibility and borrowers can refinance through the program more than once.
3. **Implications for CalPERS.** The GSE stress tests provide CalPERS and other investors in mortgage-backed securities (“MBS”) a forward-looking assessment of the financial stability of the GSEs, which could help investors to better understand issues that may cause instability in the financial markets. In addition, the FHFA’s efforts related to LLPAs and the new refinance option could facilitate the provision of liquidity in the housing finance system, which is essential to the sustainability of MBS investments.
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.