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Federal Investments Report for CalPERS Board
April 2017

I. Securities and Capital Markets

1. **Brief summary of issue.** Policy developments related to the Securities and Exchange Commission ("SEC") and the securities markets.
2. **Specific changes/developments since last report.**
   - **Nominations.** The Senate Banking Committee voted 15-8 to approve the nomination of Jay Clayton, an attorney in private law practice, to be the Chairman of the SEC. Democratic Sens. Jon Tester (D-MT), Mark Warner (D-VA), and Heidi Heitkamp (D-ND) joined all Committee Republicans in voting for Mr. Clayton's nomination, while all other Committee Democrats voted to oppose the nomination. The full Senate is scheduled to convene on Monday, May 1 at 3:00 p.m. to consider the nomination.
   - **Financial CHOICE Act.** House Financial Services Committee ("HFSC") Chairman Jeb Hensarling (R-TX) released an updated version of the Financial CHOICE Act (the "CHOICE Act 2.0"), a discussion draft that would reform the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). The discussion draft builds upon a previous version of the bill (H.R. 5983 or the "CHOICE Act 1.0"), which was introduced in the last term of Congress by Chairman Hensarling and reported favorably to the full House by the HFSC last year. The HFSC held hearings on the CHOICE Act 2.0 on April 26 and April 28. A markup is expected to be convened on May 2, 2017.
   - **Rulemakings.** The SEC adopted a final rule to increase the amount of capital that companies are allowed to raise through crowdfunding to adjust for inflation. The final rule will also adjust for inflation the threshold used to determine eligibility for certain benefits available to "emerging growth companies" under the Jumpstart Our Business Startups ("JOBS") Act. The SEC is required to adjust certain JOBS Act rules for inflation at least once every five years.
   - **Legislation.** The House passed H.R. 1219, the "Supporting America's Innovators Act of 2017," by a vote of 417-3. Introduced by Rep. Patrick McHenry (R-NC), H.R. 1219 would amend the Investment Company Act of 1940 to expand the investor limitation for qualifying venture capital funds under an exemption from the definition of an investment company. In addition, the House passed H.R. 1343, the "Encouraging Employee Ownership Act," by a vote of 331-87. Introduced by Rep. Randy Hultgren (R-IL), H.R. 1343 would direct the SEC to revise regulations to require issuers to furnish investors with additional specified disclosures regarding compensatory benefit plans if the aggregate sales price or amount of securities sold during any consecutive 12-month period exceeds $10 million, indexed for inflation every five years. The Senate Banking Committee previously approved by voice vote companion legislation to Rep. McHenry's bill (S. 444) and Rep. Hultgren's bill (S. 488). Although it is not yet

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clear when the full Senate will take up the legislation, the bills appear likely to garner sufficient bipartisan support for passage by the Senate.

- **EMSAC Meeting.** The SEC's Equity Market Structure Advisory Committee ("EMSAC") held its first meeting of 2017 to receive updates on the activities of its four Subcommittees. During the meeting, the Regulation NMS Subcommittee discussed and presented preliminary recommendations about SEC Rule 611 (the "Order Protection Rule"), which fosters intermarket price protection of orders by limiting the execution of trades on one venue at prices that are inferior to quotations displayed at another venue. Moreover, the Trading Venues Regulation Subcommittee discussed and presented preliminary recommendations on Self-Regulatory Organization rule-based limitations of liability and regulatory centralization. Meeting participants discussed whether there are better and more efficient ways to conduct cross-market surveillance in the era of automated trading.

3. **Implications for CalPERS.**
   - Advancement of Mr. Clayton's nomination could provide CalPERS and other securities market participants greater certainty about the SEC's regulatory outlook; and
   - Legislative efforts to reform Dodd-Frank and revise other securities market regulations could impact the ability of CalPERS to protect shareowner rights and to foster confidence in the capital markets.
4. **CalPERS/Federal Representative Actions.**
   - Conducted ongoing monitoring of Mr. Clayton's nomination; and
   - Consistent with CalPERS' Federal Investment Priorities for the 2017-18 Congressional session (the "Priorities"), we conducted ongoing monitoring of the financial reform bills discussed above and do not recommend action at this time.
5. **Recommendations for Next Steps.** We will continue to provide updates on other legislative and regulatory issues and recommend action by CalPERS, as warranted.

II. Derivatives Reform

1. **Brief summary of issue.** Policy developments related to the Commodity Futures Trading Commission ("CFTC") and the derivatives markets.
2. **Specific changes/developments since last report.**
   - **Nominations.** President Donald J. Trump is considering re-nominating Republican Brian Quintenz to be a CFTC Commissioner. Mr. Quintenz and Democrat Chris Brummer were nominated by former President Obama to be CFTC Commissioners during the last term of Congress and were re-nominated in January before the end of the Obama Administration. President Trump withdrew the nominations from Senate consideration in February 2017. Senate Democrats are now thought to favor the nomination of Democrat Russ Behnam, a staff member to Senate Agriculture Committee Ranking Member Debbie Stabenow (D-MI), to serve on the five-member CFTC.
   - **Giancarlo Remarks.** Acting CFTC Chairman J. Christopher Giancarlo delivered remarks at the U.S. Chamber of Commerce's 11th Annual Capital Markets

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Summit. During the agenda item entitled "Transforming the CFTC," Acting Chairman Giancarlo stated that the "American derivatives markets regulated by the CFTC have a role to play to renew economic growth" in the aftermath of the 2008 financial crisis, namely by: (1) reducing regulatory burdens; (2) fixing flawed swaps rules; (3) working more effectively with regulatory counterparts; and (4) normalizing the CFTC after Dodd-Frank. Notably, Acting Chairman Giancarlo indicated that he has requested a comprehensive review of the CFTC's budget and spending.

- **Bowen Remarks.** CFTC Commissioner Sharon Y. Bowen delivered a speech at the Eurofi High Level Seminar 2017, during which she expressed her opinion about the future of international financial market regulation and emphasized the importance of regulatory harmonization. Specifically, she said that international derivatives market regulators need "harmonization, and not fragmentation," in the exchange of market data. Commissioner Bowen stated that, "[w]ith global regulatory coordination on enforcement, we can better achieve our purpose as regulators - to incentivize the formation of efficient, transparent, well-collateralized markets that are safe for counterparties." In addition to stating that regulators "need to stay vigilant about ensuring that our clearinghouses are managing risk effectively," Commissioner Bowen discussed market fragmentation and a number of other specific issues related to global clearing that have been or should be addressed in the U.S. and Europe.

3. **Implications for CalPERS.**
   - The President's possible re-nomination of Mr. Quintenz and Acting Chairman Giancarlo's speech about the role of the CFTC could provide CalPERS and other derivatives market participants additional information about the CFTC's regulatory agenda.
4. **CalPERS/Federal Representative Actions.**
   - Conducted ongoing monitoring of the CFTC nominations process; and
   - Conducted ongoing monitoring of other 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.

III. GSE Reform

1. **Brief summary of issue.** Policy developments concerning Fannie Mae and Freddie Mac (the "GSEs") and housing finance reform.
2. **Specific changes/developments since last report.**
   - **GSE Reform.** Secretary of the Department of the Treasury Steve Mnuchin participated in a White House press briefing, during which he discussed legislative efforts to reform the GSEs. In particular, Secretary Mnuchin said that "housing reform is very important to this [A]dministration," though he added that "this is not something we're focused on in terms of legislation in the first half of

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this year." Nevertheless, Secretary Mnuchin stated that "we've been having significant discussions at Treasury with the [Federal Housing Finance Agency ("FHFA")], [and] with congressional leadership on this." In discussing a possible GSE reform legislative package, he emphasized the importance of promoting "necessary liquidity in the housing markets" while at the same time ensuring that "we don't put taxpayers at risk and leave [the GSEs] as they are."

- **GSE Scorecard.** The FHFA issued a Progress Report on the 2016 Scorecard for the GSEs, which provides a summary of significant activities undertaken by the GSEs in 2016 to advance the FHFA's strategic goals for the entities. The Progress Report includes an update about the GSEs' credit risk transfer programs and other efforts to increase the role of private capital in the secondary mortgage market. Additionally, the Progress Report addresses the implementation of Release 1 of the Common Securitization Platform, which is part of the objective of enabling the GSEs to issue a single, common security. The Progress Report also details efforts by the GSEs to enhance diversity and inclusion in furtherance of the FHFA's strategic goals.
- **Credit Risk Transfer.** The FHFA issued its Credit Risk Transfer Progress Report (the "Progress Report"), which outlines the status and volume of credit risk transfer transactions through the end of 2016. The Progress Report indicates that in 2016 the GSEs "transferred $18 billion of credit risk on $548 billion of mortgages with an unpaid principle balance… through capital markets, insurance, and pilot credit risk transfer transactions" thus reducing risk to taxpayers. In addition, the Progress Report states that the GSEs have transferred almost $49 billion in credit risk to private investors since 2013. According to Director Watt, the GSEs "have made credit risk transfer a regular part of their business and they continue to improve and expand the scope of their programs and explore different transaction structures."

3. **Implications for CalPERS.**
   - Reformation of the GSEs could impact market liquidity, mortgage interest rates and investment returns for CalPERS shareowners.
4. **CalPERS/Federal Representative Actions.**
   - Consistent with the Priorities, we conducted ongoing monitoring of the FHFA's announcement about the GSE Scorecard and the Progress Report and do not recommend action at this time; and
   - Conducted ongoing monitoring of other 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.