MEETING

STATE OF CALIFORNIA

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

BOARD OF ADMINISTRATION

INVESTMENT COMMITTEE

OPEN SESSION

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JAMES F. PETERS, CSR
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A P P E A R A N C E S

COMMITTEE MEMBERS:

Mr. Henry Jones, Chairperson

Mr. Bill Slaton, Vice Chairperson

Mr. Michael Bilbrey

Mr. John Chiang, represented by Mr. Matthew Saha

Mr. Richard Costigan

Mr. Rob Feckner

Mr. Richard Gillihan

Ms. Dana Hollinger

Mr. J.J. Jelincic

Mr. Ron Lind

Ms. Priya Mathur

Mr. Theresa Taylor

Ms. Betty Yee

STAFF:

Ms. Marcie Frost, Chief Executive Officer

Mr. Ted Eliopoulos, Chief Investment Officer

Mr. Matt Jacobs, General Counsel

Mr. Eric Baggesen, Managing Investment Director

Ms. Natalie Bickford, Committee Secretary

Mr. Dan Bienvenue, Managing Investment Director

Mr. Diego Carrillo, Investment Manager

Ms. Sarah Corr, Interim Managing Investment Director

A P P E A R A N C E S   C O N T I N U E D

STAFF:

Ms. Kit Crocker, Investment Director

Ms. Carrie Douglas-Fong, Associate Investment Manager

Mr. Matt Flynn, Chief, Operations, Performance & Technology Division

Mr. Paul Mouchakkaa, Managing Investment Director

Ms. Dianne Sandoval, Investment Manager

Ms. Anne Simpson, Investment Director

Mr. Clint Stevenson, Investment Director

Mr. Wylie Tollette, Chief Operating Investment Officer

ALSO PRESENT:

Mr. Allan Emkin, Pension Consulting Alliance

Mr. Steve Foresti, Wilshire Consulting

Mr. Dillon Gibbons, California Special Districts Association

Mr. Dane Hutchings, League of California Cities

Dr. Ruben Ingram, School Employers Association of California

Mr. Daniel Ingram, Wilshire Consulting

Ms. Dorothy Johnson, California State Association of Counties

Mr. Andrew Junkin, Wilshire Consulting

Mr. Derick Lennox, Small School Districts Association

Mr. Michael Ring, Service Employees International Union

I N D E X

I N D E X   C O N T I N U E D

P R O C E E D I N G S

CHAIRPERSON JONES: We'd like to convene the Investment Committee meeting please.

The first order of business is roll call please.

COMMITTEE SECRETARY BICKFORD: Henry Jones?

CHAIRPERSON JONES: Here.

COMMITTEE SECRETARY BICKFORD: Bill Slaton?

VICE CHAIRPERSON SLATON: Here.

COMMITTEE SECRETARY BICKFORD: Michael Bilbrey?

COMMITTEE MEMBER BILBREY: Good morning.

COMMITTEE SECRETARY BICKFORD: Good morning.

John Chiang represented by Frank Moore?

ACTING COMMITTEE MEMBER MOORE: Here.

COMMITTEE SECRETARY BICKFORD: Richard Costigan?

COMMITTEE MEMBER COSTIGAN: Here.

COMMITTEE SECRETARY BICKFORD: Rob Feckner?

COMMITTEE MEMBER FECKNER: Good morning.

COMMITTEE SECRETARY BICKFORD: Good morning.

Richard Gillihan?

COMMITTEE MEMBER GILLIHAN: Here.

COMMITTEE SECRETARY BICKFORD: Dana Hollinger?

COMMITTEE MEMBER HOLLINGER: Here.

COMMITTEE SECRETARY BICKFORD: J.J. Jelincic?

COMMITTEE MEMBER JELINCIC: Still here.

COMMITTEE SECRETARY BICKFORD: Ron Lind?

COMMITTEE MEMBER LIND: Here.

COMMITTEE SECRETARY BICKFORD: Priya Mathur?

COMMITTEE MEMBER MATHUR: Good morning.

COMMITTEE SECRETARY BICKFORD: Good morning. Theresa Taylor?

COMMITTEE MEMBER TAYLOR: Here.

COMMITTEE SECRETARY BICKFORD: And Betty Yee?

COMMITTEE MEMBER YEE: Here.

CHAIRPERSON JONES: Okay. Thank you.

The next item, I would like to take a moment of personal privilege to recognize two of our Board members. Our colleagues, Michael Bilbrey and J.J. Jelincic, are leaving us today, and this will be their last official Investment Committee meeting.

J.J. Jelincic has been on the Board for eight years, and he reminded me that he also is 32 years of service with CalPERS.

And also Michael has been on the Board for six years.

Both of you will be officially recognized at the Board meeting on Wednesday.

We know how much reading, homework, personal time, and dialogue are necessary for you to effectively make contributions to the business and functions of the Investment Committee.

I want to thank you for your service to the Investment Committee, this Board, to the State of California and its taxpayers, and all CalPERS members, retirees, employers, and staff. We sincerely wish you very success in all future endeavors.

So we'll look forward to Wednesday's meeting to officially recognize you both.

I would also like to take additional personal privilege to recognize our Chief Operating Investment Officer Wylie Tollette. Wylie recently announced that he'll be leaving CalPERS to return to Franklin Templeton.

Wylie joined CalPERS in 2014 and immediately proved to be an invaluable member of the CalPERS team. As COIO, Wylie has led the investment performance and risk analytics, investment policy, manager engagement, compliance, business planning, and operations areas of the Investment Office.

The impact that Wylie has had on CalPERS will be felt for years to come through programs like the to 2020 Strategic Plan, which guides the Investment Office's efforts to strategically reduce costs, risk, and complexity of the fund while also increasing transparency.

He's bought tremendous experience, knowledge, skill, and professionalism to the organization and he'll be difficult to replace.

We count ourselves as fortunate to have had been able to benefit from this talent for the last three years.

Wylie, we genuinely wish you the best of luck in your new role. We're going to miss you. As a reminder, however, we're always happy to hear your advice and opinions on CalPERS's operations, but moving forward, it will be restricted to three minutes during public comment.

(Laughter.)

CHAIRPERSON JONES: So let's congratulate Wylie on his...

(Applause.)

CHAIRPERSON JONES: Okay. Thank you.

And so now we will go to the consent items for action.

Do we have a motion?

COMMITTEE MEMBER TAYLOR: I'll make the motion.

CHAIRPERSON JONES: Moved by Ms. Taylor.

COMMITTEE MEMBER MATHUR: Second.

CHAIRPERSON JONES: Second by Ms. Mathur.

All those in favor say aye.

(Ayes.)

CHAIRPERSON JONES: Okay. Just a minute. We have a -- Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Yeah, I'm going to vote for the minutes, but I just want to draw attention to

Item 7, Summary of Committee Direction, because some of those directions, if we did get it, I haven't seen it yet.

CHAIRPERSON JONES: Okay. Thank you.

Okay. Mrs. -- oh, okay.

Yeah. Okay.

Then the -- so that item, all those in favor? I think I heard all the ayes.

And so opposed?

Hearing none.

The item passes.

Item 4: Information Consent Items.

Mrs. Yee.

COMMITTEE MEMBER YEE: Thank you, Ms. Chairman.

There are two items I'd like to pull off of consent for discussion: Item 4f, the Report on Alternative Investments as it relates to AB 2833; and also Item 4g, the Report to the Legislature on Divestment from -- Divest from the Iran Act and the Sudan Act Compliance.

CHAIRPERSON JONES: Okay. Thank you. We'll pull those items and hear your questions at the end of the regular agenda.

COMMITTEE MEMBER YEE: Great. Thank you.

CHAIRPERSON JONES: Okay. So that was for information.

So seeing no further requests to pull anything off, we'll go to item 5a, Asset Allocation.

Mr. Eliopoulos.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Mr. Chair, thank you very much. We're just coordinating the collection of presenters today.

Let me just briefly just introduce to the Committee while we're gathering here our Interim Chief Operating Investment Officer Matt Flynn. He sits to my right. During this interim period you'll be seeing Matt next to me in our presentations. He's just a few months shy of 15 years of service at CalPERS, and currently oversees the Investment Services Division, reporting to Wylie in his unit.

So I thank Matt for stepping up to this interim role and look forward for the Committee to see and hear more from him over the coming months.

So thank you, Matt.

Before I turn it over to Eric, I think -- for a few comments to set up this agenda item.

The asset allocation is one of the most important decisions that this Committee makes, as you're well aware. And I think the two-year process that we have used has benefited the system greatly. The amount of information, amount of discussion this Board has had together with its

Investment staff, Finance staff, really the whole professional staff of CalPERS as well as outside consultants and outside stakeholders, has brought us to this milestone of considering candidate portfolios and selecting a candidate portfolio to recommend and then for ultimate adoption together with the discount rate as part of the ALM process this week.

So with that introduction, I will turn it over to Eric.

And, Eric, it's all yours.

MANAGING INVESTMENT DIRECTOR BAGGESEN: Good morning.

Thanks Ted.

Eric Baggesen, Managing Investment Director.

As Ted mentioned, basically this action agenda item culminates two years of work. Over that two years we've done a review of the investment beliefs, portfolio priorities, capital market assumptions, so the on and on and on, a whole array of different topics, and attempted to provide an opportunity for virtually every stakeholder that has a point of view and an interest in what CalPERS does to express that point of view.

This agenda item is going to be presented very briefly by Dianne Sandoval. I'd like Diane to present this mainly as a form of recognition of the work that she and Alison Li have lead basically and much of the information that's been brought to you over the last two-year period.

So Diane will do a brief overview of some of the germane an attributes and the staff recommendation.

We also have opinion letters from your three investment consultants: Wilshire Associates, PCA, and Meketa. And we have representatives from each of those firms here if you care to ask them about their opinion letters.

And I think without any further noise from me, I would just turn it over to Diane.

INVESTMENT MANAGER SANDOVAL: Thank you, Eric.

It's good to know which me button to press.

So good morning. My name is Dianne Sandoval, and I'm an investment manager in the trust level portfolio management team. And it really is an honor to be with you this morning to walk you through our recommended policy portfolio -- strategic policy portfolio.

I just wanted to say that I am especially proud to be here this morning knowing that yesterday some of our finest members laid rest to their fallen brother, firefighter Cory Iverson, and yet continue to work under extremely challenging conditions going on three weeks now to fight the Thomas fire in Southern California. I imagine their exhaustion.

And so this morning we honor their service, and we are proud to serve those that serve California.

As Ted and Eric mentioned, today's decision will play a really important role in defining our path towards keeping our promise to help our public service workers achieve a basic level of financial security in their retirement. Your vote for the Strategic Asset Allocation will define the market exposures that staff will manage and will be the dominant determinant of portfolio volatility and risk over the next two years, at which time we will review this decision again.

Turning to the material before you, on Table 1 of page 3 we illustrate the alternative Strategic Asset Allocation combinations that we presented at the ALM workshop. Candidate portfolios A, B, C, and D represent blended - meaning short- and long-term combined - expected return levels that are 25 basis points apart, and were designed to offer a real choice, ranging from 6 and a half percent to 7 and a quarter percent. All four candidate portfolios are considered to be prudent and implementable.

The placement of these alternatives along the model-deficient frontier demonstrate an increase in expected volatility of around four basis points for each one-basis-point increase to expected return.

And I think it's important to note the differences between the short-term expected returns of 1 to 10 years and a long-term expected returns of 11 through 60 years. As Eric pointed out in the November workshop, this gap is the highest level it has been and represents higher estimation error.

I'd also want to note that the difference in the cash yield that we are showing amongst these portfolios from 3.1 percent to 2.7 percent is really not material given the $340 billion portfolio that we manage.

With that, let me summarize the four main reasons that we recommend candidate Portfolio C. First, the overwhelming feedback from stakeholders supported candidate Portfolio C during the public comment. Two hours of testimony made it clear what kind of pressure would be faced by many of our partners - the 3,000 public agencies, schools, special districts, and State of California - if we were to recommend a lower risk and return candidate portfolio at this time.

Second, this portfolio allows us to continue our current path towards a 7 percent discount rate target, which is consistent with your really important decision in December of 2016 to bring more cash into the fund as we move toward our goal of fully funding the pension benefits that have been promised.

Third, candidate Portfolio C is most similar to our current allocation and, therefore, simplifies the implementation and reduces transaction costs.

Fourth, candidate Portfolio C does not further increase our equity risk concentration. Since we presented in November, current valuation levels have not abated, and suggest that this may not be the most opportune time to take on additional equity risk, particularly in light of our 68 percent funded status.

In summary, we believe that candidate Portfolio C represents a reasonable approach to meeting the Board's objectives of improving the sustainability of the fund while partnering with our key stakeholders to understand and manage the pension costs.

With that, let me pause and turn to you with any questions.

CHAIRPERSON JONES: None at this time.

Okay. So that completes staff's presentation.

I will turn to the consultants to ask whether or not any of you have any additional comments. We do have your opinion letters in our folders.

So any other comments?

Seeing none.

Okay. This is an action item.

Ms. Mathur.

COMMITTEE MEMBER MATHUR: Yeah. I think Ms. Sandoval has laid out really four compelling reasons to adopt the staff recommendation, which is option C; and so that is what I will move.

CHAIRPERSON JONES: Okay. It's been moved by Mrs. Mathur.

VICE CHAIRPERSON SLATON: Second.

CHAIRPERSON JONES: Second by Mr. Slaton.

Okay. Thank you.

Mrs. Yee.

COMMITTEE MEMBER YEE: Just one question. And I -- if it was in the materials, I may have missed it. But can you give us a sense of the time frame for implementing the shifts to the new allocations.

MANAGING INVESTMENT DIRECTOR BAGGESEN: Why don't I take that one. Eric Baggesen, CalPERS staff.

Ms. Yee, basically we'll be bringing back an implementation item to you where we'll be discussing that in detail. So you'll probably be seeing that item in the February-March time frame.

CHAIRPERSON JONES: Okay. Before -- Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: We forget that we are long-term investors. Over the time that I've been on our Board, our focus has become shorter and shorter and shorter. We are worried about avoiding an event that has a 4 percent probability. And if we are really long-term investors, then we ought to be willing to ride the ups and downs and get paid for it.

I saw the letters, I've read the letters. And it's not clear to me that the League of Cities or the supervisors and the counties recognize that they are not currently funding at 7 percent.

And so I think we need to take more risk. I've argued that in the past. I will continue to argue it. We are long-term investors. Our biggest advantage is that we can be long-term investors. And we're not going to miss payments over the next four or five, six years, so we can avoid -- or we can accept the ups and downs.

Therefore, I'm going to move to amend and that we adopt Portfolio D, take advantage of the long-term horizon we have, help fund the system, help control employer costs. And I just think that in the long run - not the short run but in the long run - we are much better off with that portfolio.

CHAIRPERSON JONES: Okay. There's a motion by Mr. Jelincic to amend the original motion. Is there a second on that?

Seeing none, the motion fails.

COMMITTEE MEMBER JELINCIC: That's appropriate.

CHAIRPERSON JONES: Okay.

Mr. Lind.

COMMITTEE MEMBER LIND: I just had a quick question that occurred to me. Although the -- and I support the motion. All the great work that we've done in developing this candidate Portfolio C was done before we are seeing what the Republican tax plan is going to look like. And I'll reserve my political comments on that. But there -- certainly, you know, adding to the deficit and all the other things that go along with that could change things a lot. Any considerations, second thoughts? Or do we believe that two years from now in our review we could react to whatever that legislation creates?

CHIEF INVESTMENT OFFICER ELIOPOULOS: I certainly think we will have a better view of the implications of the tax bill in two years; and that would probably be more prudent -- or more reasonable, as you're suggesting, to take it into account at that time.

The tax plan has a -- you know, an array of complicated provisions. You're certainly seeing the equity markets in the U.S. reward the corporate tax cut component of the bill, at least here in the short term.

Looking out to the longer term, investors need to consider what the longer-term effects of this could be. It's a tax cut at a time when we're very late in the economic cycle in this recovery. The added impacts to various states within the United States, in other words it's affecting disproportionately some of the more productive states within the economy, that will play out over time and need to be considered.

But thinking through a complicated tax proposal like this, one, we'll know more in two years; but, two, it in many ways reinforces a desire to find a strategic portfolio that is balanced. And from that perspective, Portfolio C represents a balancing of both equity and interest rate risk. So the setting for the coming years is challenging and the effect of this tax bill will play out over many years.

COMMITTEE MEMBER LIND: Thank you.

CHAIRPERSON JONES: Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Thank you, Mr. Chair.

I just had a quick question - I think it's a follow-up on what Ms. Yee had asked - on when we would be implementing. We already started the implementation when we originally adopted the 7 percent; isn't that correct? I just wanted to und -- was confused.

MANAGING INVESTMENT DIRECTOR BAGGESEN: Yeah, I think the -- the implementa -- well, as I say, that we'll be bringing an agenda item to you to bring a clear plan on that. So there's work that will be going on in the staff over the next month or so to basically sort of solidify the plans that we have. Some of those plans will need to be talked about in closed session in contrast to --

COMMITTEE MEMBER TAYLOR: Right.

MANAGING INVESTMENT DIRECTOR BAGGESEN: -- open session. So, again, I would just encourage you to basically wait for that agenda item, and then you'll know more about the implementation path.

COMMITTEE MEMBER TAYLOR: Okay. Okay. That's where I got a little confused, because I thought we already did this.

And then my -- I just have a little bit of a comment on what Mr. Eliopoulos was saying. I think that, yes, we're going to see some long-term issues dealing -- that comes up with this legislation and I think we need to be mindful of the long-term risk of the transfer of wealth that is going on with this tax cut. That will impact our fund in the long-term. So I think we need to be keeping an eye on that, because that definitely has an impact on our fund. So I just wanted to make a commentary on that.

Thank you.

CHAIRPERSON JONES: Mr. Slaton.

VICE CHAIRPERSON SLATON: Thank you, Mr. Chair.

You know, I would -- I would have agreed with Mr. Jelincic except for a couple of facts. And I agree with Mr. Eliopoulos that we're very long in the tooth in this particular expansion.

At the same time the two concerns that I have that lead me to support Portfolio C is we're sitting with a by $20 trillion national debt as this tax bill comes for final vote. We're at 106 percent of GDP. Last time we were this high it was 118 percent in 1946. Never been this high.

But we're 68 percent funded. If we were 80 percent funded or 85 percent funded, then I think that our ability to take -- to take that volatility into account by having a higher rate would potentially be acceptable. But that's not the reality of where we are.

So I think it's very prudent, and especially in light of the pressure that we're bringing on these 3,000 plans. Because at the end of the day, all of our jurisdictions are providing community service. And when they face a situation where they start having to cut back even more from where they are today, I think it's really an unacceptable situation in California.

So I think the prudent thing right now for us to do is to approve the motion for Portfolio C.

Thank you.

CHAIRPERSON JONES: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Well, it's called decision making and I'm certainty for a reason. And I would point out that a year ago, a little over a year ago, for secret reasons we reduced the risk in the portfolio. We left close to $2 billion on the table by making that decision. We need to be long-term investors. And I agree with Bill that we are putting pressure on the employers. And, quite frankly, D would relieve some of that pressure. C continues the increase in the pressure, because we need to recognize people are not currently funding at 7. It's going to go down. Or the contributions are -- discount rate is going down for funding purposes, the contributions are going to continue to go up. I think D is a reasonable portfolio and offers some relief. And, you know, a year -- you know, year ago we made a similar decision and it cost our employers in the system big time.

So I -- you know, markets and economies don't die of old age. And there is not really a lot of pressures being exerted that would hint that a recession is coming.

We have virtually, if not every central bank in the world pushing to reinflate the economies and get it going some more.

I just do not think that it makes sense to take the lower risk and accept the lower returns. But as I started -- you know, it's decision making and uncertainty, and just as we were, in hindsight, wrong a year ago, a year from now we will either have been right or wrong. But I think D is the better choice.

Thank you.

CHAIRPERSON JONES: Mr. Costigan.

COMMITTEE MEMBER COSTIGAN: Well, I wasn't going to say anything on this, but just a couple points. In between Mr. Jelincic and Mr. Slaton.

I guess the concern I have, absent aside -- and I will say that concerns Mr. Lind raised on the tax policy, I agree with. As someone who is going to see a significant tax increase next year, I'm somewhat disappointed with my congressional friends in the Republican caucus. But when I separate it, what I'm concerned about is the S&P is up 20.33 percent year to date. The Dow's up what, 24 percent year to date.

All indications are, absent California, New York, and New Jersey -- and I get, Mr. Eliopoulos, the point you were making about the disproportionate impact, particularly the limitations of the $10,000 on SALT and property tax and how that may have a chilling effect in California.

I'm not where Mr. Jelincic is about adopting Portfolio D. But I am concerned we're going -- we're leaving on the table upside growth for the next year and a half. I mean, do you all disagree that the changes in the federal tax policy is going to stifle growth over the next two years?

CHIEF INVESTMENT OFFICER ELIOPOULOS: I think "stifle growth" would be way too strong a statement. I think it's unclear what the effect will be on growth. If you look at most of the analysis by economists, the case for stimulating the economy through tax cuts hasn't really proven out over history.

On the other hand, certainly will be returning more cash to corporations in the U.S. That's a fact. So their top-line cash balances will increase, which would give more opportunity to put that cash to productive work. And that's really the question mark is whether or not the effect of this tax cut will be to grow the economy through more productive work and more application from particularly corporations to investing in capital investments for production.

That's the unknown. That's what has to happen. There's another provision in the tax bill that allows for expensing of capital investment. That's a positive for growth. So those two effects are positive.

On the negative side is the question of whether or not both the effect on the most productive states within the country and the disproportionate amount of tax savings or cuts going to the wealthiest in the United

States, who really do not need more income in order to spend, whether that mix and combination of benefits and warning signs will produce growth.

So I think it's more of a balanced weight-and-see approach, and there are certainly some near-term benefits and some longer-term real concerns over whether it's a sustainable program going forward.

COMMITTEE MEMBER COSTIGAN: All right. Well, I have just a couple questions. I was reading BlackRock Report. They look like they've revised their upward projection for the next year or two. The individual that we had speaking to us at the July offsite -- I'm drawing a blank on her name. Just pull the report back up. But they're now looking at projecting -- that we're going to see an upswing in the market.

So I guess I'm not prepared to go where Mr. Jelincic is. What I'm concerned about, particularly -- as we were talking with a local government, we're becoming conservative in the portfolio as a long-term investor. You've got to constantly tell us, you know, we're long term, we can ride the ups and downs. And I'm just somewhat concerned that we're going to leave returns on the table.

Because a year ago, or 16 months ago we took a move to begin reducing the volatility of the portfolio because we thought another candidate was going to win, and she didn't win. And we thought we'd be in a recession right now, and we're not in a recession. In fact, it's the exact opposite. We have seen the most significant gains in the market over the last year.

And of course, I -- you know, the mistake I made was I drew back conservative too; and when I look at my portfolio, I've left a lot sitting on the table in a very diversified portfolio.

So I'm concerned right now. We developed this portfolio based upon a certain set of facts several weeks ago -- and I know you've been working on it for over a year -- and now the entire field has shifted - okay - which a month ago we didn't see. And in September of '16, when we became conservative, we made a projection going out to November and everybody got it wrong.

So I guess I'm asking, particularly when local governments are coming to us and saying they're talking about cutting services in two years from now, we either let -- are we rushing to make the decision today? I mean, do we have all the facts in front of us?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Yeah, we believe we do. And I'll let Eric and Diane speak as well.

The predominant risk and position of the portfolio is in equity. And we have a 50 percent exposure to global equity, we have an additional exposure to private equity in addition to that. So we have an equity-centered portfolio certainly from a risk perspective but also from just in overall exposure. So we don't believe we're missing out on -- you know, missing out on any more increases into the equity markets going forward.

COMMITTEE MEMBER COSTIGAN: So you -- I'm sorry, Mr. Eliopoulos. Are you then projecting over the next year we're not going to see significant increases in equities?

CHIEF INVESTMENT OFFICER ELIOPOULOS: No. We don't do the projection year by year. I think over -- what we're saying is over the next 10 years we've given the Committee our capital market assumptions.

Going into this next year, there's risk to equity valuations, but there's also risk to fixed income valuations as well. We're at a point in the market cycle where every asset class in our portfolio is priced at -- at the highest levels -- or near the highest levels they've been in history.

So --

COMMITTEE MEMBER COSTIGAN: Then I've heard that -- I'm sorry. I've heard that for the last year, that each day is another high mark we met. We went through 24-7 today, we've gone through 24-8 today. And I guess the concern I have is you're talking 10 years out. And I understand we're not looking next year or the following year. When we made portfolio A, B, C, and D there was a certain set of assumptions. So in the last four weeks Congress and the Senate have sent to conference a tax plan. Is that tax plan factored into Portfolio C? And if it hasn't passed and the conference committee didn't come together until this weekend, what's in the portfolio based upon what was decided over the weekend?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Well, certainly nothing in the portfolio has been premised on what happened over the weekend or with respect to a tax bill. We did look quite consider -- with quite consideration at past examples of tax cuts at similar points in an economic cycle. So we went back and looked at the JFK-Lyndon Johnson tax cuts in the sixties at a similar period of high valuations. We looked at the tax cuts -- the Reagan tax cuts in the mid to late 1980s, again another point in time. We had high equity valuations, stable economies, rising fiscal deficits and tax cuts.

We looked particularly at the late nineties, at sort of the end of the Clinton administration here in the U.S. as well as Japan in the late nineties, where you have this mix of high equity valuations, stable economies; particularly looking at the nineties in Japan demographic factors starting to take its toll on the Japanese economy. And what we saw as similarities to today is we have valuations at their highest levels, end of a cycle, and a stimulus or tax provision being brought forward.

What's similar to all those points in history were crises that came in the years that followed, none of them created by the stimulus or tax cuts but by other events. And I think for us the lesson from those periods in time when you have high valuations; stimulus being brought in to the market; and you have other factors such as demographics; and just to add one more because I think it's important looking at the late nineties, technological change that's coming; and, lastly, you add geopolitical risk when you think of those other eras, you -- our conclusion is a somewhat balanced portfolio, as balanced as you can afford, given both the opportunities, because the economy, as you -- as Mr. Jelincic correctly pointed out, economy's in balance, the world economies are in balance, Europe is starting to grow again, China has leveled off and appears poised to grow again, Brazil and India are growing; so there's some positives.

On the other hand, history tells us that there's some risk.

So I think that portfolios that you've been presented, as Ms. Sandoval started with, give you real choices. In the face of this context, in this setting, on balance what we're recommending is a portfolio that is in our view the most balanced of the four in front of you. If the equity markets run some more next year, we'll be disappointed. If they sell off, we'll be modestly happier than having selected perhaps a higher risk portfolio. But at the end of the day we're not predicting one or the other. We're recommending a portfolio that has some balance in the face of the uncertainty that's coming.

COMMITTEE MEMBER COSTIGAN: Thank you, Mr. Eliopoulos.

Thank you, Mr. Jones.

CHAIRPERSON JONES: You're welcome.

Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Thank you, Mr. Chair.

I did just want to say September of last year when we initially adopted the 7 percent ALM under the impression that it was imperative -- and I agree that after -- nobody expected to see what we expected to see in the election. So I agree that after the election, we left money on the table. Our markets are cyclical. So I am of the mindset and convinced that in the long term I think we're better off adopting the 7 percent. So while --

well, how long ago that was, a year and some months ago -- I was against changing to 7 percent based on the cost factor to our employers and our PEPRA employees. I am convinced at this point that the prudent strategy is the 7 percent. So I just wanted to reiterate that, because in September of last year I definitely was not on board.

(Laughter.)

COMMITTEE MEMBER TAYLOR: But I do see that this is cyclical. I also see the newspaper articles that state that the corporations have themselves stated they're not going to be reinvesting in the economy. They're going to use that money in the stock market. So I see an initial great increase in the stock market maybe for a year or so and then I -- then I see a possible decrease. And as I said -- stated earlier, the transfer of wealth is going to be a huge long-term risk. So us staying at our 7 percent I think is our wisest track.

And I thank you.

CHAIRPERSON JONES: Okay. Mrs. Hollinger.

COMMITTEE MEMBER HOLLINGER: Yeah, I wasn't going to chime in but I decided to.

I guess if we were at a different place I would agree with Mr. Jelincic that we're better off with taking on greater risk. And my concern, since my orientation is hedging risk and I hear the debates and we don't know which -- the impact of the new tax laws. But at the end of the day, I look at the fact that we're 68 percent funded. And so at that level, we can't really afford to be too wrong. So I have more of an orientation to protect our downside. That's why at the end of the day, I think C's the right choice. I agree with Mr. Slaton, if we were at a different funding level, I would be agreeing with you, Mr. Jelincic. But so -- and I think it's after meeting with several stakeholders, it's also their comfort level. And so I think it's important to pay attention to their voice in this matter.

Thank you.

CHAIRPERSON JONES: Mr. Moore.

ACTING COMMITTEE MEMBER MOORE: The State Treasurer agrees with the staff, the consultants, and the stakeholders that have commented before this Committee. Candidate Portfolio C appears to be the optimal portfolio in terms of risk and return tradeoff. In addition, the current interest rate risk exposure would be maintained and it would incur minimum transition costs. And it's for these reasons the Treasurer that candidate Portfolio C should be the candidate -- ultimate portfolio.

Thank you.

CHAIRPERSON JONES: We do have a motion and a second on this. But before we vote, there have been several requests to speak on this item. So we're going to hear from the speakers before. And as I say -- well, here are some more.

Ms. Dorothy Johnson, Derick Lennox, Dillon Gibbons, Dr. Ruben Ingram, Dane Hutchings. If you would all come in these front seats here; and you have three minutes to talk, and the timer is right below my name here. And so I would appreciate if you would gauge your comments to stay within the three minutes that is allotted.

MS. JOHNSON: Good morning. Thank you for the opportunity. Dorothy Johnson with the California State Association of Counties. I'll make my comments brief, because we have spent many hours with stakeholders in conversation. And we really do appreciate the robust dialogue here this morning.

For the record, we agree with the recommendation and support candidate C to move forward. It is a balance of risk. And for us, we are not taking this lightly, by any means. We are looking at, as was mentioned, potential low level threats to service levels. But outside the vacuum of pension costs we are also, as was mentioned, dealing with the impacts of the federal tax reform package that is moving through.

In addition, probably the most serious threat to counties is the possible tens of millions of dollars in new costs come to counties as early as 2018 for in-home supportive health care services. This is a major unknown for us. And so for these reasons, in light of the other potential risks at the table, we do support candidate C.

Thank you.

CHAIRPERSON JONES: Thank you.

MR. LENNOX: Good morning, Chair and members. Derick Lennox on behalf of a coalition of school employer associations and groups, including ACSA, the Association of California School Administrators; the California Association of School Business Officials; the Small School Districts Association; and the County -- California County Superintendents Educational Services Association.

We support the staff recommendation of candidate Portfolio C. We strongly appreciate all of the receptiveness that the Board member and staff -- Board members and staff have had towards the comments of stakeholders in the employer community. Although we would of course, you know, welcome lower rates in the future, our support for defined benefits in making sure that the fund's sustainability is going to be there in the long term is an important promise that we've made to the employees that come to work for school districts, and so that's why we think that candidate Portfolio C is going to help strike that balance between long-term sustainability and mitigating significant volatility in the employer contribution rates, especially if school districts continue to face fiscal constraints particularly in the out years.

So, again, we appreciate your receptiveness to all of our comments and we support candidate Profile C.

Thank you.

CHAIRPERSON JONES: Okay. Thank you.

MR. INGRAM: Hello. I'm Ruben Ingram, the Executive Director of School Employers Association of California, representing school boards and superintendents. And we also support staff recommendation on Portfolio C.

We spoke earlier to you last year. And so we've consistently supported the 7 percent level in a spirit of shared responsibility, as Derek said. Of course we'd like lower rates, but we want a guarantee the security to fund and we want to be sure that our employees are going to receive what they're entitled to receive.

Just for your information, we operate under what's called a local control funding formula, the LCFF. And over the last few years, the school districts have received somewhat of -- some increases under that funding formula. But we've reached kind of our limit on that now, and certainly in the out years we're not going to get any increases under that funding. So right now, all of our districts are planning to meet their budgets and to build in these increases that are coming along. And as I said to you some months ago, what we need is just stability. We need to stay the course, and so that our folks can plan for this -- for this year and into the future.

And as several other speakers have said, we just want to be sure that, as some of you said, that you take reasonable risks but not unreasonable risks, because our folks are the ones that are at risk in terms of their retirement.

Thank you.

CHAIRPERSON JONES: Thank you.

Mr. GIBBONS: Members of the Committee, Dillon Gibbons with the California Special Districts Association, also here to support the staff recommendation of Portfolio C and maintaining the 7 percent discount rate and taking what we believe to be appropriate risk in the fund.

As members Slaton and Hollinger pointed out for us, if we were in a different spot, the fund was, you know, much higher than 68 percent funded, I think we would be more willing to support Member Jelincic's idea of taking greater risk and getting more of that upside and the greater returns.

However, if there is a -- a drop in the markets, it's the employers that end up on the hook for picking up the slack, when the -- when the rate was reduced down to 7 percent, it's employers that are paying those costs. Yes, a lot of the employees are as well. At this point they're PEPRA employees. But the majority of those costs were picked up by employers, and we can't afford a drop at this point down to 6 and a quarter percent in order to cover the losses so that this fund doesn't become insolvent.

So to protect the fund, it's -- we want to see the upsides of returns at 7 percent. But we can't afford to reduce the discount rate at this point. And if there was a reduction in the economy and the stock market took a hit, that would -- employers would be on the hook for paying those costs.

For those reasons we support Portfolio C.

CHAIRPERSON JONES: Thank you.

MR. HUTCHINGS: Good morning, members. Dane Hutchings, League of California Cities. I'll keep my comments brief, allowing my comments with the other speakers today.

Simply put, we believe that the candidate Portfolio C does strike the balance between ensuring that we have a responsible rate of return against having some fiscal responsibility and predictability for our employers.

You heard loud and clear from my members in last month's meeting that we are struggling significantly with even a 7 percent discount rate. To go any lower than that would be very detrimental.

At the same time, we certainly don't want you to misinterpret our comments saying that we should be going higher to 7.25 percent. You know, simply put, as my other speakers -- as the other speakers stated, we are not in a position right now where we can endure volatility. 7.25 percent we believe would cause that volatility.

And so we thank you and hope that you can support candidate Portfolio C.

Thank you.

CHAIRPERSON JONES: Okay. Thank you very much.

Well, thank you.

And I just want to thank staff for -- changing of the guards, huh?

(Laughter.)

CHAIRPERSON JONES: Yeah. I just wanted to thank staff for all of the work that has been done to reach this point. I mean, we started back with the portfolio priorities back in January of 2016, and we have approved the asset class descriptions at the January 2017 Board meeting, we approved the capital market assumptions back in early -- late May. And so we've had our ALM workshop that has educated and provided the Board, the Committee information that's necessary to make these decisions.

And I echo the comments about the sustainability of the fund is the priority. And I think under different situations when we were more fully funded, I would be also willing to take that risk. But I agree with my colleagues who have made the comment about the risk level, it would be too great with the -- compared to our current funding rate.

So with that, I'm going to support this also.

So the motion was made and seconded.

All those in favor?

(Ayes.)

CHAIRPERSON JONES: Okay. I will -- okay, but -- so the...

All those in favor say aye.

(Ayes.)

CHAIRPERSON JONES: Those opposed?

COMMITTEE MEMBER JELINCIC: No.

CHAIRPERSON JONES: Okay. Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Okay. I voted no. I think we have made the same mistake we made a year ago. You know, a year from now we will know whether I'm right this time or not.

I would point out that the employers are not currently funding at 7 percent. There is a disconnect between the expected return on the portfolio and the discount rate we're using for funding.

And if people are actually really invested in 7 percent as a funding discount rate, we can do that regardless of what the portfolio we adopt is.

So I just think we've made a mistake. We should have taken more risk. And if 7 percent funding is really what people want, we can do that regardless of what the portfolio is.

Thank you.

CHAIRPERSON JONES: Okay. Thank you again, staff, for that report.

Now we move to Item 6, Investment Manager Engagement Programs.

(Thereupon an overhead presentation was Presented as follows.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Thank you, Mr. Chair and Committee. Wylie Tollette, CalPERS staff. And my time here is brief, as is my introduction to this next item.

Thank you, by the way, for your kind comments and thank you to the Committee for the last almost four years of guidance and experience.

Sitting to my left is Clint Stevenson, our Investment Director over the Investment Manager Engagement Programs. And then sitting to Clint's left is Diego Carrillo. He is an Investment Manager in our IMEP team. And the two of them have been working on our Emerging Manager Five-Year Plan.

So with that, I'll turn it over to Clint.

(Thereupon an overhead presentation was Presented as follows.)

INVESTMENT DIRECTOR STEVENSON: Thank you. Clint Stevenson, CalPERS Investment Director.

This agenda item requests Investment Committee approval to forward the five-year report on CalPERS Emerging Manager Five-Year Plan to the Legislature. The enabling statute requires CalPERS to submit an annual report. This is the last of those reports, or the 2012 five-year plan reporting process.

But first I thought we'd remind you of who we are. We are the group some of you may remember as Targeted Investment Programs, or TIP.

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INVESTMENT DIRECTOR STEVENSON: Now, TIP has evolved and is now named the Investment Manager Engagement Programs, or IMEP for short.

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INVESTMENT DIRECTOR STEVENSON: The TIP functions and responsibilities which are shown on the slide, Slide 2, have carried over IMEP.

In addition, we've been tasked with establishing an external manager monitoring and evaluation program, which we would cover with you in June along with the California investments that are shown at the bottom of that slide. We'll touch a bit on the investment portal and manager solicitation today. But the focus of today's update is on emerging and transition manager programs.

Now, as you know, CalPERS has invested with emerging managers for more than 20 years, either directly or through fund of funds. For purposes of our program, emerging managers are generally defined as newly formed or relatively small firms.

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INVESTMENT DIRECTOR STEVENSON: However, data shows that women and minority managers make up a higher proportion of emerging managers than established managers. Therefore, emerging manager strategies can result in greater ethnic and gender diversity among CalPERS external investment managers.

As you may recall, in June 2016 CalPERS announced the pacing investments of up to $11 billion with the new capital to our emerging and transition manager programs through fiscal year 2020.

So I'm pleased to report that all of the workstreams of the 2012 five-year plan have been successfully completed. Notable accomplishments over the five years include the strategic integration of emerging manager programs into the CalPERS portfolio. Full and emerging manager programs have expanded to include 45 total emerging managers, half of whom are diverse owned, for a total of $3.6 billion in net asset value.

Another accomplishment is the development of the Transition Manager Program. That's shown on the next slide, Slide 4.

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INVESTMENT DIRECTOR STEVENSON: The Transition Manager Program is designed to provide a path of growth and opportunity for successful early stage managers who no longer fit the parameters of an emerging manager.

This program allows CalPERS to continue to invest in successful up and coming firms, including women and minority-owned firms, transitioning from small entrepreneurial platforms to established asset management firms. Indeed, one of the primary objectives set in the 2020 plan is to conduct a solicitation for transition managers. That's shown on page 5.

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INVESTMENT DIRECTOR STEVENSON: We are assisting the asset classes with transition manager solicitation process, completing those evaluations need global equity and private equity. The proposals are currently evaluated and we'll report to the Committee at our next update.

Another accomplishment is shown on slide 6.

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INVESTMENT DIRECTOR STEVENSON: In September CalPERS hosted the 4th Annual Emerging and Diverse Manager Day.

This year -- so then it convened in 52 emerging transition and diverse manager firms, with 107 representatives from around the country. It offers managers and staff both education and networking opportunities, allowing managers that meet the CalPERS emerging transition, diverse manager definitions the opportunity to meet with the senior asset class staff and emerging manager advisors. We think this is a win-win for all parties. We use it to get a better understanding of the investment opportunities that emerging managers are seeing. But managers use it to get a better understanding of our investment objectives, and to provide more access to capital through our emerging manager advisors.

I think it demonstrates our leadership and ongoing commitment to remain engaged in this space. And we'll be making suggestions on how to make it even better in the coming years.

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INVESTMENT DIRECTOR STEVENSON: Another accomplishment is shown on slide 7; and I'll have my colleague, Diego Carrillo, cover these deductions. It would have been Diego and his team too that were really meeting and working closely with the asset classes to strengthen these programs.

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INVESTMENT MANAGER CARRILLO: Good morning. Diego Carrillo, Investment Manager within the CalPERS Investment Office. I'm pleased to cover slide 7, which focuses on recent highlights across our emerging and transition manager programs.

CalPERS recently increased its commitment to real estate's emerging manager program by allocating $350 million of additional capital to his Canyon Catalyst Fund. This brings the cumulative capital commitments to approximately $1 billion since 2012.

And as previously disclosed during the Real Assets program review, the parameters have also been expanded. Paul and his team have achieved tremendous success with this program, and Canyon also deserves credit for their disciplined manager selection and monitoring processes including mentorship.

As of June 30th, 2017, Canyon exceeded obviously benchmarks by more than 1,100 basis points over a one- and three-year time period.

Private Equity recently announced its third transition manager, Valor Equity Partners, with a $75 million commitment. Valor joins Sirius and Clearlake Capital as the three transition managers within Private Equity.

It's important to note that each one of these three were part of our Emerging Manager program.

And thanks for the Board's ongoing support for the Emerging Manager programs we expect in 2018 to at least double the size of Private Equity's Emerging Manager program.

And on a related note. I met in collaboration with Private Equity, who administered solicitation process in the first half of 2018, for the Private Equity Emerging Manager advisory mandate.

It is important to note, however, that we are satisfied with the incumbent. But conducting a solicitation will allow us to evaluate all qualified firms and run an objective manager selection process.

I'll hand it back over to Clint for slide 8.

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INVESTMENT DIRECTOR STEVENSON: And slide 8 just summarizes some of the workstream we're focusing --

That's helpful.

(Laughter.)

INVESTMENT DIRECTOR STEVENSON: Slide 8 summarizes some of the workstreams we're focusing on going forward. And we're going to continue many of the workstreams that were established in the original five-year plan. We're going to be tracking and reporting emerging and transition manager exposure and performance. We'll be engaging and participating in stakeholder event. We'll be forcing relationships with emerging and transition managers. And we'll continue our efforts to improve the program.

So I'd like to finish with some reasons why we do this, given the unique challenges that emerging managers face. And I think we do it for four reasons. We do it to access a comprehensive landscape of investment opportunities out there. We do it to develop relationships with the next generation of investment managers. We do it to generate appropriate risk-adjusted returns.

But finally, at the end of the day, we do this because we think it's vital to improving the performance of our organization and the businesses and markets we invest in on behalf of our 1.8 million members.

I'd be happy to answer any questions.

CHAIRPERSON JONES: Yes, we have some questions. And I have -- you had mentioned on slide 5 that the proposals have been received and are being evaluated. And you mentioned that they would be -- you would update the Committee at the next -- at a future meeting. So when is that date?

INVESTMENT DIRECTOR STEVENSON: I think we're scheduled to meet with them in June.

CHAIRPERSON JONES: June. Okay.

INVESTMENT DIRECTOR STEVENSON: Yes

CHAIRPERSON JONES: The other question is, have we set a date yet for our diversity forum that we have annually?

INVESTMENT DIRECTOR STEVENSON: I don't know that we have.

CHIEF INVESTMENT OFFICER ELIOPOULOS: It's biannual, every two years, not every year. And we're working with CalSTRS to identify the date for the next --

CHAIRPERSON JONES: When did we change it to biannual?

CHIEF INVESTMENT OFFICER ELIOPOULOS: This last one was -- I think the last one was at 19 months.

CHAIRPERSON JONES: Yeah, I know. But I recall discussing why hasn't it occurred. And it was for some logistic reasons, not a policy change moving to a biannual.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Well, that's something that for sure then we could have a -- we should have a conversation to make sure we're on the same page.

CHAIRPERSON JONES: Okay. Appreciate that. Okay. Thanks.

And then just one last question on the -- an appendix on slide page 11, of Attachment 1. The -- at the bottom where you have the numbers in parentheses there, and you have "5 - Canyon Catalyst." Is it -- explain that to me. Is that 5 -- that fund of fund components of catalyst?

INVESTMENT MANAGER CARRILLO: Yeah, that number 5 represents a number of emerging managers within the Canyon Catalyst program.

CHAIRPERSON JONES: Oh, so the 5 are part of the 9?

INVESTMENT MANAGER CARRILLO: The 5 is included in the 9, yes.

CHAIRPERSON JONES: Okay. Thank you.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Well, since I think the report is accurate and reflects when it is, I will move that we send it on to the Legislature.

But on your presentation I do have a couple of questions. So I don't know whether you want a second -- the second first.

CHAIRPERSON JONES: Yeah, let's -- moved my Mr. Jelincic.

COMMITTEE MEMBER MATHUR: Second.

CHAIRPERSON JONES: Second by Ms. Mathur.

Okay. Discussion.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: And then I'll start on 11. The -- and the Private Equity number of emerging managers is 222. And then apparently 21 are in the fund of fund, the -- I mean, what is that box telling me?

INVESTMENT MANAGER CARRILLO: I'm sorry. Yeah, so the definition for Private Equity is first and second institutional fund. So if you look across the entire equity portfolio to apply that definition, you will have 222 emerging managers within the total portfolio. Now this includes fund of fund exposure to emerging managers.

We have a -- what we consider a more strategic portfolio with Grosvenor. This is Domestic Emerging Manager 1 and 2. That advisor has 21 underlying emerging managers within that program.

COMMITTEE MEMBER JELINCIC: How many private equity managers in total do we have if we have 222 that are emerging?

INVESTMENT MANAGER CARRILLO: We have a -- we have a total of -- and this is as of June 30th, 2017, of 99 managers within the Private Equity portfolio.

COMMITTEE MEMBER JELINCIC: So what's the 222 telling me?

INVESTMENT MANAGER CARRILLO: This is --

COMMITTEE MEMBER JELINCIC: I'm just confused.

INVESTMENT MANAGER CARRILLO: I'm sorry. This is exposure to emerging managers that are within our fund of funds portfolios.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

The 99 includes -- good question, Mr. Jelincic. Wylie Tollette, CalPERS staff.

The majority of those managers are held within fund of funds structures. The current active fund of fund structure is the Grosvenor program. That's the 222.

The 99 is where we -- in our count for 99 private equity managers, we really only count the fund of fund manager in that number, because that's the manager that we have contractual relationship with. The contractual relationships with the underlying emerging managers are actually between the fund of fund manager and those emerging managers out there. So this is sort of the look-through down to those underlying emerging managers.

COMMITTEE MEMBER JELINCIC: So we have 222 emerging managers in fund of funds?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: That's right.

COMMITTEE MEMBER JELINCIC: 21 of which are in the Grosvenor?

INVESTMENT MANAGER CARRILLO: That's correct.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: That's correct.

COMMITTEE MEMBER JELINCIC: Okay. And the other comment is on slide 7. I raised this issue last time. I will raise it again since it's my last IC meeting.

The emerging manager program in Real Estate was approved by this Board and had a very narrow definition. The fact that we've expanded property types and geographical regions - and that was a decision that was not brought back to the Board until after it was implemented - continues to be troublesome.

Having said that, the report that -- you know, which we're saying the Legislature is accurate and -- so let's send it on.

Thank you.

CHAIRPERSON JONES: Okay. Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you.

Well, I think this is such an important program; because as a long-term universal owner, it's essential to us that we help foster the future large managers who we expect to be in business with down the road. So I think this is really important. I really appreciate how much this program has evolved and matured and improved in a very thoughtful, analytical, well-considered way. And so I just want to thank you for all of your team's efforts to help mature and develop this program so that it's truly effective in helping us to achieve our long-term goals.

I do have one question. I recognize that in 2017 the transition manager solicitation included only Global Equity and Private Equity but not Real Estate. When is the Real Estate transition manager solicitation expected?

INVESTMENT MANAGER CARRILLO: After speaking with Paul and his team, we expect for this to happen in 2018. There is ongoing segment planning to identify opportunities that could meet the portfolio fit. This process will likely conclude sometime in the first half of 2018. And I think opportunities for solicitations will occur thereafter.

COMMITTEE MEMBER MATHUR: Okay.

INVESTMENT DIRECTOR STEVENSON: At the risk of being kicked in the shins by our -- I mean, one of the --

we want -- thank you for your comment. I think you guys have a lot to be proud of of what you've done, but we've got more work to do. One of the things that we need to do is to think about that whole solicitation process, particularly the private asset classes. We need to be going out, developing relationships in advance, not waiting for the fund raising. That's too late. We need to develop the relationships far in advance of the fund raising so they could get to know us, we get to know them.

COMMITTEE MEMBER MATHUR: And the emerging manager data is not accomplishing that?

INVESTMENT DIRECTOR STEVENSON: And many of these funds -- investment funds they're full. By the time -- I mean they're full. We want to -- we want to make sure we've got a seat at the table.

COMMITTEE MEMBER MATHUR: Yeah.

I'm sorry. So the emerging manager -- emerging transition diverse manager days, those are not -- they're not -- that's not sufficient?

INVESTMENT DIRECTOR STEVENSON: Yeah. No, those are part of it. Those are part of it. But we need to cultivate relationships as well.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Ahead of time.

INVESTMENT DIRECTOR STEVENSON: Ahead of time.

COMMITTEE MEMBER MATHUR: Do you have a plan for how to accomplish that?

INVESTMENT DIRECTOR STEVENSON: Getting out there, meeting folks, talking to them, one-on-one meetings.

COMMITTEE MEMBER MATHUR: Okay. And you have a sufficient staff to accomplish that?

INVESTMENT DIRECTOR STEVENSON: We'll be busy.

(Laughter.)

COMMITTEE MEMBER MATHUR: Yeah.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Probably in partnership with the asset classes as well. I think we -- it's key to have both the IMEP team and the asset classes deeply involved in that relationship building because, as Clint says, I think if -- we want to be the first call when they do come to fund raise because I think what we found is that's advantageous from a variety of perspectives.

COMMITTEE MEMBER MATHUR: I think one of the things that I've heard when I've been out talking to, you know, various groups is that there's a perception that because we're reducing the number of relationships in our overall -- in our private equity and -- well, overall in our investment external managers, that there's a perception that we're not really receptive to smaller or emerging managers. So I think that's something we still need to continue to work to counteract.

Thank you.

CHAIRPERSON JONES: Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Thank you, Mr. Chair.

I also want to thank the team for this report and for the work that you guys have done on the Emerging Manager Program.

I also think it's a very important program to keep moving forward. I understand we have some sticking points for what we can and can't look at in terms of diversity in the Emerging Manager Program. So I'm going to ask a question that you may not be able to answer, which is: Do we have a percentage or knowledge of a percentage of our -- who -- of our emerging managers that are women owned, minority owned? I didn't see that in the report, and I was just wondering if we did.

INVESTMENT MANAGER CARRILLO: Yes, we do. So 53 percent of our Emerging Manager Programs are -- or 53 percent of the managers are women- or diverse-owned firms, 24 of 45 total.

COMMITTEE MEMBER TAYLOR: Oh, wow. Okay.

And then -- thank you very much. That's awesome.

I would like to echo what Mr. Jones said. I think when I first started I thought we were having a diversity day every year.

CHAIRPERSON JONES: Yes.

COMMITTEE MEMBER TAYLOR: Conference. I'm sorry. Not diversity day.

So I think it happened two years in a row and then it skipped a year. So I don't remember that changing and I don't remember us changing that. So, yeah, we probably should talk about that. So I will echo that as well.

And then also I just had a question. Talking to folks at conferences and stuff, I've run into people saying that our requirements for emerging managers seems to be pretty high -- standards are pretty high. And I know we set our policy and our standards, and I'm sure the Board adopted that. And maybe I was there. I don't know.

So I just -- I just hear from emerging managers, you know, brand new managers, et cetera, that we seem to have these really stringent requirements that excludes a lot of people. So I don't know if you guys want to talk about that a little bit and how we can maybe help them move in that direction or -- as we're talking to folks and going out and meeting folks.

CHIEF INVESTMENT OFFICER ELIOPOULOS: One of the roles of the IMEP team is to review the criteria and processes that the asset classes use to seek and then ultimately contract with emerging managers either through a fund-of-fund program or directly through our transition program.

So that's a role that they have.

Certainly the drafting of criteria for the fund-of-funds manager is important, because they're then the first line of selecting the underlying emerging managers.

But that is a function that we continue to see, what is -- what criteria is screening out managers, either in the emerging manager space or in the transition space? But I can assure you we're going to continue to have the same high standards across the board, many -- board, and many, many, many, many, many, in fact, all of our emerging managers that are ultimately selected meet that bar. So --

COMMITTEE MEMBER TAYLOR: Right.

CHIEF INVESTMENT OFFICER ELIOPOULOS: -- we're confident in the underlying emerging manager space that there's lots of candidate firms that meet the high standards that we set. We're continually searching through the mechanics of our criteria to make sure we don't have any unintended screening that is preventing us from reaching the talent that we want.

COMMITTEE MEMBER TAYLOR: So, in addition to that question -- and I don't know -- Clint, I had heard that these folks don't hear back, that they -- I guess they leave their names on -- or, you know, their --

INVESTMENT DIRECTOR STEVENSON: They go through the portal.

COMMITTEE MEMBER TAYLOR: They go through the portal. And then hearing that they're not hearing back. And that's -- many of them have decided to go through CalSTRS rather than PERS because it seems easier, which I hate to hear.

(Laughter.)

COMMITTEE MEMBER TAYLOR: So I don't know if you want to answer to that. I don't know. I'm sure we have something in place to make sure we get back to folks to tell them yes or no, I would assume.

INVESTMENT DIRECTOR STEVENSON: Yeah, we do, we do. And I think -- but a lot of it, I think we have a perception problem. But both you and Trustee Mathur heard the same comments that I've had, that we -- perhaps we're not as -- we're not as enthusiastic about this program as we might be.

COMMITTEE MEMBER TAYLOR: Exactly.

INVESTMENT DIRECTOR STEVENSON: And part of that is that -- I think it was Walt Whitman who said, "If you've done it, you ain't braggin'." We need to do more bragging, because there's a lot that we've done here that we need to talk about. And part of it is just overcoming that view, that we are not embracing this space as enthusiastically as we can.

COMMITTEE MEMBER TAYLOR: I've heard that as well.

INVESTMENT DIRECTOR STEVENSON: I guess we'll be looking at definitions of what emerging managers -- maybe it doesn't -- maybe you don't need to stick with just funds 1 and fund 2. Maybe we need to think about funds 3, maybe we need to think about international. There's a lot of things we'll do definitionally. But as Ted said, there's lots of smart folks out there. We don't need to lower our standards.

COMMITTEE MEMBER TAYLOR: I gotcha.

All right. Thank you

CHAIRPERSON JONES: Okay. Mrs. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

First of all, great work on this. And I note that this is the last annual plan that will be transmitted to the Legislature. And I would encourage you maybe to keep it up, even though it's not mandated. I think this is really a key part of our strategy. And the fact we've been met all of our objectives and then some I think is worth touting and it's part of we can do a better job bragging.

But I do think for our stakeholders and for the Legislature, just some mechanism that doesn't create more work but keeping them informed about what's going on with this program would be helpful.

Secondly, I was noticing some of the highlights on slide 7, which noted that one of the Global Equity emerging managers recently progressed to be a traditional manager, and now has a billion dollars under management. And I was just curious as to whether there are others that are going to follow suit?

INVESTMENT DIRECTOR STEVENSON: Well, we hope so. I guess -- we want to say most of them?

INVESTMENT MANAGER CARRILLO: Well, we certainly hope the same thing as you do. Are you speaking specifically regarding to Global Equity --

COMMITTEE MEMBER YEE: Um-hmm.

INVESTMENT MANAGER CARRILLO: So we are -- we are currently evaluating many proposals that were submitted through the solicitation. And as you probably know, the only way we can bring on managers directly through our public asset classes is through the solicitation process. So there's a wonderful opportunity now. But that evaluation is ongoing and will probably conclude sometime in the first half of 2018.

COMMITTEE MEMBER YEE: Okay. Good.

And then with regard to Global Equity, are the emerging managers more focused on domestic or nondomestic investments?

INVESTMENT DIRECTOR STEVENSON: Domestic.

COMMITTEE MEMBER YEE: Domestic. Okay.

INVESTMENT DIRECTOR STEVENSON: Domestic, yeah.

But one of the story -- I mean, part of the bragging is I think, you know, Global Equity, one of our most successful relationships started off as an emerging manager, Arrowstreet. And we've -- and now they're one of our largest, most successful firms.

So there's lots -- there are a number of stories that we could tell. We could talk about how -- you know, talk about how well Real Estate has done and relative to benchmarking. We've talked about Global Equity where we've got a manager that's transitioned to develop into one of our most successful. We could talk about Private Equity where the three firms that started off at emerging managers and now they're transition manager group.

So there are lots of stories like that that we'd like to tell more of.

COMMITTEE MEMBER YEE: Good. We need to tell more of them. Yes, exactly.

I was curious about the either global or domestic investments because I think there have been some thought that managers to non-U.S. were more competitive because the emerging manager fees for domestic investments were higher. Are you finding that or is that -- I mean, is there -- do you see a big fee differential with respect to whether it's domestic or --

INVESTMENT DIRECTOR STEVENSON: I don't think so.

COMMITTEE MEMBER YEE: -- non-U.S.?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: I don't think there's a trend you can --

INVESTMENT DIRECTOR STEVENSON: Not that I've seen. Not that I'm aware of.

COMMITTEE MEMBER YEE: Okay. That was one of the issues that our sister plan had focused on, so I was just curious.

INVESTMENT DIRECTOR STEVENSON: I think Dan is coming to the table, so he may have heard more constructive.

MANAGING INVESTMENT DIRECTOR BIENVENUE: Yeah, Dan Bienvenue, Managing Investment Director of Global Equity.

We're actually seeing one of the reasons for more participation in the domestic space is just these emerging managers tend to be fairly small. And the public equity investment universe there are 10,000 securities just needs to be narrowed. And there tends to be more with knowledge about the U.S. domestic space. They'd usually come from the U.S. domestic space in terms of their background. And that's why we're seeing it.

From a fee standpoint, the fees are actually a little higher generally on the international mandates, the ex-U.S. But the expense is greater there too and maybe that's what they're referring to.

COMMITTEE MEMBER YEE: All right. Okay. Thank you.

CHAIRPERSON JONES: Ms. Hollinger.

COMMITTEE MEMBER HOLLINGER: Yes. Totally support the Merging Manager Program. Thank you. And I think the Transition Manager Program or providing that continuum makes a lot of sense.

But I want to direct the Chair, Mr. Jones, to have a closed session regarding one of our emerging managers.

CHAIRPERSON JONES: Okay. That -- that would be a direction?

No, no, not for that.

Okay. So that concludes. We do have a motion already on this item and a second. But we have a request to speak on this item. And we'll hear that speaker first before we vote.

And that's Mr. Michael Ring.

MR. RING: Good morning, everyone. Happy Holidays to the Committee. Michael Ring, Service Employees International Union, Capital Stewardship Program.

On behalf of our leadership I wanted to strongly support CalPERS Emerging Manager Program. I'd like to share two comments from two of our leaders that explained why SEIU thinks this program is vital to CalPERS meeting its mission or paying the promised benefits.

First from our international president, Mary Kay Henry, in a letter she sent in August 2015.

"With so much research showing how returns may be enhanced by paying special attention to diversity, it is clearly of paramount importance that trustees consider these factors on an ongoing basis. One can even argue that a trustee's fiduciary duty mandates making these efforts."

And secondly, from SEIU Local 1000, President Yvonne Walker, who spoke at the Diversity Day last year.

"How boldly do we face this moment and decisively break from old thinking? How boldly do we go to diversify? We need talented people who reflect the diversity of our beneficiaries and act in their interests."

So SEIU recognizes the concrete returns that the emerging program provides to the fund's balance sheet; and as importantly for a long-term investor like CalPERS, it also shows the program's commitment -- we support the program's commitment to innovation, equal opportunity; and these things signal to talented folks that CalPERS welcomes new ideas that will bring long-term benefits to the portfolio and lead to the returns we all need.

So I specifically want to thank Diego, Clint, and Ted and the whole team and encourage this Board and all those who serve it, including the staff and the consultants who have done great work on this, to continue to strengthen this program, as we believe it's vital to the long-term success of the fund.

Thank you very much.

CHAIRPERSON JONES: Okay. Thank you, Mr. Ring. And we appreciate your taking the time to come and share your thoughts with the Investment Committee. And do indeed continue to work with staff regarding this program.

So all those in favor, aye.

(Ayes.)

CHAIRPERSON JONES: Opposed?

Hearing none.

The item passes.

We now move to Item 7, which is an information item. But before I ask staff to proceed with Item 7, I would just -- I was looking out in the audience and I noticed the recently elected Board Member, Margaret Brown, is in the audience, and I just wanted to acknowledge that she's in the audience.

Okay. Thank you. Okay.

CHIEF INVESTMENT OFFICER ELIOPOULOS: We're waiting for Wilshire. Right?

Is that 7a?

CHAIRPERSON JONES: 7a.

MR. INGRAM: Good morning. Daniel Ingram, Wilshire Consulting. We actually haven't got a slide for this item on CalPERS' financial analysis of its divestment programs set out in CalPERS Total Investment Fund Policy.

Wilshire provides the Investment Committee with financial performance analysis of CalPERS divestment programs on an annual basis. Our analysis is built to support the Investment Committee's decision-making time frame. In this letter, we provide statistics of the present value estimates of the gains and losses of the four active divestment programs; namely, tobacco, Sudan and Iran is combined, emerging market principles, and firearms.

We've also included in the appendix analysis of performance of the inactive divestment programs.

In running our numbers, we now calculate the financial impact from the date of the last Investment Committee's last affirmation of each program.

And going forward, we will include in the active divestment analysis the gains and losses from the Committee's decision to divest from pre-selected thermal coal securities in our 2018 analysis.

This item is for information. I'm happy to answer any questions regarding these statistics or any other aspect of our letter to you.

CHAIRPERSON JONES: Okay. Thank you.

We do have a two questions.

Mrs. Taylor.

COMMITTEE MEMBER TAYLOR: Yes. Thank you, Mr. Chair.

I just was a little confused, because you -- and I appreciate the report. It seems like didn't we just go over tobacco for the last year? Did we not just do that? So I'm a little confused. Didn't we decide we'd do this every five years? Is this just an annual update? Because you said you're doing this figured from the last date rather than all the way back to when we first divested. So I'm a little confused as to even why we're doing this with tobacco right now. Because I thought we just did this.

MR. INGRAM: So my understanding Total -- the Total Fund Policy, we are on an annual basis analyzing the performance gains and losses since the last affirmation. So we will be coming back --

COMMITTEE MEMBER TAYLOR: That's not what I understood. I thought we were at every five years.

CHIEF INVESTMENT OFFICER ELIOPOULOS: There's two parts to it. Every five years, review the decision whether or not to divest or -- whether to remain divest -- remain divested or to reinvest. That's the every-five-year review.

The policy requires annually to review what's the effect of divestment.

COMMITTEE MEMBER TAYLOR: What policy? I'm sorry. The policy we have adopted?

CHIEF INVESTMENT OFFICER ELIOPOULOS: Yes.

COMMITTEE MEMBER TAYLOR: And when did we adopt this?

INVESTMENT DIRECTOR CROCKER: That was in this past April we adopted updates to the Total Fund Policy. So this review is to cover all active divestments.

COMMITTEE MEMBER TAYLOR: Okay. I'm not sure that we want to reconsider that. I'm not sure we want to keep bringing this up in public session. But that's just my thoughts.

But I appreciate the report. Thank you.

CHAIRPERSON JONES: Okay.

INVESTMENT DIRECTOR CROCKER: My apologies.

It's Kit Crocker, Investment Director, CalPERS staff.

Thank you.

CHAIRPERSON JONES: Okay. Thank you, Kit.

Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

Something that keeps rolling around in my mind, and I don't know quite how to put this out there; that, you know, some of these are older divestments that are listed here. And I guess when we divest, is there a way to capture where those dollars in the Fund actually then get redirected to, for a little bit more transparency? Because I think part of what we're caught by is, you know, we see the numbers but there's really no story behind the numbers about what's happened since. And I'm now suggesting we go back to what happened since tobacco divestment and maybe going forward.

Is there a way to develop a process for how we can kind of just map out, you know, where those dollars go in the Fund?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Wylie Tollette, CalPERS staff.

Good question, Controller Yee. The dollars are reinvested into the Fund based on the current strategic asset allocation of the Fund. For example, in Global Equity they're deployed back within -- the cash that's received from divestment is then redeployed across the proportion of different asset classes, and within the Global Equity Index in proportion to its weight in the Fund.

And so Wilshire's analysis - and I'll ask Wilshire to comment on their methodology - essentially incorporates that impact because the divested security is removed from that index at that point, and then the two are essentially set up in a bit of a horse race at that point. And Wilshire's results are showing you the results of that horse raise.

That's my understanding of your methodology in a nutshell.

Mr. INGRAM: That seems right. I think what we'll probably then do is then go underneath that into sort of individual industry-level sort of redeployment of that capital, which I think sort of -- your point, if we've sort of taken some out of tobacco has somehow been topped up in other industries, we would -- haven't got that level of granularity within the redeployment of capital.

COMMITTEE MEMBER YEE: Is it impossible to do or is it -- I mean, what can we capture?

MR. FORESTI: Morning. Steve Foresti from Wilshire.

In essence, that is exactly what we are measuring. I mean, to Wylie's point, whatever dollars are pulled out of these divested names are invested on a pro rata basis across the rest of the portfolio. So that horse race of sorts that Wylie mentioned is exactly what we're measuring. There's no offsetting tilt that's happening in the portfolio. It is indeed just invested on a pro rata basis across other names.

COMMITTEE MEMBER YEE: Okay. I'm going to have a follow-up question then. I'm struggling a little bit with this. And I understand the methodology. I guess given how much attention there is to the investments from which we've divested, how do we I guess for stakeholders and others give a comfort about what's happening with those dollars after the fact? So -- after the divestment decision? So I'll come back and I'll formulate another question around that.

CHAIRPERSON JONES: Mr. Moore.

ACTING COMMITTEE MEMBER MOORE: Just want to confirm that our policy requires an affirmation every year or five years?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

I'll let Kit quote you the sections of the Total Fund Policy. But your Total Fund Policy requires a review of the divestments and an affirmation to continue it every five. And then it requires your Board's independent consultant to provide a report on the impact on the portfolio every year annually.

ACTING COMMITTEE MEMBER MOORE: So for all the active divestments, can you give me an idea of when the next affirmative -- next affirmation would take place for each of them?

INVESTMENT DIRECTOR CROCKER: Yes. We are -- the compliance unit is looking at that right now. And we've identified a Iran/Sudan for 2018.

ACTING COMMITTEE MEMBER MOORE: So that would be the next affirmation?

INVESTMENT DIRECTOR CROCKER: Yes.

ACTING COMMITTEE MEMBER MOORE: And for all the other active divestments, when would they take place?

INVESTMENT DIRECTOR CROCKER: We're thinking to pace them out one per year.

ACTING COMMITTEE MEMBER MOORE: Okay. One per year?

INVESTMENT DIRECTOR CROCKER: Yes.

ACTING COMMITTEE MEMBER MOORE: Thank you.

INVESTMENT DIRECTOR CROCKER: Kit Crocker, Investment staff.

(Laughter.)

CHAIRPERSON JONES: Thanks, Kit.

(Laughter.)

CHAIRPERSON JONES: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Yeah, I -- on page 2, in the little table there, the heading in the last column is "Estimates Begin in Calendar Quarter." And I'm not sure -- is that really what that column is, or is that column actually the last time it was affirmed?

MR. FORESTI: Daniel, I'll take that one.

So it is in fact. So tobacco's probably the best example there. The reaffirmation took place December of last year. So the first quarter of 2017 would be the first return impact since that reaffirmation decision.

COMMITTEE MEMBER JELINCIC: So then the numbers on Attachment 1, page 3 of 3, that's the loss just in the quarter, since the first quarter of '17?

Mr. FORESTI: I don't have the report in front of me.

Daniel, is that the aggregate numbers or just...

Oh, so we provided in the letter since-inception number's essentially in the appendix of the letter. So that would be back to the inception of the divestment program.

So on a going-forward basis - and this is based on feedback we received from the Committee last year - we're providing both -- since the last affirmation, tobacco is the one example at the moment. But we also for full transparency in the report in the appendix are including that since-inception information.

COMMITTEE MEMBER JELINCIC: Okay.

MR. FORESTI: So there's two sets of numbers, Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Okay. So the 137 million is the loss since the first quarter of --

MR. INGRAM: 2017.

COMMITTEE MEMBER JELINCIC: -- '17.

MR. FORESTI: So essentially two quarters' worth of impact; that's right.

COMMITTEE MEMBER JELINCIC: And on page 3 the $3.9 billion is since inception?

MR. FORESTI: Correct.

COMMITTEE MEMBER JELINCIC: Okay. Thank you.

CHAIRPERSON JONES: Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Sorry. Back up again.

Ms. Yee brought something to my mind. And I was wondering -- I think we were told this before, which is that you don't -- you don't have it to -- you don't have a way to illustrate how that money got invested elsewhere and what we're making in comparison. So if we, for example, took tobacco and firearms and took that money and just put it in global equities, could we not from inception date see what the -- how much money was originally that we put in there, and then the gains and losses, and then put that out as a comparison here?

MR. FORESTI: That -- so -- I'm glad you asked the question because I think it's an important point to clarity.

That's precisely what we're doing. So we were taking the -- for each of the programs we're taking the returns that we receive from your index vendor. We're taking the returns to the divested portfolio and comparing those to a fully inclusive portfolio.

COMMITTEE MEMBER TAYLOR: No, no, no. I mean -- I'm not saying a fully inclusive portfolio including tobacco and firearms. I'm saying you took that money out of tobacco and firearms 15 years ago, or however how long ago. We reinvested it in the Global Index. So it made money. That money made money. It just didn't make money in tobacco and firearms. So what I'm asking is, can you break out that amount of money -- you put this much in, and we made whatever our percentage gain was over that time frame, over the last 10 years - and I don't remember what it is right now. It's 5 -- 7 percent or whatever.

Can you then thereby say that amount of money we took out and put in global equities - say it's $100 million - over the last 10 years made 7 percent in global equities and then compare it to the loss?

MR. FORESTI: Again, that's precisely what we are doing. So we're not just taking, what was the return on the divested assets. We're taking, what was the return net of the fully inclusive. So it is a relative comparison. So the dollars that we present in this report I think are precisely what you're asking for. They are relative to the investment without the divestment. So it captures the redeployment of those assets.

COMMITTEE MEMBER TAYLOR: Okay. So you're saying then there's still a loss in between the two?

MR. FORESTI: Precisely right, yes.

COMMITTEE MEMBER TAYLOR: Okay.

CHAIRPERSON JONES: Mr. Slaton.

VICE CHAIRPERSON SLATON: Thank you, Mr. Chair.

I just -- on Ms. Taylor's earlier comment regarding the timing of the report. You know, when we do divestments, it's an active decision that we're making. And so I encourage the Committee to continue -- I understand the look -- the 5-year decision process to make. But I think it's important for us to be reminded every year of what the impact is of making these decisions. Whether it's positive or negative, I think it's incumbent upon us to be aware of that, because I think it informs us as we wrestle with future potential divestment decisions we might have to make. So I think it's prudent for us to look at on an annual basis.

Thank you.

CHAIRPERSON JONES: Mr. Costigan.

COMMITTEE MEMBER COSTIGAN: Thank you, Mr. Chair.

And just to carry on a little bit about what Controller Yee and Mr. Slaton said.

First of all, there's a Board policy. It's part of us continuing to be transparent. So we're showing the actions that we've taken.

So one is we shouldn't hide from it. The Board made a policy decision not to reinvest in tobacco. It was debated, discussed, you know. And what we're really talking about is that -- Mr. Moore and I were discussing. You can phrase it as lost opportunities. But I understand what Controller Yee is trying to do. It's difficult. You take what may have been a couple billion dollars and it's been redeployed across all of our asset classes. And you can potentially extrapolate, if the portfolio was $3 billion -- I think we're starting to split some hairs. We have to start first with this Board made a policy decision not to invest in tobacco. You stop there. Mr. Slaton is correct, there is an economic cost.

On the other side, this stop could have gone the other way. And we don't know. I mean, just like I wish I had bought Netflix when it was first out, Tesla when it was $8 a share, Bitcoin when it was a hundred dollars.

We can talk -- we can pick any asset and make it...

I don't want us to get lost in the minutiae, Ms. Yee. I think you raise an excellent point: How do you extrapolate backwards? But whether we did it in guns or Sudan, there is a cost. And I think it is important for the Board and policymakers to understand when we identify a specific asset - or a country or something we don't like - that there's a cost associated with it. Doesn't mean we actually lost money. It's just an asset class.

I mean, again, I have no issues with us doing it on a yearly basis. I think that the difficulty is people will zero in on a number without understanding as an entity with over 10,000 public equities and hundreds of thousands of dollars -- or, excuse me -- hundreds of thousands of projects and infrastructure - right - you're talking a small amount over. Again, we could be 200 percent funded if we'd bought Netflix and Tesla and that's all we had done.

And so I -- you're saying this is a little bit of an irrational argument. I think Mr. Slaton's absolutely correct, Mr. Jones. This information is very important. There's a cost to it. And I've been on both sides of divestment issue. I voted not to reinvest in tobacco, and I was a "no" vote when we decided to divest on guns. So it really comes down to the policy discussion and what each Board member believes is their fiduciary obligation is important.

So I think it's a great report. And I agree with Ms Yee; it would be interesting to find out more. But, Wilshire, I think you guys have tried to address it, and I appreciate it.

Thank you, Mr. Jones.

CHAIRPERSON JONES: Okay. You're welcome. Thank you.

Ms. Yee.

COMMITTEE MEMBER YEE: Thank you.

Part of the reason I posed the question is because when we do get to that next five-year point of whether to continue divestment or reinvest, our decision has to be based on economic factors. And I feel like we're not kind of getting the whole picture. I mean, it's all there I think. But usually at that point in time the focus is what we've lost with respect to not having tobacco, in our investments in tobacco, and then what we've lost -- kind of the cumulative impact of that loss.

And I think in order to make the economic finding if in fact -- depending on which way we decide to go, whether to reinvest or to continue divesting, I think that's kind of a critical piece of the information, we need to make that decision.

So I appreciate that it's kind of spelled out here with respect to what happened to the dollars related to these investments. But I think there's kind of a fuller story and analysis to be told here.

So -- but I'm happy to follow up after the speakers. I don't want to be caught again when we come up to that five-year point and we're kind of scrambling trying to figure out how to put this analysis together, because I thought the analysis the last time was quite faulty.

Thank you.

CHAIRPERSON JONES: Okay. Thank you.

Okay. This is an informational item and -- but we do have a request to speak on this.

We have two requests: Derick Lennox and Dr. Ruben Ingram.

You can come forward.

So you spoke earlier, so you know the rules.

MR. LENNOX: Good morning, Chair and members. Derick Lennox on behalf of the Small School Districts Association.

We appreciate you bringing this report together. We think it's important to highlight on a regular basis the effects of mandated divestments. And some of these were decisions made by the Board, but others of them were made for you by the Legislature and others. And so last year we were really proud to work together with your legislative staff and others and other stakeholders to reinforce with the Legislature that, you know, the people who are of the best minds when it comes to achieving risk-adjusted returns are the folks in this building and the ones across the street; not the folks on the other side of, you know, Sacramento in the State Capitol.

And that's what really concerns us. And it gives us quite a bit of heartburn when, for instance, last December or earlier today, we come before you and say, in spite of the fiscal constraints that it's going to create to go down to 7 percent, let's say, we think it's a good idea because of the long-term sustainability of the fund; when months later we're in the Legislature, you know, duking it out over whether to further constrain your investment options and decisions. And that just gives us a lot of heartburn, because we know in the field the kind of difficulties that it creates when we're not achieving the kinds of returns that we'd all like to see.

So should we invest in everything out there that makes money? Of course not. It has to be risk adjusted, it has to be smart. And those risks are risks that you all consider and should be in charge of making. We just don't want other people making them for you. And so when it comes to, you know, stakeholders interest divestment mandates, whether they're coming to you or to the Legislature, we just want to make sure that you hear loud and clear that at least --

Sorry about that.

-- some folks including school employers strongly encourage you to use your power as investors to create positive social change and not follow the political issues of the day and have that mandated upon you. And so that's our perspective.

And we again thank the Board for bringing this item up.

CHAIRPERSON JONES: Thank you.

DR. INGRAM: Ruben Ingram from School Employers Association of California.

I'd just like to say on a personal note, I'm a former school district superintendent, and I've been to many board meetings with a lot of political issues coming before my school board. And I know the pressures that you're under when those appear. And we know at the State level they're even larger than they are when they're at a local district level.

But as Derick said, what concerns us is when you're pushed by the Legislature or these other forces to take away your decision-making ability. And we again urge you to think about the risk involved rather than the political issues that come before you, even though I know those cause a lot of difficulty to deal with.

Over the past few months there have been numerous newspaper articles that I've shared with my board and my members, and I can tell you that unanimously where those -- as you know, those articles tend to say for you to use really good judgment in doing this and not necessarily invest in everything, but be careful about what you do in order to meet your fiduciary responsibilities. And when I've shared those newspaper articles with my folks, they've unanimously agreed with that position. So that is our position and we urge you to give it serious consideration.

Thank you very much.

CHAIRPERSON JONES: Thank you.

We had additional requests. Mr. Gibbons and

Mr. Hutchings. If you would come forward.

I see Dillon is there.

MR. GIBBONS: Thank you. Dillon Gibbons with the California Special Districts Association.

I want to start by thanking the Board for the actions that you've been taking during the last couple of years and your direction to your legislative team to work with the Legislature and educate them on what divestment is and what it means to this fund.

With that, I'd -- I wanted to read to you the policy principle that these special districts adopted just last year on divestment, and would encourage this Board to adopt something similar.

So our policy principle reads:

"Divestment as an investment strategy can present challenging conflicts for CalPERS in balancing current affairs against its fiduciary duty to maximize retirement investments.

"CSDA supports CalPERS' priority to its members as stated in the State Constitution, Article 16, section 17: 'A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.'

"CSDA opposes any efforts that would divert CalPERS from its duty to its members including divestment of CalPERS' assets to achieve political objectives if the divestment would have a negative impact on the overall health of the fund. CSDA supports CalPERS' proxy access efforts to effect change from within businesses that CalPERS has invested in to ensure that they are well managed for sustained, long-term success."

I think that that's -- for us as special districts, that's what we're looking for from you, is it's -- we encourage you to work with businesses to effect positive change. However, that should not be done at the risk or to the negative impacts of the fund.

So with that, thank you very much.

CHAIRPERSON JONES: Thank you.

MR. HUTCHINGS: Good morning, Chair and members. Dane Hutchings with the League of California Cities.

I align my comments with my colleagues who have already testified with regards to divestments. I just think it's important to note that we just had a conversation about the fact that one of the challenges at being at 68 percent funded is that you can't be more aggressive. And that hamstrings your investment team, it hamstrings your membership who are trying to -- or that are struggling rather to make their monthly or yearly payments.

You know, staff has articulated, you know, not only in this forum but in -- during the educational forum that, you know, really by selling a high value asset to another investor who does not leverage their proxy voting such as the way this Board does, not only is it a potential loss to the fund but there's really no effectuation of change to the company.

And so, you know, really I -- it's that saying, you do more good from the inside than you do by selling an asset to someone else who doesn't care if a -- if a company is socially responsible.

I think it's also important to note too that there is a significant difference between ESG and divestment, and that's something that your staff is done a great job in educating our members about the value of having ESG or having some of those priorities versus just straight divestment. So I know that I've been doing my level best to educate our membership on those differences, because I think it's easy for folks just to, you know, lump them all together.

And, you know, finally by -- you know, whether the number I've -- we've heard things like its cost to fund, $6 billion or $10 billion. It kind of goes all over the map. Regardless, if that's money on the table, not only are we not improving our funded status, but we're really, you know, hamstringing the investment team that works so hard to try and maximize returns.

So on one hand we tell them they can't invest in this, this, or this, and then on the other hand we chastise them in the media for not deleveraging a higher return. I think that this Board and your staff need all the tools available to maximize those returns, to ensure that that is just one piece that we can take care of that's going to be able to help your members who are paying and those employees who are relying on these pensions.

Thank you very much.

CHAIRPERSON JONES: Thank you very much for your comments.

You know, Mr. Lennox' comment triggered a question in my mind.

Which of the active and inactive components are legislatively driven versus the Board driven?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

I can take a crack at that, Mr. Chairman. Wylie Tollette, CalPERS staff.

So to be clear, the legislative divestments that you -- that are currently active as solicited in Wilshire's report do include the language that the divestments must be consistent with your fiduciary duty.

So that to a certain extent puts the onus back on the Board to try to determine that. However, the Legislature did pass the Iran and Sudan divestments. The tobacco and firearms divestments were Board decisions.

CHAIRPERSON JONES: Okay. And inactive?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

And inactive: The South Africa was legislatively mandated, the EM Countries was a Board policy, and the EM Principles is actually also a Board policy.

CHAIRPERSON JONES: Okay. Thank you very much.

Okay. That concludes that item.

We will take a 10-minute break. Let's reconvene at 11:01 for the next item on the agenda.

(Off the record: 10:51 a.m.)

(Thereupon a recess was taken.)

(On the record: 11:02 a.m.)

CHAIRPERSON JONES: Could I ask all Board members to return to the dais please so we can -- Okay.

Okay. The next item on the agenda is 7b, Responsible Contracting Program Annual Report.

(Thereupon an overhead presentation was Presented as follows.)

INVESTMENT DIRECTOR SIMPSON: Thank you very much, Chair. I'm Anne Simpson of the Sustainable Investment Program; and I'm joined by Carrie Douglas-Fong, who was previously with the TIP program. And I'm delighted to say that this work, including the diversity work with the diversity forum, which was being talked about earlier, has now been moved into the Sustainable Investment Program, which is a wonderful next step on integration.

I'm also joined by Paul Mouchakkaa, who's the managing investment director for Real Assets, and deserves a lot of the credit for the good news that we're about to share with you on the Responsible Contractor Program.

So I'm not sure who's got the clickers at this point.

Thank you.

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INVESTMENT DIRECTOR SIMPSON: I'd like to start with saying how important this program is I think to CalPERS' reputation and credibility. When the Board worked to develop and adopt Investment Beliefs, there were two ideas that have since proven to be extremely important for our focus on long-term risk-adjusted returns. And the first is the idea and Investment Belief 3, which is that our investment decisions may reflect wider stakeholder views - and rightly so - provided they're consistent with our fiduciary duty to members and beneficiaries.

And when Carrie takes you through the presentation, you'll see how the involvement of stakeholders, both labor representatives through the unions and also our external managers and staff, work together in a stakeholder dialogue to get these good results.

But the second investment belief that I think is relevant to the responsible program is the idea of the importance of managing human capital. And Investment Belief 4, as we all know it by heart, says: Long-term value creation requires effective management of three forms of capital: financial, of course we know that, it's always been our day job; but physical, which is why we have a concern with environmental issues; and human.

So with that investment belief framework, we're going to be looking at the year's progress on what is in fact a very long-standing policy and one which I think has been very carefully negotiated with all stakeholders over a period of time.

So let me turn now to Carrie, who's going to take you through the progress from this year. And we'd be glad after that to answer any questions that you might have, either for me or for Paul.

So, Carrie, over to you.

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: Good morning. Carrie Douglas-Fong, Investment Office team member.

This morning I'm going to provide you with information on the Responsible Contractor Program Policy, also known as the RCP Program for short.

I'm going to run through the purpose of the program, its history, the scope of the policy, the contracting amounts and compliance for this year and the last six years, the communication framework that the policy sets up, and give you a few examples of the Responsible Contractor Program Policy in action and results.

Anne spoke regarding Investment Beliefs 3 and 4. The policy states that CalPERS has a deep interest in the condition of workers employed at CalPERS-owned assets. Through the Responsible Contractor Program Policy, CalPERS supports and encourages fair wages and benefits based on local market conditions for workers employed by our managers, our contractors, and our subcontractors, subject to fiduciary principles.

The RCP Policy seeks to secure the condition of workers, without adverse defect on investment returns, access to investment opportunities, or significant costs.

The policy creates a framework for responsible contracting based on local conditions that we have assets.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: So we have lots of records on the Responsible Contractor Program Policy, and the very first time that the policy is referenced is in 1992. The Board at that time had let staff know that they were interested in a Responsible Contractor Program Policy for real estate. Staff went back and talked to stakeholders: Labor, CalPERS internal investment managers -- excuse me -- external investment managers, fiduciary counsel, and other stakeholders and began developing what would become the Responsible Contractor Program Policy.

In 1996, the Board approved the policy, and over the years it has evolved. The most recent evolution of the policy occurred between 2010 and 2013, where there were two different sets of amendments; and another review from 2014 to 2015. Over this five-year period, the Board asked staff to spend significant resources reviewing and revising the policy. At the Investment Committee's request, staff initiated significant engagement with all labor stakeholders and investment managers on the RCP Policy.

The results were a groundbreaking neutrality trial for core real estate and infrastructure managers applied to service contractors in 2010.

In 2012, the policy was then revised again significantly, increasing manager responsibilities and establishing more significant roles for labor stakeholders, external investment managers, contractors, and staff. As part of this review, the Board asked staff to look at union-only policies, applying the RCP Policy to other asset classes, and requiring neutrality of managers and subcontractors to both service and construction contracts.

In each review that included multiple discussions and written communications with all sides was an important part of the process.

The most recent revision in 2015, the neutrality trial for core managers, became permanent policy and the Investment Committee approved a new neutrality trial applicable to select non-core managers, essentially six funds.

The CalPERS certification for responsible contractor status was significantly revised after careful negotiation with both managers and labor. It went from essentially a simple certification to a certification with questions on it in regards to:

Do you pay fair wages and benefits based on local market conditions?

Do you pay benefits?

Do you pay medical benefits?

Do you pay dental insurance?

Do you pay other types of benefits?

And then finally, is there a retirement program?

There also are a number of questions in regards to the -- whether there have been fines; whether any of the -- the officers of the company have been de-barred, the company has been de-barred over the last two years.

That had been an entirely separate document that managers did not always see. But in that last revision, that actually became a part of the process, and it is a part of the certification that they sign.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: I'm going to say again that this was done in very careful negotiation, with managers and with labor stakeholders. The direction from the Board was to try to make sure we have a policy that works, enables us to be competitive in the marketplace, and still ensures that we're hiring responsible contractors as much as possible.

On July first, 2015, real asset managers began operating under the enhanced policy. This is going to be the second report under the 2015 Responsible Contractor Program Policy.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: The scope of the policy. The policy applies to real estate and infrastructure assets where CalPERS holds greater than 50 percent interest. So it applies where we have a majority interest and we have control. And it applies on large contracts, so contracts that are a hundred thousand dollars or greater. And the annual report always speaks to the number of contract dollars awarded under the policy, and the responsibilities that the managers have. So we always report on the managers state that they have tools in place to teach their contractors and subcontractors what the policy is. They report if they've had significant interaction with labor stakeholders, or if there are other things that came up in the policy such as we're finding we only -- in certain areas we only can find one contractor, and that contractor is our choice.

So it's -- it's an annual report that discusses important things like that that we need to be aware of in the marketplace.

And finally, when the policy does not apply, when we do not own 50 percent, the policy encourages our managers to act in the spirit of the policy. And there have been times where the policy doesn't apply but we have engaged with both labor stakeholders and also with -- with managers to try to resolve some kind of an issue.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: This shows the our RCP compliance and total contracting. This past year, it was 99.97 compliance, and $1.18 billion worth of contracting went through the policy.

So it was contracted under this policy. It was contracted under the -- essentially this process for assessing and understanding contractors.

The total amount of contracting over the last six years, it's $6.1 billion. And it's a fairly lengthy amount. I can't go back any further than six years, because at that point we went to paper files and I can't find it. But $6 billion is a significant amount of money.

(Laughter.)

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: I'm sorry?

CHAIRPERSON JONES: No, J.J., let her finish.

COMMITTEE MEMBER JELINCIC: I was just going to say, that's not good point to -- for your trustee to hear, that we can't find a --

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: I'm sure we can find them in we wanted to -- we needed to locate them.

But nonetheless, in my records, we have 6 billion worth of contracts that have been issued and let under this process which looks at whether the contractor is responsible or not.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: The RCP Policy sets up communication channels. So in the policy it states that managers need to notify unions in some manner when they enter a new -- when they enter a new area. So, for example, I think we had six this year that entered a new area. Sometimes they do it through ads. Others send out emails. Others wait until they actually have contracting to -- contracts to let and then notify.

Unions provide managers with lists of responsible contractors, and may also sign up for unions -- for managers automatic -- they have aut -- some of them have automatic notifications. So you sign up on the website, and both the unions and the signatory contractors can get -- automatically get information.

So that gives you a little bit of an idea as to the policy and how it's set up to really create continuous communication through web managers, contractors, and unions.

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ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: Next slide.

In addition to that communication, we also have really a continuous feedback loop between staff, managers, and unions.

We are talking to real asset managers on a regular basis when there are questions. And we engaged ex -- we engage extensively when the policy was reviewed and revised. If questions come up from a particular union - recently we've had a few questions - we will spend significant -- significant time talking to both those stakeholders and also our managers to try to make sure we understand what the nature of the issues are, and hopefully assist in communications so that the issue can be resolved or a path forward determined.

Some quick examples of I think not just the policy in action but also setting up a culture where managers and stakeholders and contractors are encouraged to talk to one another, Commonwealth and SEIU have worked together on a green cleaning initiative. And in a number of Commonwealth's office buildings they bring in green cleaning. SEIU and the contractors train janitorial staff. Janitorial staff gain skills. I think in speaking to staff who's received this training, it really improves their desire to come to work. They feel good about themselves. They're also frankly not subjected to harsh chemicals.

Commonwealth does an education campaign with the tenants. So it becomes a -- a continuous loop of positive communication in regards to why green cleaning is beneficial for the building, for the contractors, for the employees and the janitors who are doing the actual cleaning. And finally, for the landlord. And tenants often actually prefer it.

The next one should read Commonwealth / LiUNA. In Texas, which is I believe a "right to work" state, LiUNA does not have a very active presence. When Commonwealth was doing work on an office building there, they actually hired the very first LiUNA member to work on that project, giving them a presence in Texas that hadn't existing before. And I think that's the kind of relationship that sometimes is enabled by working through the policy.

Finally, another example which isn't so much RCP but is more a result of that culture the RCP really encourages. Our project in the Port of Oakland was -- there were a number of stakeholders involved both related to the port, related to the community, and also to labor. Centerpoint was able to work with these stakeholders and, with the Port of Oakland, to develop a community workforce agreement that was very cutting edge and which will be in place on the project that Centerpoint is doing in the port. It was not easy to do. It may sound like a very small thing, but that ability to engage and work together, which I think the policy helps support, was really what enabled this to happen.

Finally, I want to say in closing that the policy -- we think the policy that you have developed and evolved over the years is important to the marketplace. We often get phone calls from other pension funds looking to put their own policies in place. It is frequently referenced and sometimes replicated by other public pension funds and even other investors.

It sets a standard for responsible contracting in the marketplaces where we invested, particularly the mixed markets, like Seattle, San Diego.

The RCP Policy was developed to provide a framework for responsible contracting on CalPERS' investments, with sufficient flexibility to provide both risk mitigation and also sufficient returns.

The most recent revision took approximately five years, three substantial amendments, and has been in place for two. The policy applies to contracts of a hundred thousand dollars or more on domestic assets where CalPERS holds more than 50 percent.

This past year, we bid out over 1.1 billion in contracts; over the last six years, 6 billion.

It provides communication framework, which is utilized not just for contracting but for other things too. And it has positive benefits to our stakeholders and also to our properties.

And with that, Anne, back to you.

INVESTMENT DIRECTOR SIMPSON: Thanks very much, Carrie.

Well, Paul and Carrie and I would be delighted to answer any questions that you might have --

CHAIRPERSON JONES: Okay.

INVESTMENT DIRECTOR SIMPSON: -- on the report.

Thank you.

CHAIRPERSON JONES: Thank you.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: An observation and two questions.

I live in the Bay Area. The Centerpoint project in Port of Oakland actually has gotten a fair amount of press, most of it very good. But one of the frustrations is I don't think anybody in Oakland understands that that's us. And I think our PR people ought to do something to make sure we get some of the credit for it. So I offer that observation.

My two questions are actually on page 3 of the agenda item. You point out that there were no formal complaints filed during the reporting period. But it continues to absorb a significant amount of staff time.

So the question is: What is that significant amount of staff time?

And you can think about the next question, which is two paragraphs down. "Staff recommends that new opportunistic Real Estate and Infrastructure funds continue to operate on a voluntary basis under the Neutrality Trial." And my question is, if they want our money, why don't we say these are our standards. I can't -- I understand we can't do that to people that we already have a contractual relationship with. But this is specifically new. And so I would appreciate, one, what is significant, and why let new people off the hook?

INVESTMENT DIRECTOR SIMPSON: Yeah. I'm Anne Simpson. I'm going to answer the first part of your question, Mr. Jelincic. And then I'm going to turn to Paul to talk about how the policy is reflected across a broader section of the portfolio.

When we say "significant amount of staff," I think you can tell from Carrie's presentation that she spends an extraordinary amount of time listening, understanding, bringing groups together, actually focusing on what can be very complex and difficult areas of disagreement. But I think a great toll she has. But with that patience and with that other staff support that Carrie has on her team, it's actually bringing the parties together so that they're able to resolve the approach in a way that's going to give all sides a sense that progress has been made, in other words to get a positive outcome.

So when we say substantial staff, we mean that very seriously, because we see the benefits to the portfolio, which is what staff are here to ensure. And as Carrie I think suggested in her examples, what we're finding is that we gain insights into the relationship of the managers and the properties that we own, and understand better where some of the trends are going. I think an example with green chemicals for cleaning is an excellent example where you see the whole of our sustainability agenda coming together, because it's something that tenants find valuable, landlords appreciate it, it's good for the janitorial staff, and we reap the rewards in terms of the returns that follow.

On your second point about rest of the portfolio, let me turn to Paul to answer that.

Paul.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Carrie wants to start off.

INVESTMENT DIRECTOR SIMPSON: Carrie's going to start first. Very nice.

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: Good morning. Carrie Douglas-Fong.

There were only six funds that the new neutrality trial covered. And in the two years that we have had the trial, there's only been contracting in those six funds that's applicable in the last six months.

So we have one asset in Texas that was able to work with the neutrality trial. There were no issues. All of their contractors were happy to sign the waiver. But it's not very much information to go on. We had hoped to have at least three assets, if not six, where we could base some actual -- we'd have some actual results, and it just -- that is not the way it has worked out.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Paul Mouchakkaa, CalPERS staff.

I'll add to your question, Mr. Jelincic. Really the RCP taking a step back fits very neatly in the overarching ESG implementation, whereby we all are thinking about the contracting and the monitoring and management of our portfolio.

And what I mean by that is in our separate account model really it becomes -- the components of the E and the S can many times be a function of the G. And the G in which we implement our Real Estate and Infrastructure model is primarily through the separate account model whereby we do have high governance. In those instances when we do have a separate account, and we own the asset greater than 50 percent, which is the vast majority of our

Real Estate portfolio today, the RCP is in effect. And any new contract in which we would go forward in a new separate account, we would also have that part of the contracting and negotiation.

In cases where we occasionally do a commingled fund, we are generally not anywhere near the 50 percent threshold, and we are more or less a - using an economic term - a price taker in terms many of the -- of the components of that fund, and we're generally nowhere near the 50 percent threshold. We have not pursued a large portion of the Real Estate portfolio in that model; but in the separate account model, we do put the RCP program in effect.

COMMITTEE MEMBER JELINCIC: Thank you.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: You're welcome.

CHAIRPERSON JONES: Mr. Bilbrey.

COMMITTEE MEMBER BILBREY: Thank you, Mr. Chair.

So let me turn to the certification process for a minute. Is it correct that I understand correctly that it's a self-certification process, about eight questions?

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: That's correct.

COMMITTEE MEMBER BILBREY: So what do we do to verify? Do we do random audits? Do we verify the information that they're doing on the self-certification is actually accurate?

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: It's a self-certification policy. And so what we would do is in the event that an issue came up, we review with the manager the information on that certification.

There also are times where the forms are audited.

COMMITTEE MEMBER BILBREY: Okay. So that does actually happen? Because I'm hearing from LiUNA and others that they're -- they fill out the -- fill out these forms, and of course they put down glowing remarks, and then it isn't really followed up on. And so people aren't really checking and some of them are not obviously being fully forthright in what they're answering.

So I ask the Board to make sure you follow up on this policy on a regular basis to make sure that we are having these managers do what they're supposed to be doing.

Thank you.

CHAIRPERSON JONES: Thank you.

Mr. Lind.

COMMITTEE MEMBER LIND: Thank you.

First I wanted to thank Carrie for the vigor that she's, you know, shown for this -- your increasing role in the RCP Program, it's clear that you are committed to making this work. So thank you for that.

You know, as I'm out talking to different groups and folks I like to brag about our policy, because we leaders here and people recognize that. And it's important. Even though we have not yet, you know, adopted a workplan around income inequality or economic inequality, this is an example of something we're already doing to address that. And we're doing it in a way that clearly is not only good for reducing inequality but for, you know, increasing our -- the strength of our investment returns. So it's important stuff.

It's not perfect. I, like Michael, have heard from some of the labor organizations that -- particularly from the trades that, you know, have some issues. But I have encouraged them to have a dialogue with you and others, and they have, and they've told me that it's constructive dialogue; and I'm sure, you know, we'll continue to have and build those relationships.

But we should -- as J.J. mentioned, we should brag more about this program, what it really means on the ground at places like Centerpoint at the Port of Oakland, because it's so important.

So thanks to you and the other staff for the continuing work on this.

CHAIRPERSON JONES: Okay. Thank you.

Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Yes, thank you, Mr. Chair.

I also wanted to applaud our work here on the RCP Program. It's so important. When I started, you had just pretty much implemented it, and I see it's really taking off and going far. And it's so important to the sustainability of the fund.

And I -- as Mr. Lind mentioned, I know LiUNA has also mentioned that they want to move that forward into other parts of the fund.

But I think really what I'd like to make sure that I'm asking here is, how come -- one, how come only one in six in the last month -- or last six months applied? And then the -- when it happens that we don't have controlling interest and we use spirit of the language, how does that play out for us? I just kind of want an example of how that plays out for us.

INVESTMENT DIRECTOR SIMPSON: Thank you. Thank you, Ms. Taylor. It is an important program.

We just wanted to clarity the question. Carrie's glad to answer. But want to make sure we understood.

COMMITTEE MEMBER TAYLOR: I think you stated earlier that you've only had -- and maybe it was -- hold on. Let me make sure it's not in the report. You had only had one in the last six months come through; am I correct in hearing that?

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: So the -- the new neutrality trial there were only six funds that that covered. And the as -- their -- the assets need to be developed. So only one of the assets was developed and had any -- any applicable contracts that were service contracts that -- where the NTP would apply. So it was -- it wouldn't necessarily be something that is -- is positive or negative. It's just a matter of how much the contracts wind up being in that locality. And we expected there to be larger-dollar contracts than there have been. It just -- it was --

COMMITTEE MEMBER TAYLOR: It just hadn't --

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: -- somewhat surprising, yes.

COMMITTEE MEMBER TAYLOR: Has it -- and I don't want to even ask this question. Does it have anything to do with our policy?

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: It has absolutely nothing to do with -- no, it doesn't have to do with the policy. It's just --

INVESTMENT DIRECTOR SIMPSON: Circumstance.

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: -- circumstance.

COMMITTEE MEMBER TAYLOR: And then my second part of the question was: Where we have less than 50 percent controlling and we use the spirit of the law, can you kind of give me how that plays out for us. How do we use that?

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: I can maybe chime in.

COMMITTEE MEMBER TAYLOR: Sure.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: I'll give an example. It's hard to give precisely how it may play out. But I want to let the Board know that -- I'll give an example of our Port of Melbourne investment in the Infrastructure portfolio. We do not own 50 percent of the port. Yet, staff, including Carrie, we reviewed the RCP Policy with respect to our manager, QIC in that instance, and also carefully monitor even with our lower proportion any issues that may arise within that holding. I mean, it's a complicated holding given it's a port, and it's outside of the United States.

So the RCP doesn't actually apply to it. But we ensure that we review whichever manager it may be their own RCP Policy. And what I have always instructed our new investments team to do is to then cross-reference it to our own RCP and see where there may be learnings in certain instances or gaps. And we can't necessarily enforce it upon them, but we can at least be aware of what's going on.

COMMITTEE MEMBER TAYLOR: Great. I appreciate it.

I think it's so important that we make sure that workers have fair wages, fair working conditions. We've talked about other issues on this Board where workers have gotten hurt, et cetera, and we've had to address it at a last-minute situation. And I'm very appreciative of this program so that we could address it before that happens. Because in terms of long fund -- long-term fund sustainability, if you don't have a supply chain, you can't -- you have no -- nothing to invest in.

So it's very important that we protect that supply chain, I think.

Thank you.

CHAIRPERSON JONES: Ms. Mathur.

COMMITTEE MEMBER MATHUR: Thank you.

I want to add my comments about this important policy. Obviously it's been in place, I think as you noted, for about over 20 years. And over that time it has been periodically reviewed and improved I think based on really collaborative, constructive, inclusive engagement of relevant parties. Which I think that in and of its -- the policy itself is a model, but that process is also a model for success. And I think that really is -- I think this policy could not be as effective as it is without the dogged, thoughtful, constructive facilitation and commitment of our own team across the asset class and your team, Ms. Fong.

So I want to, first of all, thank you for making this such a successful program. I think it's really due to you and your team that it -- and other investment staff that's involved in it that makes it so successful.

I do have one question. And, that is, in cases where we might not have a 50 percent ownership of a particular -- or stake in a particular asset or fund, there might be other investors who have similar values. Maybe they don't have as -- similar values or similar policies in place. Do we work with other investors in those cases to see if there's an appetite within that fund to -- to enforce this kind of a policy with the manager?

ASSOCIATE INVESTMENT MANAGER DOUGLAS-FONG: We really have not done that. When we -- when we know CalSTRS is also invested, we will sometimes talk with CalSTRS. But as a rule we haven't communicated much with other pension funds.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: True. In certain cases, I'm thinking, and again, in our infrastructure portfolio where this is more prevalent to your point --

COMMITTEE MEMBER MATHUR: Yes.

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: -- we will if there's some large work going on at an airport or -- we only recently did the Port of Melbourne deal -- we will talk to the other shareholders if there are certain issues that may come up.

But I do think you raise an interesting idea and point.

COMMITTEE MEMBER MATHUR: I would think specif -- you know, specifically with the Port of Melbourne, I believe at least one of the other investors is an Australian pension fund --

MANAGING INVESTMENT DIRECTOR MOUCHAKKAA: Correct.

COMMITTEE MEMBER MATHUR: -- which has similar views or similar policies to what we would have, I believe. And so I imagine that there might be some additional opportunity in that area.

So thank you very much.

CHAIRPERSON JONES: Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

And thank you, Carrie, for all of the great work. You really have become the face of this policy externally. And I'm sorry you're saddled with unfortunately a lot of the requests that come in that oftentimes don't really I guess meet the scope of the policy. So -- but just really appreciate your working through those.

I just want to kind of see whether there might be a way for us to be proactive about getting word out about the policy, and what I think is really a misunderstanding about the scope of the policy.

I think there is a misunderstanding about the fact that this policy doesn't solve everything. That may be -- whether it's any wrongdoing or any kind of underground activity, whatever the issue is. But, you know, there are larger networks - and I'm not suggesting that we join them. But I think some educational opportunities before some of these networks might be appropriate. Because as these issues arise, there might be other entities who may actually be the better recipient of concerns that do arise.

And just in terms of here in California, you know, just a foundation for your contracting, there is a whole network of people and State agencies and private vendees that work around the whole -- a range of issues around the underground economy that I think would be really beneficial if we could plug ourselves into putting on some educational sessions with them.

Because I do find that where there's a misunderstanding is where I try to help with some of the public education is really on the scope of the policy. And I think we can be a little bit more proactive with respect to just putting it out there. I think the examples are great. It really brings it home in terms of where we can be helpful.

And I would agree with J.J. and others who's saying that where we've had successes, we really should attack those more.

Thank you.

CHAIRPERSON JONES: Thank you.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Yeah. I'd like to follow up on Michael's question about the audits. And I'm glad to hear that we are doing audits. Presumably we're also doing some spot checks. But I will tell you, that's not consistent with what I have -- what I have heard in the past.

But I'm glad if it's happening now.

Thank you.

CHAIRPERSON JONES: Okay. Thank you.

I heard a theme the last two presentations in telling our story. When we talked about the emerging manager program, one of the comments Clint made is that we, you know, are going to be beef up telling our story. And then here was a similar kind of comment about, you know, we're doing good but who knows about it.

So I think that maybe a broader area for a takeaway and direction is to see how we could better market ourselves to the various committees and components of who we do business with and to the broader community, so it may be able to add some value to our programs.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Yes. And I'll work with our CEO and Brad to think about strategies to do that.

CHAIRPERSON JONES: Okay. Thank you.

Okay. We do have a request to -- one request to speak on this item.

Michael Ring.

MR. RING: Hello again, Chairman Jones, Committee members. Michael Ring SEIU Capital Stewardship Program.

Just wanted to share SEIU's strong support for this program. I also probably am one of the reasons that the staff time is being used a lot that J.J. referred. So I apologize to Ms. Douglas-Fong and other colleagues; and also to consultants like Mr. Emkin's team who work with many of us.

I think that the takeaway that I'd like you all to share is that, while clearly SEIU comes at this work, most people assume, on the perspective of the janitors and security guards we represent in the industry - and that absolutely is a critical component of this - this program is really at the center of what I believe is a very thoughtful approach to fiduciary incorporation of human capital management issues into the industry.

And the ability of the real estate markets to be sustained, especially high-level core real estate that you guys are focused on, the tenants in those buildings expect excellent service. They expect to be treated and have a great experience when they come to do their jobs. And the only way they're going to do that is if the workforce is in a position to deliver those services; and that's really what this program is about from the Fund's perspective. And I think that your team is at the front of that. I know there's work to do with some of our colleagues in different parts of this industry, and I don't think that's going to change. I think that the policy is a living document and that the program is a living program, and this is an area that we all need to work together on to really figure out how do we incorporate the people who do the jobs that bring value into the Fund to the forefront. And this program is exemplary and I'd like to congratulate the Fund for being a leader and starting this program many years ago but also continuing to dedicated sophisticated, thoughtful staff and collaborating with service providers who really understand this area so that we're successful on all fronts in making sure that your program in the real estate industry is successful.

So thank you very much.

CHAIRPERSON JONES: Okay. Thank you, Mr. Ring. We always appreciate your comments.

Okay. The next item, Item 7c, Investment Office Roadmap and Target Operating Model Update.

CHIEF INVESTMENT OFFICER ELIOPOULOS: Mr. Chair, while Wylie is getting his clicker and getting ready to introduce or cover the office roadmap and target operating model update, let me just as a brief introduction just add my thanks and sincere appreciation to Wylie for his leadership in the Fund. And I think it's appropriate that this last agenda item -- although I know we have some consent agenda items to come. But this particular agenda item that Wylie will walk you through is appropriate because he has been an exceptional leader for CalPERS and particularly in the areas of our crafting and architecting our strategy, our roadmap, our governance model, and all of the things that come under the target operating model.

And I just praise him as a partner and a person, but also I think to give praise to those that come out of the private sector to serve in the public sector for the mission that really resonates with all of us. That calling is a special and unique one and I think CalPERS has benefited from Wylie's commitment to that. And I think what you see reflected in this agenda material is really a sign of what can happen at an institution when we're able to get someone of such talent.

So, Wylie, take it away.

Thank you.

(Thereupon an overhead presentation was Presented as follows.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you, Ted; and thank you for your leadership and partnership over the last almost four years. It's been a true pleasure.

And that also gives me a chance to thank Matt, who will -- is going to be taking on the acting COIO role. And you've got a great candidate for that. He has been with the target operating model, which is a key component of the 2020 Vision, since its inception. So he has a great deal expertise on that.

So I'm going to take about 10 or 15 minutes to sort of walk through slides. And then I would encourage questions for Matt or Ted or I on anything I discuss here.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

So the INVO 2020 Mission and Vision were first communicated to the Committee and staff in December 2014.

These statements articulate the Investment Office's mission to manage the CalPERS investment portfolio in a cost-effective, transparent, and risk-aware manner in order to generate returns to pay benefits. It's a very simple and relatively concise mission, and that's quite intentional. Our vision continues to focus on being repeatable, predictable, and scalable in our portfolios and in our operating practices.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

On slide 3 we have a visual showing the five strategic objectives that have been part of INVO's mission for some time, actually even prior to the 2020 Vision. Those are in the big blue bubbles. And those line up, interestingly enough, with the CalPERS Strategic Plan, which the Board recently approved. You can see a "reduce cost and complexity," "Fund sustainability," and "risk management"; that there's very direct alignment between those objectives and the five strategic objectives within our 2020 Vision.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

So we're about 60 percent of the way through this in terms of time. And we thought it would be appropriate to sort of do a bit of a mid-cycle review of the five-year

2020 Vision.

So this sort of shows what we have been calling our complexity ledger. And what you can see there is we've made good progress on the front -- in terms of reducing complexity; for example, eliminating the ARS strategies back in September of 2014. In total, we've actually reduced the number of managers over this time period from about 315 to 147. So more than 50 percent, and very significant progress in that regard, and really focused the portfolio around the most successful managers.

And the middle are a variety of projects which are really work in progress. And actually when we submitted this, the PEARS system was still work in progress. But I'm pleased to report that it is now complete and fully embedded in our private equity operations.

We've also made changes to the benchmarks. We've implemented our execution services and strategy group, which is really combining our trading functions across assets.

Our very important ESG strategic plan development which the Board's quite familiar with, that continues, and you'll be getting quite a fulsome update on that in March.

And then you heard earlier today from our Investment Manager Engagement Program.

And so those are areas that are sort of -- they're -- in terms of complexity, they're sort of a push. They're changes. They probably don't reduce complexity a lot, but we think that they probably help streamline the portfolio operations and investment management.

On the right side are some new strategies. So they've potentially added some complexity to the office. So, as I said, it's a bit of a balance.

We've decided that some of these were really important for us to do; for example, the overlay management, the CalPERS short-term investment fund, and some modifications we made to our MAC Program.

All of those were potential additions to complexity. We now have processes in place to examine the impact on the performance to make sure that that complexity is compensated. We believe it is. But we have robust processes now that help us ensure that that's the case when they've elapsed over an appropriate time period.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Slide 5 is sort of stairstep slide. And actually we've been presenting this since the beginning of the 2020 Vision. We came up with it initially and -- when we first started. And we were strangely prescient in our predictions of what we were going to undertake at each year. We've actually stuck remarkably close to the plan, including, you'll notice, in 2016 and '17 winning the CalPERS softball championship.

(Laughter.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

So that was quite an important element of the Strategic Plan.

(Laughter.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Well, this year we still have work to do.

(Laughter.)

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

As we move further into 2017 and 2018, one of the things we continue to really reinforce - and you see it highlighted in bold there, it was something we really focused on for the last 18 months or so - is establishing a more formal trust-level investment decision-making process within the Investment Office, with the idea that we wanted a process that would really sustain itself through personnel turnover. For a large institution like this, it's important that there remain disciplines and durability in the way we actually make investment decisions within the office so it's not dependent on any one person, including the CIO or COIO.

We think that there needs to be process in place that really captures all of the intelligence in the office, so that to help manage large swings in the decision-making process. And I'm pleased to say that we've been able to accomplish that. And it -- I hope it's a legacy that I'll be able to leave here as a robust internal committee investment strategy group and subcommittee structure.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

There was a few organizational realignments we completed within the last year. We've created a new Global Government and Economics group and a new MID position for that. Really, that's recognizing the fact that global economics is really a truly important element in managing a $340 billion portfolio. And that's information that we need -- we feel we need direct access really at the CIO and Total Fund level. So we've essentially elevated that function. And you've heard for some time period from John Rothfield, our chief economist, we're really expanding the role of that economics team within the management of the Total Fund.

We've centralized the Private Asset Analytics program - and you may have heard me mention this earlier in the fall - really to create a degree of independence between the folks analyzing the performance and performance attribution around the private assets and the investment decision-making functions. I think that independence is really important. And I like to say it's independent yet integrated, so that essentially the referees are not necessarily also the folks on the field. I think some degree of independence there is really important for a robust decision-making process.

And we've realigned the Sustainable Investments program, including adding a new MID position that we're currently recruiting for. And you also saw another change in our Sustainable Investments program where we moved Carrie and her group into that program to really consolidate our diversity inclusion and labor engagement activities.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

For the Roadmap, we have a total of 30 roadmap initiatives, which sounds like a lot, and it is a lot. But we have a fairly large team of people working on that. And we still have a fair amount of work to do, and you'll -- I'll help illustrate in a slide or two why that is.

Some of the key initiatives we're working on is the TOM, the Target Operating Model, refresh. And you'll see a draft of that refreshed slide.

And Investment Data Strategy. And this is one I'm really excited about. And I'm sure Matt, who's helping to lead that, will -- can provide some additional information on it. But it's really to position CalPERS to really leverage the huge asset that we have in the vast amount of investment data that is resonate within our systems. That is a -- it's an asset that we currently leverage. But we're convinced that new technologies as they're developed are going to be able to leverage that data even more. And so we want to make sure we're well positioned for that.

And then of course the Board is quite familiar with our efforts around our Private Markets Business Model Design.

We're also working on the Risk Function Business Design. We have a team in my Investment Risk and Performance group who's looked at the risk -- investment risk functions across a variety of our global peers, and is working to restructure the risk function so that it can really keep in tune with best practices across the industry.

And last, but certainly not least, is our work in the Sustainable Investments Research and our ESG Strategic Plan, including just very recently -- I'm sure you've seen the activity on all of our six ESG strategic planning workstreams. As I mentioned, you'll be getting a full update on all of those in March. But just this last week, you may have seen the news -- and this is one of the initiatives there is around climate. And we made good progress this week with the Global Climate 100+ Initiative in Paris.

So excited to see that work continue just very recently.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

This is the new Target Operating Model. And I'll flip ahead quickly to the appendix so you can remember the old one. It's a slide that this Investment Committee should be quite familiar with.

And there was a couple of challenges that we were beginning to observe. First off, we've made tremendous progress on reducing the level of risk. Our Operating Committee within the Investment Office has a pretty disciplined process for assessing the risk of this in conjunction with our ICOR team, who analyzes the risk of all those boxes. And there used to be a lot more reds and yellows. So I'm pleased to see that we've been making good progress.

But one of the challenges is, it's quite complex. You'll see that there's actually a total of 48 boxes.

The second just quite practical challenge is, it's very difficult to absorb or even read any of that text on the screen. And so we worked with Cutter, which is a consulting firm that works in the investment management and operations space. They were involved in the original development of the Target Operating Model to simplify it. And you can see we've simplified it. We've basically cut the number of functions outlined in the Target Operating Model from 48 to 24.

We've also reduced the functional swim lanes, we call them, from 6 to 5.

You can see the four that are at the top of the Target Operating Model are industry standard. This is -- this is Cutter's industry standard investment operating framework. So we're using the same operating framework that any other asset owner or actually asset manager might employ, the same basic functional boxes.

There's an advantage to that, in that it allows us to assess our functions versus an industry peer group; and Cutter has helped us do that. Now that we've adopted the maintenance and the management from the consultant within our own teams, we still can leverage Cutter, the independent consultant, to provide peer feedback on where we stand. And that feedback is incorporated into these risk assessments.

There's a unique element to the -- to our new Target Operating Model, and that's the engagement function. We believe, and CalPERS has asserted, that we have one of the most robust and largest teams deployed around engagement. And I've used the word "robust" twice now, so I know that I owe Marcie four times. So they're keeping track, as I think -- there's a fee that one must pay when you use that particular word at CalPERS amongst the executive team.

So I'm sure someone's keeping track of the fee that I owe.

But we've also done an assessment of where we stand on the engagement side, with Cutter's help. Although I must confess, looking for a peer group that really we can stack up directly with, particularly in the U.S., is a challenging thing. We have a large and powerful team across both our asset classes and within Anne Simpson's Sustainable Investment Group focused on that.

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CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

So next steps around the Roadmap and the Target Operating Model. We're going to continue to use the refined and simplified TOM that you just saw to manage the risks -- the remaining risks that we have. We're going to complete the 30 Roadmap initiatives and the 20 smaller program level initiatives that we've targeted for this year. Those are built in to our senior level team as well as our staff's investment performance appraisals this year. So how we do on completing those things is factored into everyone's compensation.

And you'll continue to get reporting on this. However, this might be the last time you get it at Investment Committee, because we're working carefully with the enterprise to build our reporting around the Target Operating Model into the Strategic Planning Updates that you receive in Finance -- in the Finance Committee. And so you'll continue to see this information but you might perhaps see it within a different Committee.

So with that, I'll pause and see if there's any questions on this.

CHAIRPERSON JONES: Thank you, Wylie.

Ms. Taylor.

COMMITTEE MEMBER TAYLOR: Yes, thank you.

Thanks, Wylie. This was a great report.

And I just had one quick question. I have to put my glasses on so I can see.

When the -- I really appreciate the smaller Roadmap/Redefined TOM Dashboard on page 9 of the 13.

What -- the only question I have - and they are the same as they were -- the three things in red, they're the same as they were on the other one. Could you explain those for us, just -- the one that really kind of made me go "What?" - and I thought -- I think last year I was thinking I just didn't -- I just don't understand - was the data management. Why is that a risk -- high risk right now?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

It's a high risk because we -- and I'll ask Matt to chime in, who's leading that initiative. Basically we have counted on some of our vendors, primarily State Street Bank, to really help own and manage our data management strategy. As the custodian, they have -- they have, I would say, the bulk of the raw investment data that we create, compile, and use. But there is a significant chunk of investment data that we develop internally, and our tools to retain, organize, catalogue, and then leverage that internally-created investment data are not where they need to be.

And so Matt and a team of people from throughout the office, and including our manager, Bertrand Mouton, who comes to us actually from BlackRock and joined us last year, and has experience in this area, they're working to develop a strategy to capture not just the data that's owned and maintained by the custodian but also all the internally developed investment research and other types of data.

We create vast amounts of information internally within the Investment Office. A good example is some of the information related to the RCP, for example. A lot of that is retained right now in a variety of different areas and shared drives and spreadsheets, and unstructured data within SharePoint. And we really want to have a tool that allows us to leverage and find patterns in all of that information, because we're convinced that eventually that can result in investment -- better investment decision making.

So, Matt, I don't know if there was anything you wanted to add to my answer.

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: Good afternoon. Matt Flynn, CalPERS team member.

I guess the only two things I would maybe reframe on top of what Wylie said is, the intent of this strategy is -- as Wylie suggested, is to extend the data across all of the asset types and what is this metadata. So data that doesn't necessarily live in the State Street system, in order to expose that information set to our team members to make informed -- better-informed investment decisions.

And then the other sort of architectural shift that we're hoping to make is a shift from a system-centric architecture where a BlackRock or a risk platform or something else all has its own vertically integrated data to a system that is again very horizontal. That we have basically a data-centric view of our world, and we can literally just plug and play systems in and out of that data lake, if you want to look at it that way, without regard to worrying about the actual care and feeding of the individual applications.

So it's a relatively significant shift in both philosophical and organizational structure. But it's all really done with the goal of making informed -- better-informed investment decisions.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

It's also a tremendous amount of work, which is why we have this box red.

COMMITTEE MEMBER TAYLOR: So, and that -- and you're talking about also including that horizontal data link, as you called it.

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: Yes, yes.

COMMITTEE MEMBER TAYLOR: Everybody that we have that -- like BlackRock, et cetera --

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION

CHIEF FLYNN: Correct.

COMMITTEE MEMBER TAYLOR: -- so that we have access to all -- or not "we," but your Investment Office has access.

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: Correct. Currently you were to access most of the fixed income information, for example, through the BlackRock Aladdin platform. Our future state would have all of the fixed income data alongside the Global Equity data, alongside the Real Estate data, so on and so forth, in a single platform that individual tools could just consume without having --

COMMITTEE MEMBER TAYLOR: How's that going?

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: -- to go point to point.

COMMITTEE MEMBER TAYLOR: I know that takes a lot of work. How's that going?

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: This is the first year. Our goal is -- by the end of the fiscal year is to bring forward a little bit more clarity on our design as well as the hypothetical architecture that we think we need to build as well as some ideas on what might end up being organizational changes in order to effect the ultimate outcome.

COMMITTEE MEMBER TAYLOR: All right. Thank you very much.

CHAIRPERSON JONES: Okay. Ms. Mathur.

COMMITTEE MEMBER MATHUR: Well, I want to take this opportunity to thank you, Wylie. Because I -- you have really undertaken with this TOM, the Target Operating Model, such a significant body, an important body of work. And the progress that you and your -- I know you haven't done it alone. You've had a team. But your vision to accomplish this has really been tremendous. And I think it's the sort of back office that is often unseen. It's not -- you know, it's really exciting to make trades and things like that. But this is so essential to the effective and efficient management of these assets. And without this, and without continual sort of improvement of these processes and data management an all of that, we wouldn't be able to I think continue to improve, and particularly with so many assets that we manage, as you well know.

So we are really going to miss you here. I think you've been a tremendous addition on our team and a tremendous leader in the Investment Office. And thank you very much for spending almost four years with us.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Well, thank you very much.

CHAIRPERSON JONES: Okay. Ms. Yee.

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman.

Let me also add my deepest thanks to Wylie as well; not just for the vision, but this just really took a lot of work. And to stay focused on the goal and to now really begin to have some comfort around the operations in the Investment Office, you know, truly being streamlined, and where hopefully things aren't going to fall through the cracks because there's just so many things that we're trying to stay on top of.

I had a couple questions. And one is, on slide 4 - and maybe it's just the way it's described - but the implementation of systems, it includes the PEARS system. I thought that was completed.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: It is. It is complete.

COMMITTEE MEMBER YEE: And so tell me what's -- oh, so is this -- this is just kind of a looking back?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE: Um-hmm.

COMMITTEE MEMBER YEE: Okay. Got it.

So this is a time orientation. Okay.

And I had the same reaction to the ESG Strategic Plan Development. But that's -- oh, okay.

Thank you.

CHAIRPERSON JONES: Mr. Slaton.

VICE CHAIRPERSON SLATON: Thank you, Mr. Chair.

When you first told me -- when I first heard that you were departing, I'm reminded of the movie Shane with Alan Ladd, where Joey says, "Shane, come back, come back."

(Laughter.)

VICE CHAIRPERSON SLATON: But you have -- you've worked hard, and all of you have worked hard to make sure that you're backstopped and that the work continues unabated, even though you're departing.

My question is the one I always ask when it comes to the red box of data management. So by when does it become yellow or green?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

That's a great question, Mr. Slaton. I would say that the timeline around the risk management and fund structure and business model, I think there's a reasonable chance that those could move -- that the top two red boxes could move to yellow at some point in the next year. The -- I would say that the -- we have decent sort of vision of what we should -- we need to undertake around both of those.

And the Fund Structure and Business Model actually could be much quicker than that.

The data management, the timeline is less clear, to be frank. I think after Matt and his team complete the roadmap initiative, which they're targeting June. So that's probably a good question to frankly keep open and ask again in May when Matt is at Finance bringing the TOM at its current state, because at that point we may have a better sense of timeline.

The one caveat is, having been involved in several organizations now that have undertaken data management initiatives, they have a remarkable history of going off the rails and taking forever. And I see you nodding, so you may have some similar experience.

And so what we're really trying to do is be concise in our initial goals and our initial objectives to be limited in scope - we're definitely not trying to sort of boil the ocean, so to speak - and really be targeted on trying to make achievable, low-hanging fruit types of changes that allow us to leverage the data we have without really trying to completely re-architect everything is the way to frame it. So I'll have to leave that one with my acting COIO to answer.

VICE CHAIRPERSON SLATON: Okay. Well, I agree with you. And, Matt, you have work ahead of you obviously. But, you know, in high experience, if you don't have a target that you're shooting for, then it makes it very difficult to get there.

So whether the target gets hit or not, whether you make it, that's a secondary issue. But in my way of thinking, it's important to have a target.

Then my last comment, Wylie, to you is that I'm -- you know, this is all about process over personalities - and we talked about that on break - that, you know, having a process in place that survives regardless of the people that happen to be holding the position creates the strength of the organization. So I thank you for your work and you've accomplished a lot in your short time here.

Thank you.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Well, thank you.

CHAIRPERSON JONES: Okay. Thanks again. And seeing no further questions, we are now going to go back to the top of the agenda. We had two items that were pulled.

But before I go back to those two items, first, Ted, I skipped over your report after -- so I don't know if you had anything else to add.

CHIEF INVESTMENT OFFICER ELIOPOULOS: I've managed to weave all my talking points into the answers that were brought out -- of the questions so far.

CHAIRPERSON JONES: I picked up some of them. Sorry about that.

CHIEF INVESTMENT OFFICER ELIOPOULOS: So I'm glad to defer that.

CHAIRPERSON JONES: Okay. Good.

And also I just want to also acknowledge we have a visitor from CalSTRS. The CIO, Chris Ailman, is visiting us today.

Okay. Now we go back to 4f and 4g that was pulled. Ms. Yee had some questions on those two items.

Ms. Yee, have you put your mike -- okay.

CHAIRPERSON JONES: Ms. Yee.

COMMITTEE MEMBER YEE: Thank you very much, Mr. Chairman.

I asked that Item 4f be pulled off consent. And I thought that with the ongoing discussions that we're having about the Private Equity model, I was concerned about -- not concerned -- I guess really wanted to have a little bit of an update with respect to the implementation of AB 2833, and whether -- I know the staff report notes some ambiguities with the bill and some efforts to try to clarify it. And -- but I also wanted to just get a sense of whether you've noted any impacts from the GPs after the bill passed and, you know, just a little bit more texture with respect to what's happened since the bill and whether there will be a need for follow-up legislation.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Yes. Thank you, Ms. Yee.

And thank you as well to this Committee for all of the guidance and experience over the last four years. I'm very pleased and honored to have served those who serve California for the last four years. It's been a true honor.

Thank you.

So now, 2833. It was enacted last year really and applies to all new partnership agreements and new capital commitments under existing partnership agreements made on or after January 1st, 2017. I just thought I would highlight that this is really a law that kicks in really for new commitments.

For any commitment made prior to 2017 we're required to make reasonable efforts. And I think what you'll see in the report is we actually accomplished quite a lot. We reported on almost all of the partnerships we had really. And our partners were actually significantly involved and very helpful frankly in helping us pull together a lot of this information.

This is our inaugural report. We're striving for consistency across asset classes; clarity in terms of the character of the various cash flows involved; and, above all, transparency. So when in doubt, CalPERS took the approach of putting information in the report. We actually added some columns to the report that were not specifically required in the law, because we felt that they were helpful. So we hope that we've erred essentially on the side of disclosure here.

For example, we've elected to include real assets. We know that there are several pension plans in the State who are also subject to this law that did not include real assets.

The law, the scope of what constitutes an alternative investment vehicle, or AIV, isn't completely clear. And so that was subject to some interpretation, and so we interpreted it to include it, but others -- it's a reasonable debate to have.

We also included, for example, some of the funds that our total plan portfolio management team has invested in, such as the MAC Program, because they're structured using partnership legal structures.

And so we believe that they could be interpreted as following under the scope of AIVs, so we went ahead and included them.

That gives you a flavor of our approach to AB 2833, where we really strove to -- when in doubt, we included something.

I'm quite confident, and I hope that one of the things that has continued to be clear is that CalPERS really I think is a leader in the space of fee and carry disclosure. And hopefully this report will reinforce that.

We're just now -- every other plan is now going through the process of reporting this date before the end of the calendar year. And so we're just now getting a sense of what the other plans are doing. And so what we expect to do is when we have all of those other plans - we have been in dialogue with several of them, including the UC Regents and STRS - is to get the folks responsible for doing this reporting across many of the plans in California to try to come up with some more standardization, because we know this year there's going to be quite a variety of different approaches throughout the state.

And we expect to make iterative refinements to both our report and, quite possibly, we might come back to this Committee with suggestions on refining and clarifying the way the law is crafted and the language in there so it's just more clear for future generations of pension investment folks and reporting folks.

So with that, I'll turn it over to Kit, if you have anything to add. Kit has been helping to lead our efforts across the asset classes. Sarah Corr, Paul Mouchakkaa, Jane Delfendahl from the Real Assets team have also been very deeply involved in helping us pull together this first report.

And we're happy to take questions on it.

CHAIRPERSON JONES: Yes, Ms. Yee.

Do you have any further questions --

COMMITTEE MEMBER YEE: I don't have any further questions really.

CHAIRPERSON JONES: -- on that item?

COMMITTEE MEMBER YEE: I appreciate that.

CHAIRPERSON JONES: Okay. We have Mr. Saha.

And we have one question here, J.J.

ACTING COMMITTEE MEMBER SAHA: Thank you, Chairman.

Our office actually was the impetus behind the report, as we were sponsors of AB 2833. And this was the first legislative-required report generated in response to this legislation. So I'd like to thank staff for all the hard work in providing information requested by the legislation.

We feel the information appears to be responsive to the Legislature and goes a long way to provide transparency into the fees and expenses that CalPERS and alternative investment vehicles and portfolio companies pay to GPs. We previously had a few questions for staff as well as a suggestion on the presentation and report, and that were answered earlier in the week, so we're pretty satisfied.

Also with regard to the additional maybe time to comment with regard to staff bringing it back to the Committee, we welcome that too.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you.

CHAIRPERSON JONES: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: I want to thank you for this. It's a lot easier to read than the iPad.

Can you explain to me what columns 10, 14, 15 and 17 are and what the differences, if any, may be.

INVESTMENT DIRECTOR CROCKER: Column 10 is the information that Private Equity has been providing pursuant to .26, the PRA statute. And it is the same as column 14, which is the information requested under AB 2833, clause A2.

And column 17 is being provided as an -- out of an excess of caution, in case -- this was one point where we weren't entirely sure of the legislative intent. We had differing interpretations based upon who you talked to here among staff. So we just decided to include both.

Column 17 would be that subset of fees and expenses paid to the GP and related parties that was made with capital contributions that were made in the form of being netted out against distributions. So it is a subset of 14. It is not in addition to 14.

COMMITTEE MEMBER JELINCIC: Okay. So 10 and 14 are every dollar that the GP took out of our pocket either directly or indirectly?

INVESTMENT DIRECTOR CROCKER: Yes, and also other expenses at the partnership level that maybe didn't go to the GP. So...

COMMITTEE MEMBER JELINCIC: Okay. And then 17, can you walk me through that again. And I will --

INVESTMENT DIRECTOR CROCKER: So there was some thought among some of our staff that people who had been in contact with the authors of the legislation that there was a desire to separate out capital contributions that were made by netting against a distribution. So, say, there was a distribution -- a partnership distribution that was payable and then a contemporaneous capital call. Instead of money going, you know, both directions, you would net out the amount of the capital call against the distribution. And then you would report our pro rata share of that that went to the GP and related parties for fees and expenses.

So on the off chance that that was of interest, of regulatory interest under the statute, we included that in column 17.

COMMITTEE MEMBER JELINCIC: Okay. Using the -- on the first page of this, California Asia Investors, LP. And I pick on them just because they're at the bottom and it's easy to see.

Why does column 14 and 17 wind up being the same if one is the fees and expenses and one is capital calls netted against distributions?

INTERIM MANAGING INVESTMENT DIRECTOR CORR: Sarah Corr, Investment staff.

As Kit mentioned earlier, column 17 is a subset of column 14. So to the extent that all of the expenses and fees that were paid during the year were netted out of a distribution, then the amounts would be the same.

COMMITTEE MEMBER JELINCIC: Okay. So this is fees paid out of the -- fees paid out -- or netted against distributions?

INTERIM MANAGING INVESTMENT DIRECTOR CORR:

Correct.

COMMITTEE MEMBER JELINCIC: Rather than capital calls netted against --

INTERIM MANAGING INVESTMENT DIRECTOR CORR:

Capital obligations that were funded through them being netted out of the distribution.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

I think the -- if I might add. Essentially there's -- the two options for paying fees and expenses were for us to cut a check directly as the result of a capital call that they make -- that the partnership makes; or for that partnership to net that out of a distribution that we would otherwise get.

So you can think of it, rather than just cutting a check, they took it out of the check that we then received and netted it against that.

So that's all that 17 is saying. It's frankly kind of a mechanical. But we suspect that it may not be important in the tone of the law whether we cut a check or whether they took it from a distribution. But just in case that is important to the reader, we included that in column 17.

COMMITTEE MEMBER JELINCIC: Okay. So that maybe I'm not understanding the heading. It's really fees netted against distributions.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Well, not necessarily. If -- and I'll let Kit elaborate. But we actually never technically pay a fee. The partnership pays the fee. The only thing we really do is either contribute capital to a partnership or get capital back.

Now, what the partners do with that capital, they may use it -- that partnership may use it to pay the general partner fees. They may use it to make investments. They may use it for a variety of different things.

But the legal character of anything we do is just capital call or capital distribution back to us, because us, we're a limited partner.

Now, again the partnership pays the fee. And so we've captured that. We've looked through that partnership and tried to characterize properly the nature of what those amounts are. But the legal structure is just capital call or distribution.

COMMITTEE MEMBER JELINCIC: Okay. So this -- I'm not getting it.

It is the fees that they re -- they reduce the distribution by the amount of the fees that they collect and whatever. And that's what's showing up in 17?

INVESTMENT DIRECTOR CROCKER: Yeah. And I think -- Kit Crocker, CalPERS staff.

I think one reason this is confusing is that it is not in fact significant at all. I mean, whether you have a separate -- wire a separate -- do a separate wire transfer or net it out against a roughly simultaneous partnership distribution, it's still a capital contribution. So it's all the same cash flow, it's all the same, you know, legally. It represents the exact same thing.

COMMITTEE MEMBER JELINCIC: So the fees are a capital contribution?

INVESTMENT DIRECTOR CROCKER: We make -- as LPs we make capital contributions to the partnership. The partnership then uses that money to in part pay fees and in part pay expenses. And not all of that goes to the GP or related parties.

COMMITTEE MEMBER JELINCIC: Okay. I --

INVESTMENT DIRECTOR CROCKER: Oh, and of course they also use it to buy investments, right? Some of if goes -- most of it goes into the ground hopefully.

COMMITTEE MEMBER JELINCIC: We hope so.

Or we really don't have much confidence in what they claim is the values of the fund if it's not going there.

Okay. I think I understand it. Thank you.

CHAIRPERSON JONES: Okay. Thank you.

Then we move to 4g.

Ms. Yee, You had a question on that one?

COMMITTEE MEMBER YEE: Thank you, Mr. Chairman. I did. And this is probably in anticipation of a future discussion, but -- because of the sensitivity of divestments generally when we have discussions about them. And I wanted to see about teeing up some potential questions to come back.

Now, given the situation particularly in Iran where there are probably more companies with business ties to Iran now than we've seen perhaps in the past. My questions really have to do with -- I think this matter's probably coming back next fall to us -- but just questions about what the process would be for ending the Iran Divestment Act and the timing of how long that would be accomplished. And then obviously we're going to see perhaps some -- some signals from this administration that might obviously affect what we do or what may affect Iran.

And then, secondly, if CalPERS has the ability to remain invested in some of the companies that are doing business -- that have business ties with Iran if we determine that it would not meet our fiduciary duty to invest.

So I mean, just kind of setting the stage for that discussion. I mean, they seem like pretty common-sense questions, but I just didn't want that to go unnoticed.

Thank you.

CHAIRPERSON JONES: Okay. Thank you.

Okay. Great.

Okay. So that moves us to Summary of Committee Directions.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you, Mr. Chair.

I only have two items. The first was to discuss a particular emerging manager issue in closed session.

I think that was the first thing.

And then the second thing was to work with our Public Affairs group to essentially get the word out around the RCP and the good work that we're doing with the Responsible Contracting Policy. Those are the two that I captured.

CHIEF INVESTMENT OFFICER ELIOPOULOS: And the Emerging Manager Program.

CHAIRPERSON JONES: Yes. Okay.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Thank you.

CHAIRPERSON JONES: You referred to the Emerging Manager to the Legislature. But then also we wanted to have a follow-up discussion, if necessary, on the Annual Diversity Program. So if you come back, if there's no issues, then we have it, then we don't have to have a discussion on it. But if there some issues or any impediments of doing it, then we need to have a discussion. Okay?

Okay. Thank you.

J.J.

COMMITTEE MEMBER JELINCIC: Yeah, one other thing that ought to be included is - last month we gave some direction to produce certain information, which I have not seen. And so maybe we ought to restate that go back and produce the information that you were told to produce last month.

CHAIRPERSON JONES: Okay. Which particular information are you referring to, J.J.?

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

There was --

COMMITTEE MEMBER JELINCIC: It was in the minutes.

CHIEF OPERATING INVESTMENT OFFICER TOLLETTE:

Yeah, it's in the minutes. And we actually have -- we have folders on our desks waiting for that with draft versions of that data. So I can assure you that we actually haven't forgotten about those. They're definitely work in process right now.

CHAIRPERSON JONES: Okay. Thank you.

Okay.

COMMITTEE MEMBER JELINCIC: I hope it gets released before I get off the Board.

(Laughter.)

CHAIRPERSON JONES: That's Wednesday, J.J.

COMMITTEE MEMBER JELINCIC: January 14th.

CHAIRPERSON JONES: That's right. Right, right, right.

Okay. Anyway, thank you again.

So that concludes the open session of the Investment Committee.

We will take a -- I guess we got five minutes and -- is that five minutes we go into closed session?

So how long is the closed session?

Okay. Well, then we better break for lunch then.

(Laughter.)

CHAIRPERSON JONES: Okay. We will reconvene at 1:15 for closed session Investment Committee.

(Thereupon California Public Employees' Retirement System, Investment Committee meeting open session adjourned at 12:34 p.m.)

C E R T I F I C A T E OF R E P O R T E R

I, JAMES F. PETERS, a Certified Shorthand Reporter of the State of California, do hereby certify:

That I am a disinterested person herein; that the foregoing California Public Employees' Retirement System, Board of Administration, Investment Committee open session meeting was reported in shorthand by me, James F. Peters, a Certified Shorthand Reporter of the State of California, and was thereafter transcribed, under my direction, by computer-assisted transcription;

I further certify that I am not of counsel or attorney for any of the parties to said meeting nor in any way interested in the outcome of said meeting.

IN WITNESS WHEREOF, I have hereunto set my hand this 25th day of December, 2017.

JAMES F. PETERS, CSR
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