



Finance and Administration Committee
Agenda Item 4d

November 14, 2017

Item Name: 2016-17 Year-End Budget and Expenditure Report

Program: Financial Office

Item Type: Information Consent

Executive Summary

This report presents the CalPERS Year-End Budget and Expenditures for Fiscal Year (FY) 2016-17 and satisfies the 2016 Budget Act (Chapter 23, Statutes of 2016) reporting requirement to submit a final year-end report to the State Controller, the Department of Finance, the Joint Legislative Budget Committee, and fiscal committees of the Legislature; in addition, the report will be submitted to the Legislative Analyst's Office, the Government Operations Agency, and the Office of the Legislative Counsel.

(\$ in Millions)	FY 2016-17				FY 2015-16
	Budget	Actual Expenditures	(\$ Under) Over	Percent Expended	Actual Expenditures
Administrative Operating Costs	\$458.8	\$437.8	(\$21.0)	95.4%	\$421.5
Investment Operating Costs	89.5	69.5	(20.0)	77.6%	72.6
Investment External Management Fees	896.7	613.5	(283.2)	68.4%	794.5
Third Party Administrator Fees	272.8	286.4	13.6	105.0%	282.6
Subtotal: Operating Costs	\$1,717.8	\$1,407.2	(\$310.6)	81.9%	\$1,571.2
Enterprise Project Costs	37.7	34.1	(3.6)	90.4%	32.1
Headquarters Building Costs	31.3	26.2	(5.1)	83.7%	27.7
Total Budget	\$1,786.9	\$1,467.5	(\$319.4)	82.1%	\$1,631.0

Of the total FY 2016-17 CalPERS Budget of \$1.8 billion, actual expenditures were \$1.5 billion, a savings of \$319.4 million (17.9 percent). As reflected above, the Investment External Management Fees were \$283.2 million below budget primarily due to (a) Private Equity savings as a result of the 2016-17 budget being approved prior to identifying and separating other fees, (b) lower than anticipated Real Assets fees, and (c) Global Equity re-allocation of assets to traditional managers on a more favorable base fee.

Savings in the Administrative Operating Budget totaled \$21.0 million, primarily due to position vacancies, the continued reduction in temporary staffing and consulting services, less reliance on outside counsel services, and lower than anticipated software and training costs. Savings in the Investment Operating Costs Budget totaled \$20.0 million, mainly due to investment consultants, external legal, and master custodian costs. Details for each of the six budget categories are presented in the Analysis section below.

Strategic Plan

This agenda item supports the CalPERS 2012-2017 Strategic Plan, to cultivate a high-performing, risk intelligent and innovative organization by actively managing business risks with an enterprise-wide view.

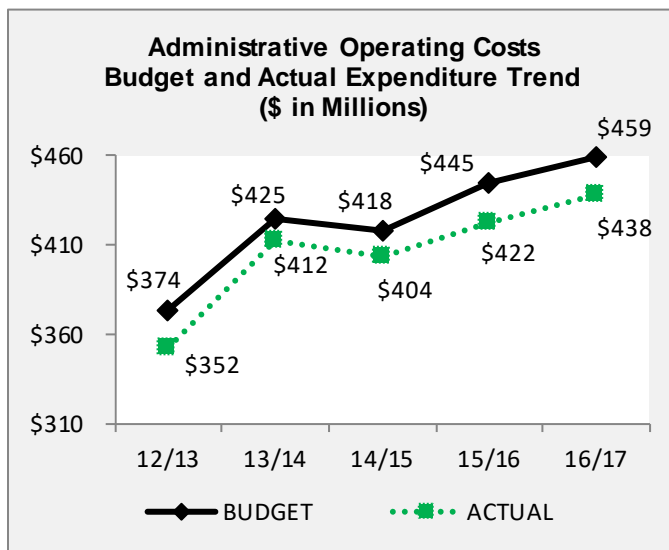
Background

The CalPERS Total Budget is comprised of six categories: Administrative Operating Costs, Investment Operating Costs, Investment External Management Fees, Third Party Administrator Fees, Enterprise Project Costs, and the Headquarters Building Costs. The CalPERS Total Budget is reviewed and approved by the CalPERS Board of Administration.

Analysis

Administrative Operating Costs

Of the total \$458.8 million Administrative Operating Costs Budget, CalPERS expended \$437.8 million, which was \$21.0 million or 4.6 percent under budget due mainly to staffing vacancies (\$9.9 million), reduced reliance on temporary staffing and consultants (\$4.9 million), and savings in travel, data processing, outside counsel services, and general operating expenses (\$5.7 million).

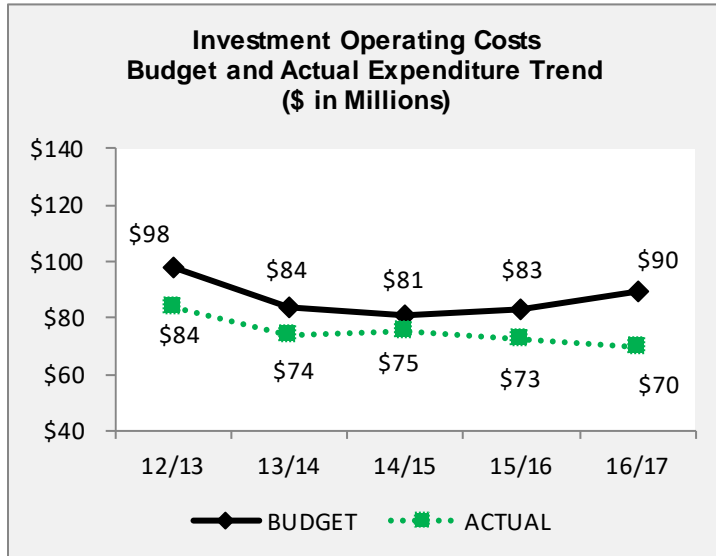


Compared to last year’s 2015-16 expenses of \$421.5 million, there was a net increase of \$16.3 million. Increases resulted mainly from (a) statewide management pay increases of \$1.9 million, (b) 39.0 new positions approved by the Board at a cost of \$5.9 million, (c) rank & file bonuses of \$5.8 million, (d) staff benefit increases of \$4.8 million, (e) the state leave buy-back program of \$1.2 million, and (f) data processing and consultant services of \$2.5 million. These increases were offset by \$5.6 million reductions in temporary staffing, statewide pro rata assessment, reduced reliance on outside counsel, and other operating expenses.



Investment Operating Costs

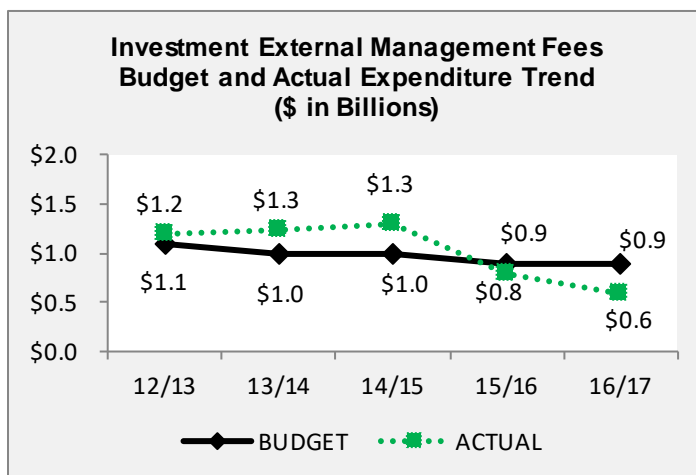
Of the total \$89.5 million Investment Operating Costs Budget, CalPERS expended \$69.5 million, which was \$20.0 million or 22.3 percent under budget. This is primarily due to the Investment Office’s continued efforts to reduce consulting costs, lower master custodian and external legal fees.



Compared to last year’s 2015-16 expenses of \$72.6 million, there was a decrease of \$3.1 million due to efforts to reduce consulting costs and lower than projected master custodian and external legal fees.

Investment External Management Fees

Of the total \$896.7 million Investment External Management Fees Budget, CalPERS expended \$613.5 million, which was \$283.2 million or 31.6 percent under budget. This is mainly due to a Private Equity savings as a result of the 2016-17 budget being approved prior to identifying and separating other types of fees, Real Assets performance fees accruals were paid at a lower amount than anticipated. The decrease is also due to the Global Equity re-allocation of assets to traditional managers on a more favorable base fee and the timing of performance fees paid to external managers along with the transition of some managers to a base fee only model.



Compared to last year’s 2015-16 expenses of \$794.5 million, there was a decrease of \$181.0 million mainly due to a more efficient method of capturing pure management fees for Private Equity (prior year expenses included other types of fees), the continued re-allocation of assets to traditional managers on a more favorable fee base for Global Equity, and the payment of Real Assets performance fees at a lower amount than accrued.



Investment External Management Fees				
(\$ in thousands)	FY 2016-17			FY 2015-16
	Budget	Actual Expenditures	(\$ Under) Over	Actual Expenditures
External Mgmt (Base)				
Global Equity	\$92,750	\$80,546	(\$12,204)	\$70,054
Fixed Income	8,797	10,781	1,984	10,206
Real Assets	165,378	187,068	21,690	178,583
Private Equity ¹	391,000	234,494	(156,506)	353,338
Absolute Return Strategy	4,000	675	(3,325)	6,229
Activist Funds	6,185	6,513	328	19,803
Multi Asset Class	9,358	8,194	(1,164)	8,115
Total External Mgmt (Base)	\$677,468	\$528,270	(\$149,198)	\$646,328
External Mgmt (Performance)				
Global Equity	\$72,258	\$23,043	(\$49,215)	\$50,250
Fixed Income	4,114	2,915	(1,200)	3,363
Real Assets ²	142,865	56,592	(86,273)	82,875
Absolute Return Strategy	-	2,689	2,689	(781)
Activist Funds	-	-	-	12,451
Multi Asset Class	-	-	-	-
Total External Mgmt (Performance)	\$219,237	\$85,239	(\$133,998)	\$148,158
Total External Mgmt. Fees	\$896,705	\$613,509	(\$283,196)	\$794,486

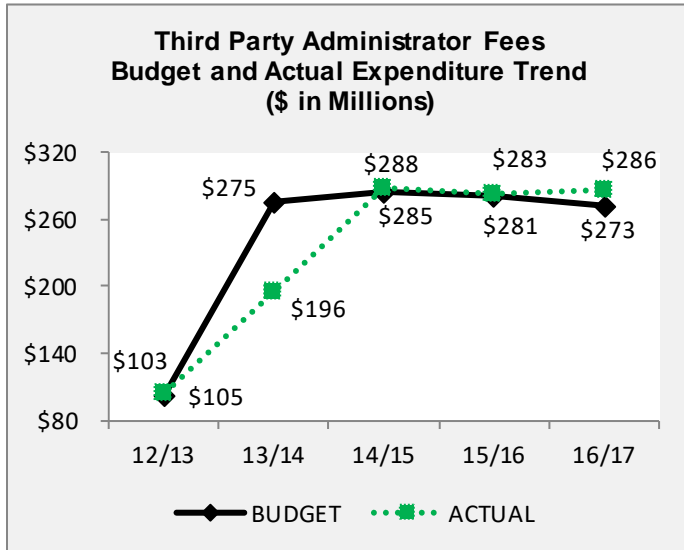
¹The reported expenditures of \$234.5 million includes gross management fees inclusive of waivers, and management fee offsets.
²FY 2016-17 fees are in alignment with CAFR's basis of accounting.

Third Party Administrator Fees

Of the total \$272.8 million Third Party Administrator Fees Budget, CalPERS expended \$286.4 million, which was \$13.6 million or 5.0 percent over budget. The Flex and Self-Funded Health Program costs were 5.5 percent higher than projected due to increased enrollment in plans with higher administrative fees, as well as administrative costs related to the close-out of the Blue Shield Net Value plan. Long Term Care Program costs were 3.0 percent higher due to higher than anticipated membership. These expenses were offset by \$602,000 or 15.4 percent decrease in the cost of the Supplemental Income Plan as these fees are mainly driven by market fluctuations and asset balances.

Third Party Administrator Fees (\$ in millions)	FY 2016-17				FY 2015-16
	Budget	Actual Expenditures	(\$ Under) Over	Percent Expended	Actual Expenditures
Long Term Care Program	\$20.2	\$20.8	\$0.6	103.0%	\$19.9
Flex and Self-Funded Health Program	248.7	262.3	13.6	105.5%	259.0
Supplemental Income Plan	3.9	3.3	(0.6)	84.6%	3.7
TOTAL	\$272.8	\$286.4	\$13.6	105.0%	\$282.6

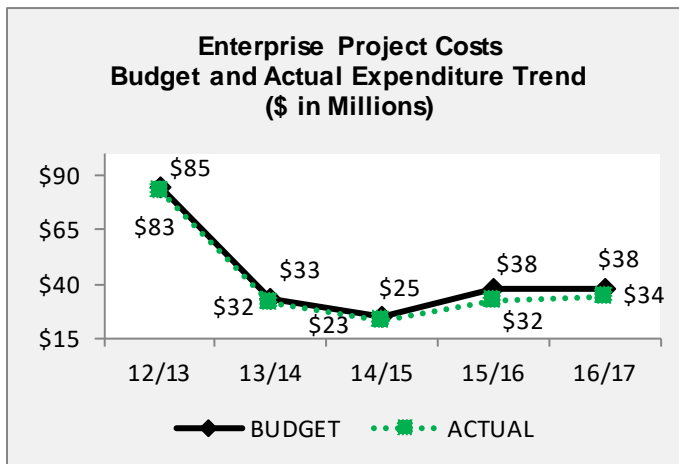




Compared to last year's 2015-16 actual expenditures of \$282.6 million, there was an increase of \$3.8 million mainly driven by enrollment changes in the Health Plans and administrative costs related to the close out of the Blue Shield Net Value plan.

Enterprise Project Costs

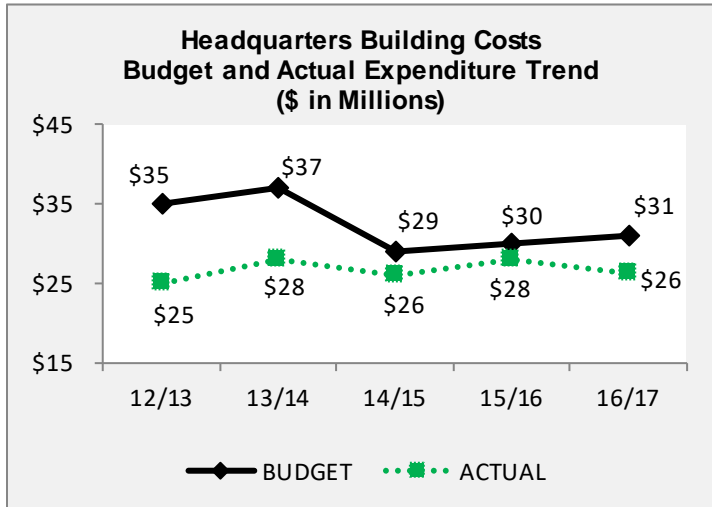
Of the total \$37.7 million Enterprise Project Costs Budget, CalPERS expended \$34.1 million, which was \$3.6 million or 9.6 percent under budget, due mainly to savings in the Security Roadmap and the Infrastructure Modernization projects as a result of lower costs negotiated for hardware and software purchases and lower consultant services costs.



Compared to last year's 2015-16 expenses of \$32.1 million, there was a net increase of \$2.0 million. The costs of projects completed in FY 2015-16 (\$1.9 million) offset the costs of the new projects approved in FY 2016-17 (\$3.9 million).

Headquarters Building Costs

Of the total \$31.3 million Headquarters Building Costs Budget, CalPERS expended \$26.2 million, which was \$5.1 million or 16.3 percent under budget due to lower costs in owner improvements for maintenance, supplies, wire plant/data, and electrical distribution upgrade. Building improvements were also lower due to efforts to reduce costs by delaying purchases and projects related to supplies and carpet stock, and drought tolerant plant replacement. Similarly, furniture needs for the master space plan and insurance costs were lower than anticipated.



Compared to last year's 2015-16 expenses of \$27.7 million, there was a net decrease of \$1.5 million mainly due to the postponement of landscape renovations, carpet stock purchases, personnel savings (\$1.2 million); lower than anticipated workstation conversions and furniture needs (\$1.4 million). The decrease was offset mainly by increases in operating expenses related to janitorial, parking management, other management fees increases, along with repairs to the fire/life safety system (\$0.9 million).

Budget and Fiscal Impacts

There are no costs associated with this item.

Benefits and Risks

Failure to submit the year-end report to respective legislative offices could put CalPERS at risk of noncompliance with the control language in the 2016 Budget Act.

Attachment

Attachment 1 – Transmittal Letter to the Joint Legislative Budget Committee

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