

# California Public Employees' Retirement System

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## Fiscal Year 2019-20 Annual Budget Proposal

First Reading  
April 16, 2019



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## Executive Summary and Highlights

CalPERS' proposed budget represents the financial resources needed to achieve strategic priorities and initiatives, meet core business needs, and further the mission of delivering retirement and health care benefits to members and their beneficiaries. The budget supports CalPERS' five strategic goals:

- Fund Sustainability
- Health Care Affordability
- Reduce Complexity
- Risk Management
- Talent Management

The total 2019-20 proposed budget is \$1.898 billion; an increase of \$199.4 million, or 11.7 percent, over the 2018-19 authorized budget. Total authorized positions remain unchanged at 2,875.

### 2019-20 Total Budget

(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Administrative Operating Costs	\$ 444,065	\$ 498,107	\$ 530,299	\$ 32,192	6.5%
Investment Operating Costs	68,425	93,421	120,436	27,015	28.9%
Investment External Management Fees	727,208	767,009	899,791	132,782	17.3%
Third Party Administrator Fees	288,652	305,612	319,273	13,660	4.5%
<b>Total: Operating Costs</b>	<b>\$ 1,528,350</b>	<b>\$ 1,664,149</b>	<b>\$ 1,869,798</b>	<b>\$ 205,650</b>	<b>12.4%</b>
Enterprise Project Costs	22,366	9,591	3,352	(6,240)	(65.1%)
Headquarters Building Costs	23,603	24,372	24,374	1	0.0%
<b>CalPERS Total Budget</b>	<b>\$ 1,574,319</b>	<b>\$ 1,698,112</b>	<b>\$ 1,897,524</b>	<b>\$ 199,411</b>	<b>11.7%</b>
<b>Authorized Positions</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>-</b>	<b>0.0%</b>

Following are the major highlights of the 2019-20 proposed budget:

- Administrative Operating Costs include \$6.3 million to conform with the Board's February 2019 action to increase Investment Office salaries in alignment with the strategic goal of Talent Management and promoting a high-performing workforce.
- Administrative Operating Costs include \$19.7 million to fund compensation increases negotiated through the State's collective bargaining process.
- All permanent positions funded in the temporary help blanket are eliminated.

- Investment Operating Costs include \$16 million to implement new trading platforms, and \$4.9 million for Data and Analytics software subscriptions to improve Fund Sustainability.
- Investment External Management Fees increased \$132.8 million as compared to 2018-19 and reflects asset allocation strategies and asset class market assumptions to improve Fund Sustainability.
- In accordance with Senate Bill (SB) 1413, Chapter 665, Statutes of 2018, CalPERS will implement the California Employers Pension Prefunding Trust (CEPPT) program to provide an investment strategy to assist local governments plan for and fund their pension obligations.
- Enterprise Project Costs include \$3.4 million for three projects to improve Fund Sustainability and Reduce Complexity within the organization. The projects will complete the final phase of the Actuarial Valuation System Redesign and Enhancement Project, continue development of the new Human Resources Management Solution, and implement a new online Member Electronic Payment System.

### 2018-19 Current-Year Update

CalPERS' 2018-19 total authorized budget is \$1.698 billion. Of this amount, \$750.4 million, or 44.2 percent, was expended as of December 31, 2018. Based on an analysis of resource utilization, CalPERS forecasts that it will end the 2018-19 fiscal year with approximately \$26.8 million in unexpended funds, which equals 1.6 percent of the total budget.

(in thousands)	2018-19 Authorized Budget	2018-19 Expenditures and Encumbrances thru 12-31-18	Percent Expended	Forecast	Savings
Administrative Operating Costs	\$498,107	\$243,815	48.9%	\$476,691	\$21,415
Investment Operating Costs	93,421	28,788	30.8%	93,421	-
Investment External Mgmt Fees	767,009	323,289	42.1%	767,009	-
Third Party Administrator Fees	305,612	143,168	46.8%	300,575	5,037
<b>Total Operating Costs</b>	<b>\$1,664,149</b>	<b>\$739,060</b>	<b>44.4%</b>	<b>\$1,637,696</b>	<b>\$26,453</b>
Enterprise Projects Costs	9,591	2,671	27.9%	9,265	327
Headquarters Building Costs	24,372	8,663	35.5%	24,372	-
<b>CalPERS Total Budget</b>	<b>\$1,698,112</b>	<b>\$750,395</b>	<b>44.2%</b>	<b>\$1,671,333</b>	<b>\$26,779</b>

The expenditure categories tracking well below 50 percent at mid-year include:

- **Investment Operating Costs** – These expenses historically track at less than 50 percent due to a lag in vendor invoicing.
- **Investment External Management Fees** – These expenses historically track at less than 50 percent due to the timing of fee payments and market fluctuations.
- **Enterprise Project Costs** – At mid-year, contract negotiations for the Contact Center Cloud Migration and Human Resources Management System projects were delayed and funds had not been encumbered. The contract for the Contact Center Cloud Migration was subsequently executed in January 2019, and CalPERS expects to execute the contract for the Human Resources Management System by the end of the fiscal year.
- **Headquarters Building Costs** – Headquarters Building expenditures that were below 50 percent at mid-year were largely due to improvement projects that were in progress or yet to begin. For example, the project to convert HVAC controls began in October 2018 with an estimated completion date in June 2019. Similarly, the flooring project to accommodate the Call Center's return from West Sacramento to Lincoln Plaza's East building started in late November 2018, with an April 2019 completion date. Finally, the project to bring Lincoln Plaza North Building's emergency lighting and notification systems up to current fire code is still in the design phase. The completion date for this project is dependent on the State Fire Marshal's approval of design documents.

Of the \$26.8 million forecasted savings, \$21.4 million is in Administrative Operating Costs and is largely driven by \$15.0 million in vacancy-related salary savings. There is also \$5 million in savings in Operating Expense and Equipment (OE&E) categories, including general office expenses, data processing, and consultant services.

In addition to projected savings in Administrative Operating Costs, CalPERS estimates \$5.0 million in Third Party Administrator Fee savings resulting from actual enrollment data that identifies fewer enrollments in higher fee health plans than originally estimated.

### CalPERS Budget Process

For each fiscal year, CalPERS engages in two formal budget processes - an annual budget process and a mid-year review. The annual budget process is designed to develop the twelve-month budget for Board approval prior to the start of a new fiscal year on July 1<sup>st</sup>. In contrast, the mid-year budget review is to address new, critical, unforeseen, and emergency resource needs not included in the annual budget.

The annual budget development process includes a review of existing budgeted resources as well as new funding requests to maintain, improve, or implement services, initiatives, and projects. Financial Office budget staff work collaboratively with each division to understand their organizational structures and business objectives as a basis for maintaining existing funding levels and approving requests for new resources.

CalPERS utilizes a formal budget request process to consider, prioritize, and approve new resource requests. Pursuant to the CalPERS Budget Policy, the main criteria used to prioritize requests include:

- Mitigating risk
- Identifying opportunities for cost efficiencies
- Aligning with the Strategic Plan and Business Plan
- Implementing CalPERS Board of Administration decisions and directives
- Complying with legal mandates

Divisional senior management and executive leadership review and discuss all formal budget requests before final funding decisions are made.

Development of the annual budget also includes a position pooling process that redirects vacancies to where they are most critically needed within the organization. The objective of this process is to limit unnecessary staffing and related budgetary increases, and to provide new staff resources to divisions with the highest needs.

## 2019-20 Proposed Budget

CalPERS' total 2019-20 proposed budget is \$1.898 billion; an increase of \$199.4 million, or 11.7 percent, over the 2018-19 authorized budget.

2019-20 Total Budget					
(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Administrative Operating Costs	\$ 444,065	\$ 498,107	\$ 530,299	\$ 32,192	6.5%
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Third Party Administrator Fees	288,652	305,612	319,273	13,660	4.5%
<b>Total: Operating Costs</b>	<b>\$ 1,528,350</b>	<b>\$ 1,664,149</b>	<b>\$ 1,869,798</b>	<b>\$ 205,650</b>	<b>12.4%</b>
Enterprise Project Costs	22,366	9,591	3,352	(6,240)	(65.1%)
Headquarters Building Costs	23,603	24,372	24,374	1	0.0%
<b>CalPERS Total Budget</b>	<b>\$ 1,574,319</b>	<b>\$ 1,698,112</b>	<b>\$ 1,897,524</b>	<b>\$ 199,411</b>	<b>11.7%</b>
<b>Authorized Positions</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>-</b>	<b>0.0%</b>

As reflected below, the 2019-20 proposed budget reflects a \$266.6 million increase in expenditures over the past five years.

Total Budget 2015-16 through 2019-20						
(in thousands)	2015-16 Actual	2016-17 Actual	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	Five-Year Change
Administrative Operating Costs	\$421,534	\$437,809	\$444,065	\$498,107	\$ 530,299	\$108,765
Investment Operating Costs	72,601	69,486	68,425	93,421	120,436	47,835
Investment External Management Fees	794,486	613,509	727,208	767,009	899,791	105,305
Third Party Administrator Fees	282,584	286,401	288,652	305,612	319,273	36,689
<b>Total: Operating Costs</b>	<b>\$1,571,204</b>	<b>\$1,407,206</b>	<b>\$1,528,350</b>	<b>\$1,664,149</b>	<b>\$1,869,798</b>	<b>\$298,594</b>
Enterprise Projects Costs	32,074	34,088	22,366	9,591	3,352	(28,723)
Headquarters Building Costs	27,682	26,230	23,603	24,372	24,374	(3,308)
<b>CalPERS Total Budget</b>	<b>\$ 1,630,961</b>	<b>\$ 1,467,524</b>	<b>\$ 1,574,319</b>	<b>\$ 1,698,112</b>	<b>\$ 1,897,524</b>	<b>\$ 266,563</b>
<b>Authorized Positions</b>	<b>2,765.0</b>	<b>2,880.0</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>110.00</b>

The major factors driving cost increases over the past five years include:

- Collectively bargained employee compensation increases added \$53.6 million to Administrative Operating Costs.
- Investment-related technology expenses for data and analytical tools and new portfolio management platforms increased Investment Operating Costs by \$32.3 million, and increased use of investment-related consultants for real estate and sustainable investment activities contributed an additional \$5.2 million.
- Improved market performance increased the amount of Investment and External Management fees paid by \$105 million. More specifically, assets in the Public Employees Retirement Fund (PERF) grew \$56 billion between June 30, 2016, and June 30, 2018.
- Expanded health plan options, increased enrollments, and new Third Party Administrator contracts added \$36.7 million in Third Party Administrator Fees.

Over this same timeframe, CalPERS actively engaged in efforts to streamline internal operations and achieve savings. As a result, CalPERS:

- Eliminated 98 permanent blanket positions by transitioning team members into authorized position vacancies.
- Reduced temporary help expenditures by \$8.6 million.
- Reduced Headquarters (HQ) Building expenses by \$3.3 million.

The following pages detail the 2019-20 proposed budget by expenditure category.

## I. Administrative Operating Costs

Administrative Operating Costs include personal services expenditures (i.e. salaries, wages, and benefits for permanent and temporary help staff) and other Operating Equipment and Expenses (OE&E) for each branch within CalPERS. Administrative Operating Costs in 2019-20 are proposed at \$530.3 million. This is an increase of \$32.2 million, or 6.5 percent, as compared to the 2018-19 authorized budget.

Administrative Operating Costs by Object of Expenditure

(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
<b>[1] PERSONAL SERVICES</b>					
Salaries & Wages	\$ 224,827	\$ 254,581	\$ 264,944	\$ 10,363	4.1%
Temporary Help	7,183	7,315	5,138	(2,177)	(29.8%)
Overtime	1,827	2,100	2,048	(51)	(2.4%)
Benefits	109,566	137,502	143,520	6,017	4.4%
<b>Total Personal Services</b>	<b>\$ 343,402</b>	<b>\$ 401,498</b>	<b>\$ 415,650</b>	<b>\$ 14,152</b>	<b>3.5%</b>
Vacancy Savings		(18,738)		18,738	(100.0%)
<b>Revised Total Personal Services</b>	<b>\$ 343,402</b>	<b>\$ 382,759</b>	<b>\$ 415,650</b>	<b>\$ 32,891</b>	<b>8.6%</b>
<b>[2] OPERATING EXPENSES &amp; EQUIPMENT</b>					
General Expense	\$ 7,110	\$ 9,552	\$ 11,358	\$ 1,806	18.9%
Software	1,263	2,205	1,842	(363)	(16.5%)
Printing	2,085	1,963	1,990	27	1.4%
Postage	3,899	3,336	2,843	(493)	(14.8%)
Communications	1,255	1,816	1,845	29	1.6%
Data Processing Services	15,599	15,802	15,362	(440)	(2.8%)
Travel	2,311	3,257	3,580	323	9.9%
Training	1,044	1,730	1,732	2	0.1%
Medical Exam/Disability Travel	1,208	1,916	1,451	(466)	(24.3%)
Facilities Operations	5,724	5,464	5,390	(74)	(1.4%)
Central Administrative Services	24,411	26,195	25,567	(628)	(2.4%)
University Enterprises, Inc.	149	415	521	106	25.6%
External Legal Counsel	3,246	6,007	5,877	(130)	(2.2%)
Professional Services	5,336	5,993	6,075	82	1.4%
Consultants	18,524	21,946	20,025	(1,921)	(8.8%)
Audit Services	1,152	695	1,969	1,274	183.3%
Federal Legislative Rep	870	600	600		0.0%
Admin Hearings	1,391	1,300	1,418	118	9.1%
Consolidated Data Centers	87	90	105	15	16.7%
Equipment (Includes EDP)	4,000	5,064	5,098	34	0.7%
<b>Total Operating Expenses &amp; Equipment</b>	<b>\$ 100,663</b>	<b>\$ 115,348</b>	<b>\$ 114,649</b>	<b>\$ (699)</b>	<b>(0.6%)</b>
<b>Total Costs</b>	<b>\$ 444,065</b>	<b>\$ 498,107</b>	<b>\$ 530,299</b>	<b>\$ 32,192</b>	<b>6.5%</b>

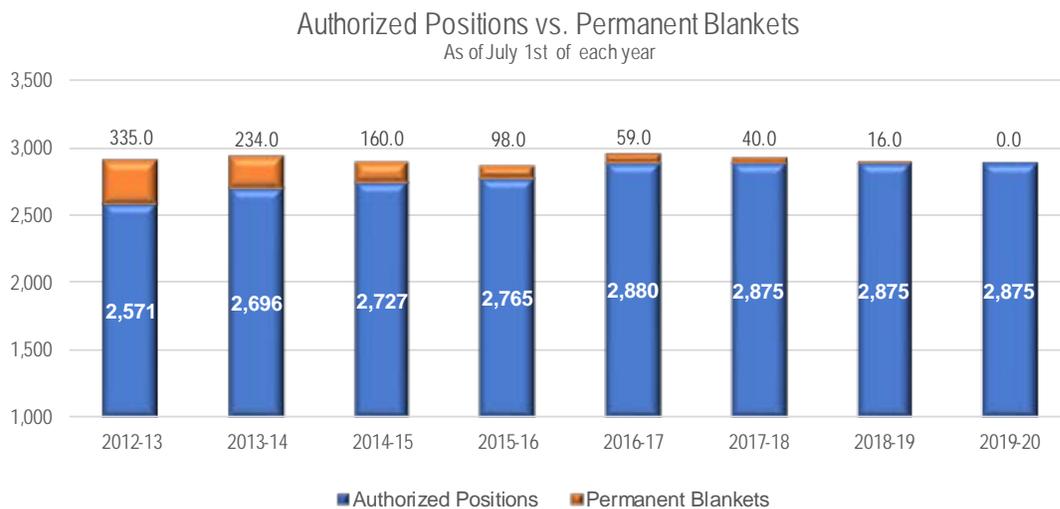
The net increase in Administrative Operating Costs reflects a \$32.9 million increase in Personal Services expenditures, slightly offset by a net \$0.7 million decrease in OE&E. The Personal Services increase includes \$19.7 million in estimated general salary and benefit increases negotiated through the State's collective bargaining processes, and \$6.3 million resulting from the Board's February 2019 approval of salary increases for specific Investment Officer, Manager, and Director classifications.

The net decrease in OE&E includes an increase in General Expenses of \$1.8 million driven by a \$0.7 million increase in legal expenses and a \$1.0 million increase for fiduciary insurance coverage. CalPERS is evaluating the purchase of commercial fiduciary insurance for the Public Employees' Retirement Fund (PERF) and related retirement fund operations. This insurance would eventually replace the existing fiduciary liability self-insurance program if the commercial policy is determined to be in the best interests of CalPERS. At present, the proposed commercial fiduciary insurance policy contemplates \$100 million of coverage with an annual premium of approximately \$1 million. CalPERS will separately review the current commercial fiduciary insurance policy for its health related funds and operations in the near future. These General Expense increases are offset by reductions in various other OE&E categories, the largest of which is a \$1.9 million decrease in consultant expenditures. Of this decrease, \$1.2 million reflects reduced consultant expenditures for the my|CalPERS system.

Please refer to Appendix I for Administrative Operating Costs by branch.

### Authorized Positions

CalPERS' proposed budget holds the authorized position count at 2,875 and does not include any funding for permanent positions in the blanket. At its peak in 2012-13, there were 335 positions in the temporary help blanket that were for permanent, ongoing workload. Before the start of the 2019-20 fiscal year, CalPERS will transition the remainder of these blanket positions into vacant authorized positions. The following chart provides data on total authorized and permanent blanket positions over the past eight years.



In its continuing effort to achieve efficiencies and cost savings, CalPERS implemented a position pooling process that coincides with developing the annual budget. Through this process, CalPERS redirects vacancies to where they are most critically needed in the organization. The following chart displays year-over-year position changes among CalPERS' branches, and identifies the pooled positions available for redirection during the budget year.

### Authorized Positions by Branch

Branch	2018-19	2019-20	Change
Actuarial Office	58.0	62.0	4.0
Communications & Stakeholder Relations	79.0	80.0	1.0
Customer Services and Support	866.5	868.5	2.0
Enterprise Compliance	26.0	24.0	(2.0)
Executive Office	16.0	18.0	2.0
Financial Office	217.0	204.0	(13.0)
General Counsel	141.0	141.0	0.0
Health Policy and Benefits	211.0	210.0	(1.0)
Investment Office	350.0	344.0	(6.0)
Operations and Technology	910.5	911.0	0.5
Position Pool	0.0	12.5	12.5
<b>Total Authorized Positions</b>	<b>2,875.0</b>	<b>2,875.0</b>	<b>0.0</b>

### Social Security Administration

Since 1955, CalPERS has served as the designated State Social Security Administrator for California. In short, this entails overseeing contracts and reporting between the Federal Social Security Administration and approximately 2,300 state and local government employers. The Administrative Operating Costs budget includes personal services and OE&E for CalPERS to perform this work, and historically, residual interest earned on Social Security taxes deposited in the Old Age and Survivors' Insurance (OASI) Trust Fund covered the expenditures. In 2019-20 however, there will be insufficient funding in the OASI Trust Fund to fund costs incurred. As a result, pursuant to Government Code Section 22551, CalPERS will begin charging an administrative fee to public employers that provide social security coverage to their employees. CalPERS is currently seeking Department of Finance approval of the fee structure, and will work with employer groups to notify them of this new fee.

## II. Investment Operating Costs

Investment Operating Costs include specific expenditures incurred for investment activities, such as consultants to inform the Board of investment initiatives or to support the implementation of investment technologies and platforms; external audit, legal, and appraisal services related to asset valuations; fund administration and custody; data and analytics software; and maintaining or implementing trading and portfolio management systems. Investment Operating Costs in 2019-20 are proposed at \$120.4 million. This is an increase of \$27 million, or 28.9 percent, as compared to the 2018-19 authorized budget.

Investment Operating Costs					
(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Investment Consultants	\$3,301	\$9,300	\$9,860	\$560	6.0%
Board Consultants	4,817	4,633	5,221	588	12.7%
Technology Consultants	3,750	5,567	7,600	2,033	36.5%
<b>Total Consultant Expenses</b>	<b>\$11,868</b>	<b>\$19,501</b>	<b>\$22,681</b>	<b>\$3,180</b>	<b>16.3%</b>
Audits	\$65	\$705	\$705	-	0.0%
Tax Advisory Services	1,001	1,200	1,200	-	0.0%
Master Custodian Fee	4,951	7,657	11,453	3,796	49.6%
Fund Administration Services / Fees	2,680	2,898	3,900	1,002	34.6%
External Legal	2,516	5,800	5,800	-	0.0%
Appraisal Fees	5,759	10,000	10,000	-	0.0%
Company Expense	854	890	950	60	6.7%
Miscellaneous Operating Expense	2,309	300	300	-	0.0%
<b>Total Operating Expenses</b>	<b>\$20,135</b>	<b>\$29,450</b>	<b>\$34,308</b>	<b>\$4,858</b>	<b>16.5%</b>
Data	\$4,678	\$6,600	\$7,500	\$900	13.6%
Analytics	9,251	11,000	15,000	4,000	36.4%
Trading and Portfolio Management Systems	20,637	24,692	38,769	14,077	57.0%
Business Operations Tool	1,849	2,000	2,000	-	0.0%
Other Technology Expense	8	178	178	-	0.0%
<b>Total Technology Expenses</b>	<b>\$36,422</b>	<b>\$44,470</b>	<b>\$63,447</b>	<b>\$18,977</b>	<b>42.7%</b>
<b>Total Investment Operating Expenses</b>	<b>\$68,425</b>	<b>\$93,421</b>	<b>\$120,436</b>	<b>\$27,015</b>	<b>28.9%</b>

Major Investment Operating Cost increases include:

- \$1.1 million in Investment and Board Consultants related to contract fee increases and Global Fixed Income and Sustainable Investment strategies.
- \$2.0 million for Technology Consultants to assist with the implementation of new platform solutions to improve fund sustainability.
- \$3.8 million increase in Master Custodian Fees resulting from a higher fee structure for the new five-year contract beginning in 2018-19. The \$7.6 million budgeted in 2018-19 did not reflect the new contract terms and is approximately \$3.0 million lower than actual costs. Savings in other Investment Operating Expenses categories will cover this shortfall.
- \$4.9 million increase in Data and Analytics subscription costs due to increased usage to internalize more investment functions related to the Total Fund strategy and provide enhanced analysis and reporting.
- \$14.1 million increase to implement new portfolio management systems and platforms to provide better access to and utilization of data, and to monitor risk and performance across the Total Fund. The platforms include new multi-asset order management and trading, data strategy, active risk management, and liability modeling.

### III. Investment External Management Fees

Investment External Management Fees represent amounts that CalPERS pays to external investment advisors with whom it contracts to manage specific portfolios. The Board approves Investment Advisor Contract extensions on an annual basis, and the contracts typically range from seven to twelve years. Details on investment fees paid are included in the Comprehensive Annual Financial Report (CAFR).

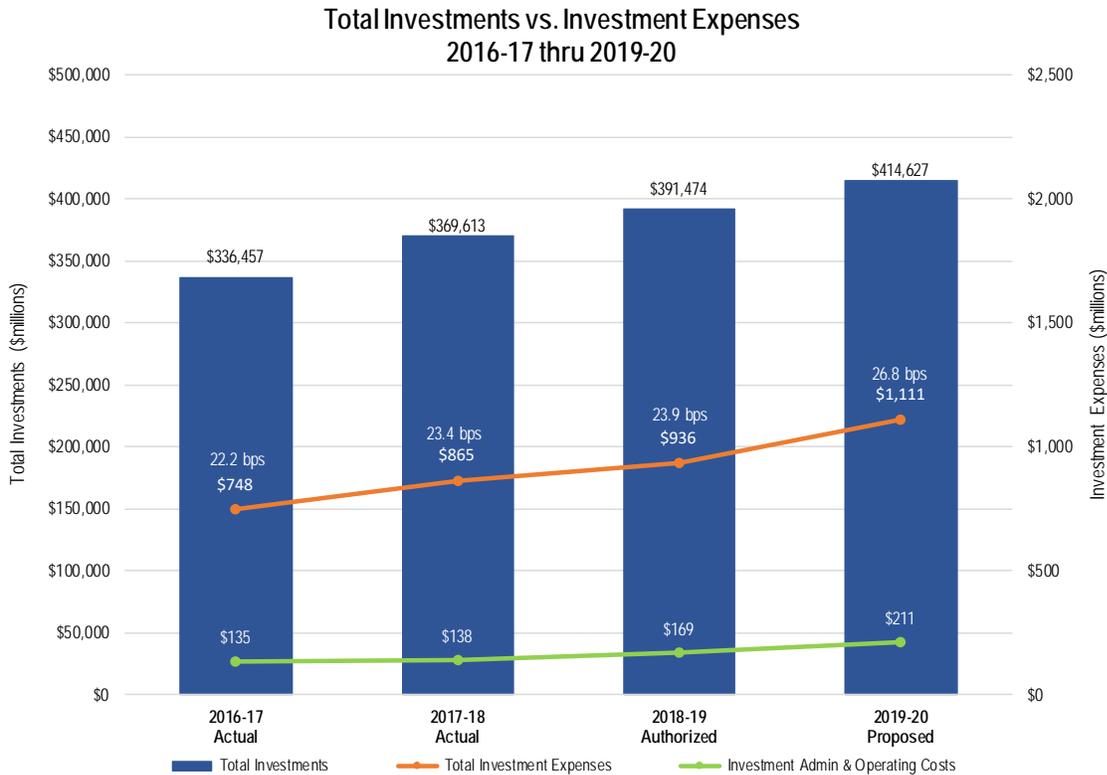
CalPERS estimates annual Investment External Management Fees based on market assumptions and investment diversification strategies. Total Fees in 2019-20 are estimated at \$899.8 million. This is an increase of \$132.8 million, or 17.3 percent, as compared to the 2018-19 authorized budget. The drivers of this increase are in Private Equity base fees for the Pillars I and II asset allocation plans, and in Real Assets performance fees resulting from a strong market.

Investment External Management Fees					
(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Global Equity	\$86,508	\$93,000	\$126,719	\$33,719	36.3%
Fixed Income	7,890	10,003	13,793	3,790	37.9%
Real Assets	191,815	185,201	188,213	3,013	1.6%
Absolute Return Strategy	487	332	305	(27)	(8.1%)
Private Equity	247,678	258,000	295,000	37,000	14.3%
Activist Funds	6,594	-	-	-	-
Multi Asset Class	20,487	30,900	40,800	9,900	32.0%
Opportunistic Strategies	-	-	1,500	1,500	100%
<b>External Mgmt - Base Fees</b>	<b>\$561,460</b>	<b>\$577,436</b>	<b>\$666,331</b>	<b>\$88,895</b>	<b>15.4%</b>
Global Equity	\$26,750	\$84,896	\$52,224	(\$32,671)	(38.5%)
Fixed Income	3,366	2,908	3,214	306	10.5%
Real Assets	123,998	100,969	176,021	75,052	74.3%
Absolute Return Strategy	1,647	800	-	(800)	(100.0%)
Multi Asset Class	9,987	-	2,000	2,000	100%
<b>External Mgmt - Performance Fees</b>	<b>\$165,748</b>	<b>\$189,573</b>	<b>\$233,460</b>	<b>\$43,887</b>	<b>23.2%</b>
<b>Total External Mgmt Fees</b>	<b>\$727,208</b>	<b>\$767,009</b>	<b>\$899,791</b>	<b>\$132,782</b>	<b>17.3%</b>

#### Basis Points Trend

To evaluate the relation of investment-related expenditures to the total investments, CalPERS calculates expense ratios using basis points. The estimated expense ratio for the 2019-20 Proposed Budget is

26.8 basis points. As detailed in the next chart, the ratio is increasing as compared to prior years. While Administration and Investment Operating Costs are relatively flat, estimated increases in External Management Fees are driving the ratio higher.



Note: The bps calculation reflects Total Investment Expenses in relation to Total Investments.  
Total Investment Expenses includes Investment External Management fees and Investment Admin & Operating Costs.

## IV. Third Party Administrator Fees

CalPERS contracts with Third Party Administrators to support the delivery of health and pension services with a focus on strengthening and improving long-term sustainability for its members. The Board approves the Third Party contracts with terms that typically extend five years and include annual fee increases. Third Party Administrator Fee expenses cover administration, recordkeeping, and participant communication services for the following programs:

- CalPERS Health Benefits Program
- Long-Term Care Program
- Supplemental Income Plan Program
- California Employers' Retiree Benefit Trust Fund Program (CERBT)
- California Employers' Pension Prefunding Trust Program (CEPPT)

Total Third Party Administrator Fees estimated in 2019-20 are \$319.3 million. This is an increase of \$13.7 million, or 4.5 percent, as compared to the 2018-19 authorized budget. The estimate is based on enrollment projections, including enrollments by plan type, and is typically revised during the mid-year budget process after the Board approves new health plan rates.

Third Party Administrator Fees

(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Health Program	\$ 244,082	\$ 259,495	\$ 272,613	\$ 13,118	5.1%
Pharmacy Benefit Manager	19,677	21,682	22,451	769	3.5%
<b>Total, Health</b>	<b>\$ 263,759</b>	<b>\$ 281,178</b>	<b>\$ 295,064</b>	<b>\$ 13,887</b>	<b>4.9%</b>
Long Term Care Program	21,221	20,732	20,151	(581)	(2.8%)
Supplemental Income Plan	3,565	3,585	3,922	337	9.4%
California Employers' Retiree Benefit Trust (CERBT)	107	118	115	(3)	(2.5%)
California Employers' Pension Prefunding Trust (CEPPT)	-	-	20	20	-
<b>Total Third Party Administrator Fees</b>	<b>\$288,652</b>	<b>\$305,612</b>	<b>\$319,273</b>	<b>\$13,660</b>	<b>4.5%</b>

The year-over-year increase in Third Party Administrator Fees reflects annual fee increases included in the executed contracts. The California Employers Pension Prefunding Trust (CEPPT) program is a new program authorized by Senate Bill (SB) 1413, Chapter 665, Statutes of 2018. Expenditures for the CEPPT program in 2019-20 are funded by a General Fund appropriation authorized by SB 1413.

**V. Enterprise Project Costs**

Each year, CalPERS undertakes information technology projects to improve operations, enhance services to members, and stay current with industry trends and practices. The 2019-20 proposed budget includes \$3.4 million for two ongoing and one new project.

Enterprise Project Costs			
(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget
my CalPERS Business Optimization	\$8,774	-	-
Business Intelligence	581	-	-
Data Backup, Restoration, and Disaster Recovery	6,959	-	-
Long Term Care Third Party Administrator	858	-	-
Business Continuity	248	-	-
CalPERS Education Center Replacement	1,314	-	-
Actuarial Valuation System Redesign / AAI	3,631	5,108	2,942
Information Security Technology Solutions	-	576	-
Contact Center Applications - Migration to Cloud	-	517	-
Human Resources Management Solution (HRMS)	-	3,390	236
Member Electronic Payment System	-	-	174
<b>Total Enterprise Projects</b>	<b>\$22,366</b>	<b>\$9,591</b>	<b>\$3,352</b>

Actuarial Valuation System Redesign/Advanced Analytics Integration: \$2.9 million

Funding in 2019-20 is to complete the final phase of enhancements to CalPERS' new actuarial valuation system. Began in 2014-15, this project replaced core valuation functionality to enhance and increase valuation activities to more accurately model liabilities and calculate funded status. While the new system launched in October 2018, additional enhancements are required to improve cash flow projections, complete generational mortality rates, comply with new GASB reporting requirements, and provide better data analytics and document and workflow management capabilities. Beginning in 2020-21, CalPERS estimates \$0.8 million annually in ongoing operations and maintenance costs for the redesigned valuation system.

Human Resources Management Solution: \$0.2 million

Funding in 2019-20 is for limited-term staffing resources to support existing staff who will be redirected to work on the continuing, four-year project to develop a new, cloud-based human resources system. CalPERS estimates that these funds will be needed for two years, plus an additional \$0.5 million in fiscal years 2020-21 and 2021-22 for increased vendor support for configuration testing and training and development.

### Member Electronic Payment System: \$0.2 million

The 2019-20 proposed budget includes funds to develop and implement a new electronic payment system to enable members and beneficiaries to make credit or debit card payments online.

Implementation of an online payment system will result in improved collections and a reduction in staff resources to manually process the 34,000 paper checks received each year. CalPERS estimates that the new system will be functional by March 2020. Ongoing annual maintenance and operations expenditures are negligible.

## VI. Headquarters Building Costs

The HQ Building Budget reflects expenses incurred to operate, maintain, and improve the Lincoln Plaza Buildings. The budget also includes other expenses such as security and maintenance for regional offices, the offsite emergency operations center, the Front Street parking lot, and warehouse space. Also displayed are offsetting rent revenues earned. Total proposed HQ Building expenses in 2019-20 are \$25.8 million. This is an increase of \$0.3 million, or 1.2 percent, as compared to 2018-19.

2019-20 Headquarters Building Account Budget

(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase/(Decrease)	% Increase/(Decrease)
<b>Operating:</b>					
Utilities	\$2,390	\$2,291	\$2,365	\$74	3.2%
Engineering Services	2,922	3,372	4,038	666	19.8%
Janitorial	3,144	3,288	3,439	151	4.6%
Landscaping	796	855	865	10	1.1%
General Maintenance	1,234	1,447	1,215	(232)	(16.1%)
Security	2,399	2,598	2,911	313	12.1%
Property Mgmt. & Administrative Fees	1,308	1,509	1,512	3	0.2%
Café Plaza	306	176	247	71	40.2%
Offsite Expenses <sup>1</sup>	634	642	961	320	49.8%
Emergency Operations Center (EOC) <sup>2</sup>	722	455	451	(4)	(0.8%)
Operating Other <sup>3</sup>	1,946	1,860	2,022	162	8.7%
<b>Total Operating Expenses</b>	<b>17,800</b>	<b>18,493</b>	<b>20,026</b>	<b>1,533</b>	<b>8.3%</b>
<b>Non-Operating:</b>					
Owner Improvements <sup>4</sup>	2,776	3,919	3,187	(732)	(18.7%)
Building Improvements <sup>5</sup>	4,261	3,338	3,614	276	8.3%
Furniture & Fixtures	1,810	563	300	(263)	(46.7%)
Building Insurance	4	610	360	(250)	(41.0%)
<b>Total Non-Operating Expenses</b>	<b>8,851</b>	<b>8,429</b>	<b>7,461</b>	<b>(968)</b>	<b>(11.5%)</b>
<b>Subtotal Expenses</b>	<b>\$26,650</b>	<b>\$26,923</b>	<b>\$27,487</b>	<b>\$565</b>	<b>2.1%</b>
Less: Revenue <sup>6</sup>	1,636	1,404	1,655	250	17.8%
<b>Total HQ Building Expenses</b>	<b>\$25,015</b>	<b>\$25,519</b>	<b>\$25,833</b>	<b>\$314</b>	<b>1.2%</b>
Less: Amount included in Admin. Budget	1,411	1,146	1,459	313	27.3%
<b>Total Headquarters Building Budget</b>	<b>\$23,603</b>	<b>\$24,372</b>	<b>\$24,374</b>	<b>\$1</b>	<b>0.0%</b>

<sup>1</sup> Offsite expenses include Front Street parking, warehouse space, and regional office security and maintenance. In 2019-20, CalPERS shifted \$0.2 million in regional office security expenses from General Maintenance to Offsite Expenses to more accurately categorize these costs.

<sup>2</sup> EOC expenses include leasing costs, utilities, janitorial, security, landscaping, and generator maintenance.

<sup>3</sup> Other Operating expenses includes specialized maintenance, permitting, and testing of building electrical and HVAC systems, and green building initiatives.

<sup>4</sup> Owner Improvements include enhancements made to support operations and the movement of divisions, units, and/or staff within CalPERS. In 2019-20, CalPERS shifted \$0.5 million in engineering salaries from this line item to Engineering Services to more accurately categorize these costs.

<sup>5</sup> Building Improvements include structural alterations and repairs and related project management.

<sup>6</sup> Estimated revenue from parking and the Subway, Chocolate Fish, and Montessori daycare leases.

Of the \$25.8 million total costs, \$1.5 million is budgeted as Facilities Operations expenses within the Administrative Operating Costs budget and represents the affiliate funds' share of building expenses.

The net \$0.3 million year-over-year increase is due to the following:

- \$1.5 million increase in Operating Expenses driven by contract wages for engineering, janitorial, and security staff, and for specialized maintenance of electrical and HVAC systems, including green building initiatives. The increase also reflects a shift in engineering staff salaries from Non-Operating Expenses to Operating Expenses to more accurately and consistently categorize the expenses.
- \$1.0 million decrease in non-operating expenses resulting from the removal of one-time expenses to relocate the Call Center from West Sacramento to Lincoln Plaza, and the shift of engineering staff salaries to Operating Expenses.
- \$0.3 million increase in estimated rent revenue that offsets expenditures.

The proposed HQ Building Budget includes \$3.4 million for building improvement projects in 2019-20, the largest of which is \$2.1 million for water intrusion repairs. Also included are fire and life safety upgrades and other minor building alterations.

## I. Administrative Operating Costs by Branch

Following is the allocation of proposed Administrative Operating Costs by Branch. As discussed in Section D.1, salary increases are the primary drivers of the year-over-year changes.

Administrative Budget by Branch

(in thousands)	2017-18 Actual	2018-19 Authorized Budget	2019-20 Proposed Budget	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Actuarial Office	\$ 9,987	\$ 11,353	\$ 12,465	\$ 1,111	9.8%
Communications and Stakeholder Relations	14,885	15,489	17,046	1,557	10.1%
Customer Services and Support	92,797	104,023	107,245	3,222	3.1%
Enterprise Compliance Office	2,794	3,191	3,359	168	5.3%
Executive Office	6,849	6,570	7,719	1,149	17.5%
Financial Office <sup>1</sup>	24,411	31,863	37,251	5,387	16.9%
General Counsel	24,518	28,552	31,627	3,075	10.8%
Health Policy and Benefits Branch	27,194	32,398	33,908	1,510	4.7%
Investment Office	69,812	75,422	91,026	15,605	20.7%
Operations and Technology	146,407	163,051	163,086	35	0.0%
Pro-Rata Assessment	24,411	26,195	25,567	(628)	(2.4%)
<b>CalPERS Total Budget</b>	<b>\$ 444,065</b>	<b>\$ 498,107</b>	<b>\$ 530,299</b>	<b>\$ 32,192</b>	<b>6.5%</b>

<sup>1</sup> Includes unallocated expenses such as Executive incentive payments, a reserve for retirement payouts, and pooled positions and related funding.

## II. Administrative Operating Costs by Fund

Following is the allocation of proposed Administrative Operating Costs to each trust fund based on a combined direct and indirect methodology. In general, the year-over-year increases to the funds reflect overall salary increases as discussed in Section D.I. For some trusts, decreases for specific circumstances offset the increases. More specifically, the Health Care Fund decreases because of a reduced pro-rata assessment as well as a shift in health plan participant enrollment. In addition, the Judges and Legislators Retirement Funds have decreases due to a reduction in legal expenses.

Administrative Operating Costs by Fund

(in thousands)	Actual	2018-19 Authorized	2019-20 Proposed	2018 to 2019 Change	
				\$ Increase / (Decrease)	% Increase / (Decrease)
Public Employees' Retirement Fund (PERF)	\$ 358,893	\$ 397,317	\$ 425,603	\$ 28,286	7.1%
Public Employees' Contingency Reserve Fund (CRF) <sup>1</sup>	28,665	32,088	33,792	1,704	5.3%
Public Employees' Health Care Fund (HCF) <sup>1</sup>	39,907	47,109	46,963	(146)	(0.3%)
Long-Term Care Fund (LTCF)	5,163	6,036	7,607	1,571	26.0%
Annuitants' Health Care Coverage Fund (AHCCF)	3,434	4,808	5,493	685	14.2%
Deferred Compensation Fund (IRC 457)	1,598	1,884	1,768	(116)	(6.2%)
Supplemental Contributions Program Fund (SCP)	137	140	123	(17)	(12.1%)
Judges' Retirement Fund (JRF)	1,680	2,546	1,997	(549)	(21.6%)
Judges' Retirement Fund II (JRF II)	2,082	2,841	2,277	(564)	(19.9%)
Legislators' Retirement Fund (LRF)	556	578	509	(69)	(11.9%)
Replacement Benefit Custodial Fund (RBF)	450	450	537	87	19.3%
California Employers' Pension Prefunding Trust Fund (CEPPT)	-	-	423	423	100.0%
Old-Age & Survivors Insurance Fund (OASI)	-	-	988	988	100.0%
Reimbursements <sup>2</sup>	1,500	2,310	2,219	(91)	(3.9%)
<b>Total Administrative Operating Costs</b>	<b>\$ 444,065</b>	<b>\$ 498,107</b>	<b>\$ 530,299</b>	<b>\$ 32,192</b>	<b>6.5%</b>
<i>Statewide Pro-Rata Assessment</i>	<i>\$ 24,411</i>	<i>\$ 26,195</i>	<i>\$ 25,567</i>	<i>\$ (628)</i>	<i>(2.4%)</i>
<i>CalPERS Administrative Costs</i>	<i>\$ 419,654</i>	<i>\$ 471,912</i>	<i>\$ 504,732</i>	<i>\$ 32,820</i>	<i>7.0%</i>

<sup>1</sup> These amounts include estimates for statewide employee compensation pending Department of Finance approval.

<sup>2</sup> Reimbursements include specialized actuarial valuations prepared for public agencies, cost of photocopies/postage related to the Public Records Act requests, annual employer conferences, and administrative assessments for employers' delinquent payroll.