

# Fiduciary Training

January 19, 2017



**Board of Administration and Executive Offsite**  
JANUARY 2017

## Overview of Presentation

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- Fiduciary Duties 101
- Fiduciary nuances regarding particular Board decisions.
- California Public Records Act essentials
- Ins and outs of Bagley-Keene for Boards/Committees
- Considerations for Board members who speak publicly on CalPERS topics

## Fiduciary Duties 101 - The Two Prongs – Prudent Care & Loyalty: Overview of Fiduciary Duty of Care

- Prudent expert rule (Cal. Const., art. XVI, § 17(c))
- Duty to assure competency of retirement system assets (Cal. Const., art. XVI, § 17(e)).
- Duty to monitor and take corrective action when reasonably appropriate. (Rest. 3d Trusts, § 227, p. 14 (1992), comment d; *see generally Tibble v. Edison International*, 575 U.S. \_\_\_\_, 135 S. Ct. 1823, 191 L. Ed. 2d 795 (May 18, 2015))



# Fiduciary Duty of Care: Delegation

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- Prudent delegation queries: (1) whether to delegate; (2) how to delegate; (3) to whom a task is delegated; and (4) how to supervise.



## Fiduciary Duty of Care: Duty to Consult

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- Duty to consult with experts as necessary or appropriate and reasonable to the making of informed judgments

(Rest. 3d Trusts, supra, § 227, p. 15, comment d)



## Fiduciary Duty of Care: Duty to Consult

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- An implicit corollary of duty to consult:
  - if a fiduciary fails to follow the advice of its professional consultants, it must demonstrate an informed, reasonable, and prudent rationale for failing to do so.



## Fiduciary Duty of Care: Duty to Consult

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- Another implicit corollary:
  - expert advice from a reasonable and disinterested source should provide the basis for a Board’s decision to take an alternative course of action on a topic within that area of expertise (e.g., investment, actuarial, legal).



## Summary re Fiduciary Duty of Care/Prudence

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- Prudence requires that trustees and staff *ask questions* and *understand the rationale* for actions before proposing or taking them
- Prudence requires *providing and analyzing advice* and *recommendations* received from experts, not acting as a “rubber stamp,” but also, if the Board is not adopting the experts’ recommendation(s), having a reasonable basis for doing so that is *informed by the applicable expertise* implicated by the decision and that is consistent with fiduciary duties
- Prudence requires *following the Plan Document* (e.g., PERL, PEPR), *and other applicable law* (e.g., Bagley-Keene), as well as the Board regulations, policies, resolutions and other rules governing the retirement system



## Overview of Fiduciary Duty of *Loyalty*

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- Exclusive benefit rule (Cal. Const., art. XVI, § 17(a))
- Prompt delivery of benefits and related services (Cal. Const., art. XVI, § 17(a))

## Overview of Fiduciary Duty of *Loyalty* (cont.)

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- Primary duty rule (Cal. Const., art. XVI, § 17(b)) (duty to the overall best interest of members and beneficiaries)
- Duty of impartiality among members and beneficiaries
- Trustees are not permitted to administer the retirement system as an “agent” for the party that appointed, or subgroup of members that elected, that individual to the Board.

## Fiduciary Duty of Loyalty: Exclusive Benefit and Primary Duty Rules

### *What about CalPERS employers?*

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- The California Constitution clearly articulates the Board member's primary duty to members and beneficiaries:
  - "The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. *A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.*" (Art. 16, sec. 17(b), emphasis added).

## Fiduciary Duty of Loyalty: Exclusive Benefit and Primary Duty Rules

### *What about employer contributions?*

- The duty of “minimizing employer contributions” is not a *fiduciary* duty except to the extent that prudence requires paying only reasonable expenses, though it is a constitutional duty.
- Further, that constitutional duty is *secondary* to the primary duty to assure the competency of system assets to pay all promised benefits.

# Fiduciary Duty of Loyalty: Impartiality

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- Another aspect of the duty of loyalty is the duty of impartiality: *the duty to consider the overall best interests of all of the members and beneficiaries, without unduly sacrificing the interests of one group of beneficiaries to the interests of another.*



## **Fiduciary Duty of Loyalty:** **Conflicting Interests Among Members and Beneficiaries**

- Dissimilar interests among beneficiaries are built into most trusts.
- Trust law has evolved to grant trustees a fair measure of discretion to balance those competing beneficiary interests.
  - See Rest. 3d Trusts, §§ 50, 183 comment a, and 232; *Estate of Bissinger* (1963)212 Cal.App.2d 831, 833; and IIIA Fratcher, Scott on Trusts, § 232, p. 7 (4th ed. 1988) (“The trustee, however, ordinarily has considerable discretion in preserving the balance between beneficiaries”).

## Fiduciary Duty of Loyalty: Conflicting Interests Among Members and Beneficiaries



- Can be complex and crosscutting.
- Determinations of priorities among members and beneficiaries must serve the *overall best interest of members and beneficiaries of the retirement system*.
- Appropriate balance may not be obvious when the interests within the member and beneficiary groups are not the same.

## Fiduciary Duty of Loyalty:

### All Trustees Serve All Retirement System Members

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- Loyalties of Board Members
  - The U.S. Supreme Court noted that although the statute: “requires an equal balance between trustees appointed by the union and those appointed by the employer, *nothing in the language of [the provision] reveals any congressional intent that a trustee should or may administer a trust fund in the interest of the party that appointed him, or that an employer may direct or supervise the decisions of a trustee he has appointed.*”

[*NLRB v. AMAX Coal Co.*, 453 U.S. 322, 331 (1981) (emphasis added) (discussing fiduciary duties incorporated into pre-ERISA Labor-Management Relations Act).]



## Fiduciary Duty of Loyalty: *Loyalties of Board Members*

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- *NLRB v. AMAX* also noted that the  
“The management-appointed trustee ‘represents’ the employer only in the sense that he ensures that the union-appointed trustee does not abuse his trust with respect to the funds contributed by the employer. Nowhere in the debates over [the LMRA trust provision regarding board composition] did any Member of either House of Congress suggest that the employer ‘representative’ as a trustee of a benefit fund created under this statute could or should advance the interest of the employer in administering the fund.” 453 U.S. at p. 330, n.13.

## Fiduciary Duty of Loyalty: *Loyalties of Board Members (cont.)*

- California law applicable to public pension funds also does not permit trustees to administer the retirement system as an “agent” for the party that appointed, or subgroup of members that elected, that individual to the Board.
- On the contrary, the California Constitution (Prop. 162) seeks to prevent such political “meddling” or “interference” by others and mandates loyalty through primary duty to members and beneficiaries.

(See generally, *Hittle v. Santa Barbara CERA*, 39 Cal. 3d 374 (1985) (traditional fiduciary duties apply to public retirement system trustees); *Claypool v. Wilson*, 4 Cal.App.4th 646, 676-7 (1992) (Cal. Const., art. XVI, sec. 17 imports the existing law of trusts))

**Fiduciary Duty Requires the CalPERS Board to  
Comply With Other Applicable Laws As Well Such As. . .**

- California Public Records Act
- Bagley-Keene Open Meeting Act

# California Public Records Act (PRA) - Gov. Code secs. 11120-11132

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## Purpose of the CPRA

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- In enacting this chapter the Legislature, mindful of the right of individuals to privacy, finds and declares that access to information concerning the conduct of the people's business is a fundamental and necessary right of every person in this state.

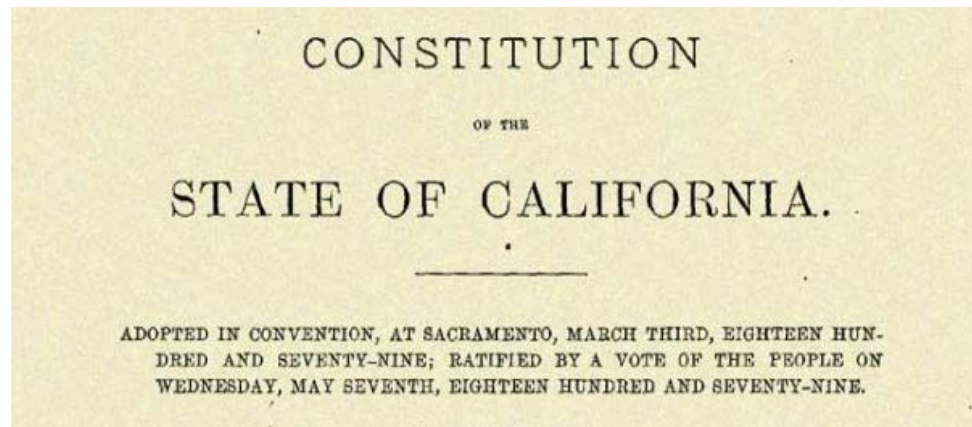
(Gov. Code § 6250.)



# California Constitution: Article 1, Section 3

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- **Section 1:**  
Inalienable rights including privacy
- **Section 3:**  
Right of access to information concerning the conduct of the people's business (open meetings and writings of public, individuals and agencies) (*added in 2004*)



## California Constitution: Article 1, Section 3

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- § 3(b)(2) - Laws broadly construed if they further access, narrowly construed if they restrict it.
- § 3(b)(3) - Right to privacy neither superseded nor modified.
- § 3(b)(4) - Constitution neither superseded nor modified.

## California Constitution: Article 1, Section 3

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- § 3(b)(5) - Constitutional and statutory exceptions to public access to public records or meetings not repealed or nullified.





# Requesting Public Records

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- All public records are open to inspection unless exempt from disclosure by express provisions of law.  
(Gov. Code § 6253.)



## Most Common Exemptions

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- Gov. Code § 6254, including among others:
  - Preliminary drafts, inter and intra agency memos not retained by the public agency in the ordinary course if public interest in withholding the records clearly outweighs the public interest in disclosure.
  - Records re pending litigation unless finally adjudicated or otherwise settled.
  - Personnel, medical or similar files the disclosure of which would constitute an unwarranted invasion of personal privacy
  - Records, the disclosure of which is exempted or prohibited pursuant to federal or state law, including, but not limited to, provisions of the Evidence Code relating to privilege

## Most Common Exemptions (cont.)

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- Gov. Code § § 6254.1-6254.30 contain numerous specific exceptions to and clarifications regarding, CPRA provisions.
- Most applicable to public retirement systems is section 6254.26, protecting 6 categories of such records from CPRA disclosure.

## Other Common CPRA Exemptions

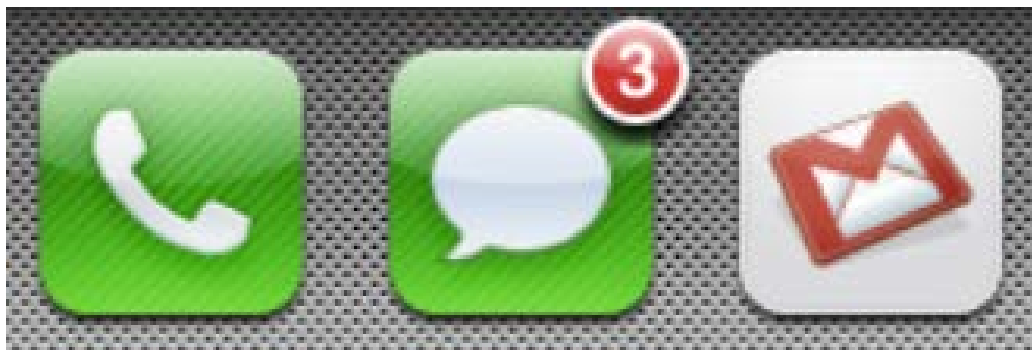
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- **Gov. Code § 6255 (balancing test)**
  - **Agency shall justify withholding any record by demonstrating that the record is exempt under express provisions of the CPRA or that on the facts of a particular case the public interest served by not disclosing the record clearly outweighs the public interest served by disclosure of the record.**
    - **“Deliberative Process” privilege?**
- **Listing of Additional Potential Statutory Exemptions in Government Code §§ 6275, et seq.**

## **PRA Case Pending Before the California Supreme Court: *Private Devices of Public Officials***

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- Are emails and text messages on private devices relating to public agency business “public records” under the Public Records Act?



**PRA Case Pending Before the California  
Supreme Court: *Private Devices of Public Officials* (cont.)**

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- ***City of San Jose v. Superior Court (Smith)***,  
Calif. Supreme Court Case #S218066
  - Oral argument occurred on Wednesday, December 7, 2016, decision expected during first quarter of 2017.
  - Rigorous questioning of both attorneys:
    - Petitioner/CPRA requestor was asked about privacy interests and how to limit scope of requested rule
    - Respondent/City Attorney was asked about deliberate efforts of public officials/employees to avoid CPRA by using private devices for business.

## **Bagley-Keene Open Meeting Act of 2004** **(Gov. Code §§11120-11132): Policy Declaration**

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“It is the public policy of this state that public agencies exist to aid in the conduct of the people’s business and the proceedings of public agencies be conducted openly so that the public may remained informed.”

“In enacting this article, the Legislature finds and declares that ... Actions of state agencies be taken openly and that their deliberations be conducted openly.”

## **Bagley-Keene Open Meeting Act of 2004 (Gov. Code §§11120-11132): Policy Declaration**

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“The people of this state do not yield their sovereignty to the agencies which serve them. The people, in delegating authority, do not give their public servants the right to decide what is good for the people to know and what is not good for them to know. The people insist on remaining informed so that they may retain control over the instruments they have created.”



## Bagley-Keene: Purpose

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- When a body sits down to develop its consensus, there needs to be a seat at the table reserved for the public
  - The Legislature has provided the public with the ability to monitor and, to some degree, participate in the decision-making process
  - Some efficiency is sacrificed for the benefits of greater public participation in government

## Bagley-Keene: Overview

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- All Board meetings must be open and public
  - The Board must provide its agenda to the public for all meetings, at least 10 days in advance unless an exception applies
  - The Board must conduct its meetings and make its decisions in public
  - The Board must allow all persons to attend and address topics within the Board's jurisdiction in its meetings through public comment

## What is a *Meeting*?

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- Meeting: A majority of members of the body in the same time and place, to hear, discuss or deliberate on any item within their jurisdiction, including:
  - Informal sessions or invitation-only conference attendance
  - Telephone conferences
  - E-mails
  - Due diligence trips by board or standing committee quorum



## Emails?

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- **California Attorney General concludes:**
  - A majority of board members of a local public agency may not e-mail each other to develop a collective concurrence as to action to be taken by the board without violating the Brown Act even if the e-mails are also sent to the secretary and chairperson of the agency, the e-mails are posted on the agency's Internet website, and a printed version of each e-mail is reported at the next public meeting of the board.

84 Ops.Cal.Atty.Gen 30 (2001)

## What is a Not a *Meeting*?

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- Not a “Meeting”:
  - Individual meetings
    - So long as not spoke & wheel serial communications

## What is a Not a *Meeting*?

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- Not a “Meeting” (cont.):
  - Conference and retreat attendance to discuss subject matter of general interest to persons or bodies in a given field, so long as they are open to the public
    - Unless conference or retreat is designed to focus on “the laws or issues of a particular body”
    - No private discussions with other members (quorum) about subjects that may be on an upcoming agenda.

## What is a Not a *Meeting*?

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- Not a “Meeting” (cont.):
  - Social or ceremonial attendance
    - No “shop talk” among quorum of Board/Committee

# Agenda Requirements and Practices

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- Agenda must contain a “brief description of the items of business to be transacted or discussed in either open or closed session.”
  - Description “generally need not exceed 20 words” (Gov. Code sec. 11125(b)).





## Agenda Requirements and Practices

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- Agendas for regular meetings must be distributed at least 10 days in advance of the scheduled meeting.



## Agenda Requirements and Practices

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- Special meetings may be called for one of nine reasons specified by statute when “compliance with the 10-day notice provisions . . . would impose a substantial hardship on the state body or when immediate action is required to protect the public interest.” (Gov. Code sec. 11125.4(a))

# Permitted Subject Matter for Special Meeting

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1. To consider “pending litigation,” as defined
2. To consider proposed legislation
3. To consider issuance of a legal opinion
4. To consider disciplinary action involving a state officer or employee
5. To consider the purchase, sale, exchange or lease of real property
6. To consider license examinations and applications
7. To consider an action on a loan or grant provided pursuant to a provision of the Health and Safety Code
8. To consider its response to a confidential and final draft audit report, as permitted by another statute
9. To provide for an interim executive officer of a state body upon the death, incapacity, or vacancy in the office of the executive officer.

(Gov. Code sec. 11125.4(a).)

## Agenda Requirements and Practices

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- **Not All Agenda Errors Prevent Agency Action**
  - Hypertechnical agenda violations of the Brown Act will not undo agency action where efforts at substantial compliance made and no showing of material harm

*North Pacifica LLC v. California Coastal Commission*  
(2008) 166 Cal.App.4th 1416

## Agenda Requirements and Practices (cont.)

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- What to do if topic not specifically agendized for “action”
  - Attempt to use agenda language that is sufficiently broad to retain board ability to act, if desired, but also specific enough so public and other board members know what to expect.

## Agenda Requirements and Practices (cont.)

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- **What if a particular item is not agendized?**
  - The item may be added to agenda only if:
    - Majority of board may determine that matter constitutes an “emergency,” in rare circumstances as defined, provide one-hour notice to the media, and is held in open session, or

## Agenda Requirements and Practices (cont.)

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- An item may be added to agenda if (cont.):
  - Two-thirds of board members present, or unanimous board if less than two-thirds are present, reasonably determine that “immediate action” is needed that came to attention of the “state body” after agenda posting, and

(cont. on next slide)

## Agenda Requirements and Practices (cont.)

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- An item may be added to agenda if (cont.):
  - Notice is provided at least 48 hours before the meeting to the members of the body and all national wire services, along with timely posting on the Internet.
  - A special exception exists for “pending litigation,” as defined, that arises after agenda posting where the postponement will prevent the state body from complying with legally imposed deadlines. (Gov. Code sec. 11126.3(d).)



## Non-Agendized Reports?

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- **Under the Open Meeting law applicable to local agencies (the “Brown Act”), a statute provides that members of the Board and staff may:**
  - “briefly respond to statements made or questions posed [in public comment]”
  - “on their own initiative or in response to questions posed by the public, . . . ask a question for clarification, make a brief announcement, or make a brief report on his or her own activities” and

## Non-Agendized Reports?

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- **Brown Act provision on Board member comments on non-agendized reports (cont.):**
  - Board members may “provide a reference to staff or other resources for factual information, request staff to report back to the body at a subsequent meeting on the matter, or take action to direct staff to place a matter of business on a future agenda.”  
(Gov. Code sec. 54954.2, subd. (a)(2))
- **Bagley-Keene appears to be silent on this topic.**

## Non-Agendized Reports?

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- Even under Brown Act, violations of this rule have been found where a topic of public interest was addressed in a general report by executive staff and report was deemed too long or substantive to fall into the “brief oral report” exception.
  - *Community Ventures Partners, Inc. v. County of Marin*, Marin County Superior Court (2016).
- However, a short discussion on a non-agenda item regarding placing the item on the next agenda does not violate the Brown Act.
  - *Cruz v. City of Culver City*, 2 Cal.App.5<sup>th</sup> 239 (2016).

## Meeting Requirements and Practices

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- Public Comment Or Testimony
    - Every agenda for a regular meeting must provide an opportunity for members of the public to directly address the legislative body on any item under the subject matter jurisdiction of the body.
      - Provision not applicable if the agenda item already considered by committee composed exclusively of members of the Board where public comment available
        - Unless item substantially changed after the committee heard it
- (Gov. Code sec. 11125.7, subdiv. (a))

## Meeting Requirements and Practices

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- Public Comment Or Testimony
  - Reasonable regulations are permissible to limit total time allocated for public comment on particular issue and for each individual speaker.



## Regulations re Public Comment

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- CalPERS' proposed regulation 552.1 is consistent with approach of many other public entities in California that limit public comment to three minutes per speaker
  - Also common: flexibility to the Board or Committee Chair to make viewpoint-neutral adjustments to that time limit as warranted under the circumstances presented.
  - If a member of the public uses a translator to speak (without simultaneous translation equipment), then the time provided in any such regulations shall be at least doubled “to ensure that non-English speakers receive the same opportunity to address the state body.” Gov. Code sec. 11125.7, subdiv. (c))

## Closed Sessions

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- May have a closed session only if *specifically* permitted by statute.
- Notice in regular agenda required, along with *recitation of closed session authority*.
- Even if a board may, as a matter of law, consider a matter in closed session, might there be policy reasons not to?

## Closed Sessions (cont.)

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- **Rules:**
  - Disclosure of closed session discussion is *prohibited* unless the majority of the Board votes to authorize disclosure or court orders it.





## Closed Sessions Topics

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- **Litigation Exception:**
  - Applies to “pending litigation” when, on advice of CalPERS’ legal counsel, discussion in open session concerning those matters “would prejudice the position of the state body in litigation”
    - The confidential legal memorandum required by Gov. Code sec. 11126(e)(2)(C)(ii) of Bagley-Keene is not included in the Brown Act.

## Closed Sessions Topics: Litigation

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- “Pending litigation,” is defined to include
  - Adjudicatory proceedings before a court, administrative body exercising adjudicatory authority, hearing officer or arbitrator, to which the state body is a party.
  - A point has been reached where, in the opinion of CalPERS on the advice of its legal counsel, based on existing facts and circumstances, there is a significant exposure to litigation.
  - CalPERS has decided or is deciding whether to initiate litigation.

(Gov. Code sec. 11126(e))

## **Closed Sessions Topics: Executive Personnel**

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- Specific provision for CalPERS and CalSTRS permitting closed session “when considering matters pertaining to the recruitment, appointment, employment, or removal of the chief executive officer or [chief investment officer]...”

(Gov. Code sec. 11126(g)(1))

## Closed Sessions Topics: Investment Decisions

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- Specific provision for CalPERS and CalSTRS permitting closed session “when considering investment decisions.”
  - This broad exception does not apply under the Brown Act, which permits closed session for investment discussions only as to the “purchase or sale of a particular specific investment,” and/or purchase, sale, exchange or lease of real estate,” with specified conditions.

(Gov. Code sec. 11126(g)(1))

## Closed Sessions Topics: Investment Decisions (cont.)

- Gov. Code sec. 11126(g)(1) further provides:
  - “For purposes of consideration of shareholder voting on corporate stocks held by the state body, closed sessions for the purposes of voting may be held only with respect to election of corporate directors, election of independent auditors, and other financial issues that could have a material effect on the net income of the corporation.” (Emphasis added)

## **Closed Sessions Topics: Long Term Care Program**

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- The CalPERS Board is specifically permitted to hold closed sessions “when considering matters relating to the development of rates and competitive strategy for plans offered pursuant to [the Public Employees’ Long-Term Care Act.] (Gov. Code sec. 11126, subd. (h).)

## **Closed Sessions Topics: Health Care Contract and Rate Strategy**

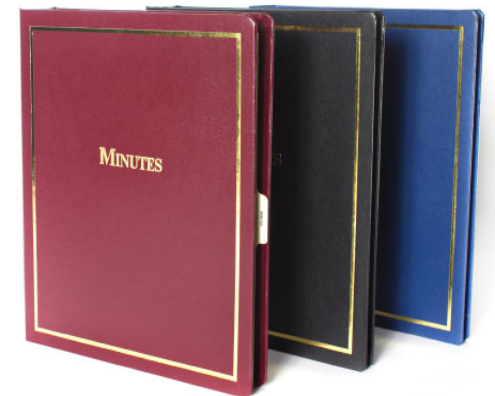
- CalPERS discusses Health Plan contract and rate strategy in closed session under the broad authority provided to state bodies and boards to hold closed session with their representatives to discharge their responsibilities under various statutes governing bargaining over “salaries, salary schedules or compensation in form of fringe benefits.” (Gov. Code sec. 11126(c)(17).)

## Closed Sessions Minute Book

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- **Closed Session minute books are required of state bodies such as CalPERS.**
  - Minute books are not public records, and they “shall be kept confidential.”
  - However, they also shall be available to members of the state body not legally excluded from the closed session, or “if violation of [Bagley-Keene] is alleged to have occurred at a closed session, to a court of jurisdiction.”
  - The minute book may, but need not, contain a recording of the closed session.

(Gov. Code sec. 11126.1)





## Reporting Out of Closed Session

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- After closed session, the Board is to reconvene into open-session prior to adjournment and “make any reports, provide any documentation, and make any other disclosures required by Section 1125.2 of action taken in the closed session.”
  - Section 1125.2 applies only to a decision to “appoint, employ, or dismiss a public employee arising out of any closed session of the state body.”
  - Section 1125.2 also requires such votes to be reported “publicly at a subsequent public meeting,” including “any rollcall vote thereon.”

(Gov. Code sec. 11126.3(f))

## Reporting Out of Closed Session

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- Other than reports under section 1125.2, public reports on closed session votes under Bagley-Keene do not appear to require reporting of roll-call votes.
- Contrast the Brown Act, which requires legislative bodies of local agencies to “publicly report any action taken in closed session and the vote or abstention on that action of every member present,” within the parameters set by statute. (Gov. Code sec. 54957.1)

## Further Considerations for Board Members Who Speak on CalPERS-Related Topics

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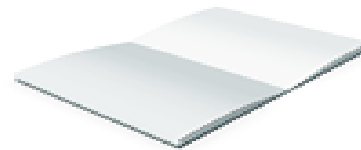
- CalPERS Board Policies:
  - Governance Policy



## Further Considerations for Board Members Who Speak on CalPERS-Related Topics

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- Governance Policy – Big Picture
  - “Individual Board members are fiduciaries and trustees. As such, Board members will at all times act in the best interest of CalPERS and its members and beneficiaries, consistent with the Board member’s fiduciary duty, and take positive steps to prohibit breaches of duty through negligence or intentional action.” (Sec.IV.A.)



Definition

**Fiduciary Duty**

## Further Considerations for Board Members Who Speaks on CalPERS-Related Topics

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- Governance Policy – Communications With Third Parties.
  - “Any such contacts and communications will be in the Board member’s capacity as an individual Board member with the understanding that the individual Board members do not represent CalPERS or the Board, and have no authority to bind CalPERS to any agreements, unless specifically authorized to do so by the Board.” (Sec. X.G, emphasis added.)



## Further Considerations for Board Members Who Speak on CalPERS-Related Topics

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- How about other types of communications not expressly addressed in the Governance Policy? Such as,
  - communications with the press
  - in speeches at meetings of outside organizations
- Issue: Are you expressing individual views, or those of CalPERS?
  - If your own, how clear is it that your statements are not those of CalPERS?
  - If speaking for CalPERS, was the communication authorized as required by CalPERS Policy?

## Full Circle

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- When CalPERS Board members speak – people listen.
- Consider carefully the method, tone and content of your speech.
- The speech reflects on CalPERS and may have negative consequences to CalPERS if not carefully and/or accurately expressed.
- Fiduciary duties of Board members should be the guiding principle of Board members' actions as to all activities in which Board members are conducting CalPERS business.

## Final Fiduciary Take-Aways

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- Recognize that although courts afford retirement boards broad discretion in decision-making, “exclusive authority” is not absolute discretion



## Final Fiduciary Take-Aways (cont.)

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- Board and Executives need to avoid “abuse of discretion” and financial conflicts of interest
  - Process important – make sure record reflects that process: clear and fair communications with members, written materials provided by expert consultants, comprehensive agenda backup, detailed legal memoranda, minutes reflecting deliberation
  - Education, inquiry, disclosure of reasons for action, reflecting due consideration to overall best interest of members and beneficiaries
  - Active independent actuarial and investment oversight, prudent discussion, considerations and exercise of judgment regarding same.
  - Legal consultation and compliance with applicable law



Questions?

# Thank You!

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