

California Public Employees' Retirement System

Fiscal Year 2020-21 Mid-Year Budget

November 17, 2020



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Executive Summary

This Mid-Year Budget reflects adjustments to the 2020-21 Annual Budget approved by the Board of Administration on April 22, 2020, and emphasizes reductions driven by the COVID-19 pandemic. As revenue shortfalls across the state have negatively impacted employers' financial resources and ability to make pension payments, the reductions reflect CalPERS' commitment to reducing its costs and fiscal impacts to the Public Employees' Retirement Fund (PERF).

At mid-year, CalPERS proposes a \$72.3 million net decrease to its 2020-21 Total Budget. This includes a \$68.5 million, or 9.9 percent decrease, in Operating Costs. The reduction is driven by statewide compensation reductions resulting from the COVID-19 pandemic, as well as CalPERS-directed position and administrative reductions to further lower expenditures. Through a re-evaluation of workload and focus on protecting its core mission, CalPERS proposes to permanently eliminate 32 vacant positions, reducing total authorized positions for the first time in several years. In addition, the Mid-Year Budget identifies a \$3.9 million net decrease in External Investment Management and Third Party Administrator Fees to reflect revised investment strategies and updated health plan enrollment projections.

2020-21 Mid-Year Total Budget

(\$ in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	% Change From Annual
Administrative Operating Costs	\$545,782	(\$68,701)	\$477,081	(12.6%)
Investment Operating Costs	124,856	1,574	126,430	1.2%
Enterprise Projects Costs	-	-	-	0.0%
Headquarters Building Costs	24,338	(1,335)	23,003	(5.5%)
Total: Operating Costs	\$694,976	(\$68,462)	\$626,514	(9.9%)
Investment External Management Fees	685,906	6,187	692,093	0.9%
Third Party Administrator Fees	312,670	(10,047)	302,623	(3.2%)
Total: Fees	\$998,575	(\$3,860)	\$994,716	(0.4%)
CalPERS Total Budget	\$1,693,551	(\$72,322)	\$1,621,230	(4.3%)
Total Positions	2,875.0	(32.0)	2,843.0	(1.1%)

The following pages detail the 2020-21 Mid-Year adjustments by expenditure category.

I. Administrative Operating Costs

Administrative Operating Costs include personal services expenditures (salaries, wages, and benefits for permanent and temporary staff) and Operating Expenses and Equipment (OE&E) for each branch at CalPERS.

At mid-year, CalPERS proposes a \$68.7 million, or 12.6 percent reduction, in Administrative Operating Costs. This includes a net \$52.1 million decrease in Personal Services expenses resulting from statewide compensation reductions driven by the pandemic (\$33.3 million decrease), revised general salary and benefit increases negotiated through collective bargaining (\$4.3 million decrease), and additional CalPERS-directed reductions in positions, temporary help, and overtime (\$14.5 million decrease). In total, CalPERS proposes to eliminate 32 vacant positions for an ongoing reduction of nearly \$3.8 million, and to delay recruitments for other vacancies to achieve additional one-time savings of \$9.3 million.

CalPERS also proposes to decrease OE&E by \$16.6 million, or 13.6 percent, to achieve further savings. Of this amount, \$7.0 million is ongoing, and \$9.6 million is one-time. Many reductions, such as Travel, Training, Printing, and Postage are directly driven by the pandemic. More specifically, while travel and training opportunities are currently limited and will result in reduced expenditures, printing and postage reductions reflect new ways of operating in a virtual environment. For example, in 2020-21, CalPERS will distribute the PERSpective publications electronically instead of by mail. This change alone saves approximately \$2.5 million in printing and postage costs. Similarly, as a result of the State Controller's Office (SCO) sending retiree benefit warrants electronically rather than by mail, CalPERS will save \$1.1 million in SCO charges included in the Professional Services line item. Further, virtually hosting the 2020 Educational Forum rather than in-person reduced the budget another \$0.6 million.

Other OE&E reductions reflect an emphasis on cost effectiveness and spending only what is critically necessary to meet CalPERS' core mission. This includes limiting purchases of office supplies and other items included in General Expenses, eliminating or reducing certain Data Processing services, renegotiating External Legal contract terms, and increasing reliance on internal staff to decrease Consultant expenses.

CalPERS will re-evaluate assumptions for all one-time reductions during development of the 2021-22 Annual Budget to determine the extent to which additional ongoing reductions can be achieved.

Administrative Operating Costs by Object of Expenditure

(in thousands)	2020-21 Authorized Annual Budget	2020-21 Proposed Mid-Year Budget	Change From Annual	
			\$ Increase / (Decrease)	% Increase / (Decrease)
[1] PERSONAL SERVICES				
Salaries & Wages	\$ 268,836	\$ 241,648	\$ (27,188)	(10.1%)
Temporary Help	2,485	1,452	(1,033)	(41.6%)
Overtime	1,912	1,831	(81)	(4.2%)
Benefits	150,288	126,479	(23,809)	(15.8%)
Total Personal Services	\$ 423,521	\$ 371,409	\$ (52,112)	(12.3%)
[2] OPERATING EXPENSES & EQUIPMENT				
General Expense	\$ 10,999	\$ 8,843	(2,156)	(19.6%)
Software	3,158	2,754	(404)	(12.8%)
Printing	1,736	411	(1,324)	(76.3%)
Postage	3,363	2,106	(1,258)	(37.4%)
Communications	1,763	1,641	(122)	(6.9%)
Data Processing Services	20,173	16,621	(3,553)	(17.6%)
Travel	3,618	1,526	(2,091)	(57.8%)
Training	1,673	810	(863)	(51.6%)
Medical Exam/Disability Travel	1,457	1,233	(224)	(15.3%)
Facilities Operations	4,685	4,726	41	0.9%
Central Administrative Services	25,765	25,765		0.0%
University Enterprises, Inc.	536	305	(231)	(43.1%)
External Legal Counsel	6,038	5,898	(140)	(2.3%)
Professional Services	6,141	4,810	(1,331)	(21.7%)
Consultants	20,404	17,817	(2,587)	(12.7%)
Audit Services	1,687	1,687		0.0%
Federal Legislative Rep	600	600		0.0%
Admin Hearings	1,402	1,402		0.0%
Consolidated Data Centers	250	250		0.0%
Equipment (Includes EDP)	6,812	6,466	(346)	(5.1%)
Total Operating Expenses & Equipment	\$ 122,261	\$ 105,672	\$ (16,589)	(13.6%)
Total Costs	\$ 545,782	\$ 477,081	\$ (68,701)	(12.6%)

Authorized Positions

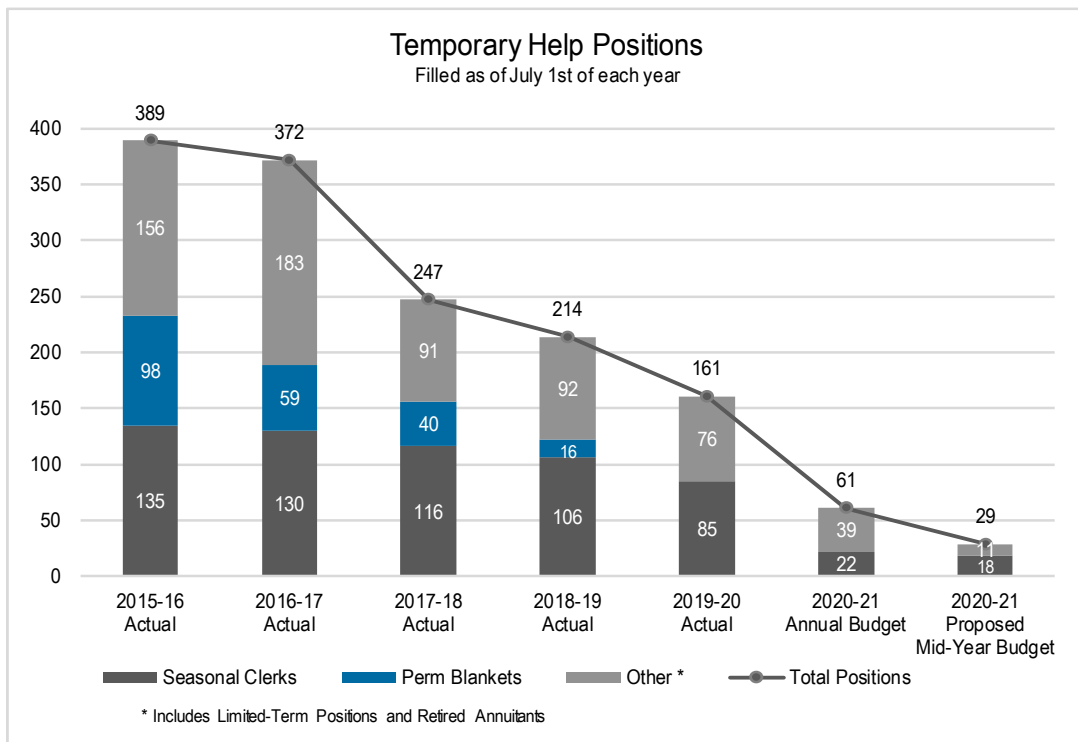
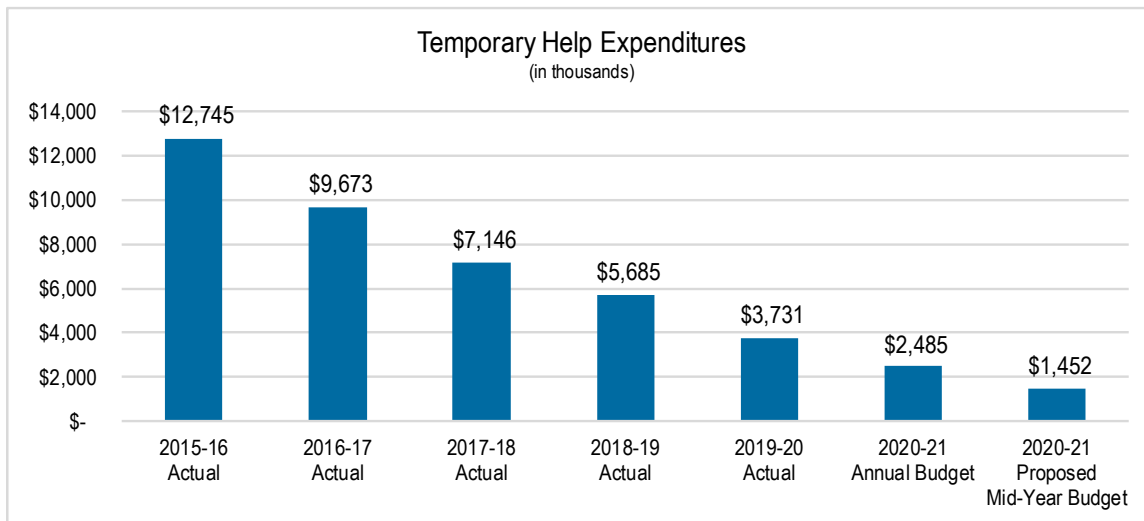
The following table displays authorized positions by branch and details the areas from which vacant positions will be eliminated. As a matter of practice, CalPERS analyzes each position that becomes vacant and considers workload needs to determine the necessity to fill. In past years, vacancies not needed for their original purpose were transferred to the position pool and kept available for redirection in the organization should other needs arise. Currently however, CalPERS proposes to eliminate 32 vacant positions to achieve ongoing savings.

Authorized Positions by Branch

Positions by Branch	2020-21 Authorized	Mid-Year Reduction	2020-21 Revised	% Change From Annual
Actuarial Office	64.0	-	64.0	0.0%
Communications and Stakeholder Relations	79.0	-	79.0	0.0%
Customer Services and Support	892.0	(5.0)	887.0	(0.6%)
Enterprise Compliance Office	24.0	-	24.0	0.0%
Executive Office	17.0	(1.0)	16.0	(5.9%)
Financial Office	199.0	(9.0)	190.0	(4.5%)
General Counsel	162.0	(1.0)	161.0	(0.6%)
Health Policy and Benefits	211.0	(5.0)	206.0	(2.4%)
Investment Office	340.0	(1.0)	339.0	(0.3%)
Operations and Technology	885.0	(10.0)	875.0	(1.1%)
Position Pool	2.0	-	2.0	0.0%
Total Authorized Positions	2,875.0	(32.0)	2,843.0	(1.1%)

Temporary Help

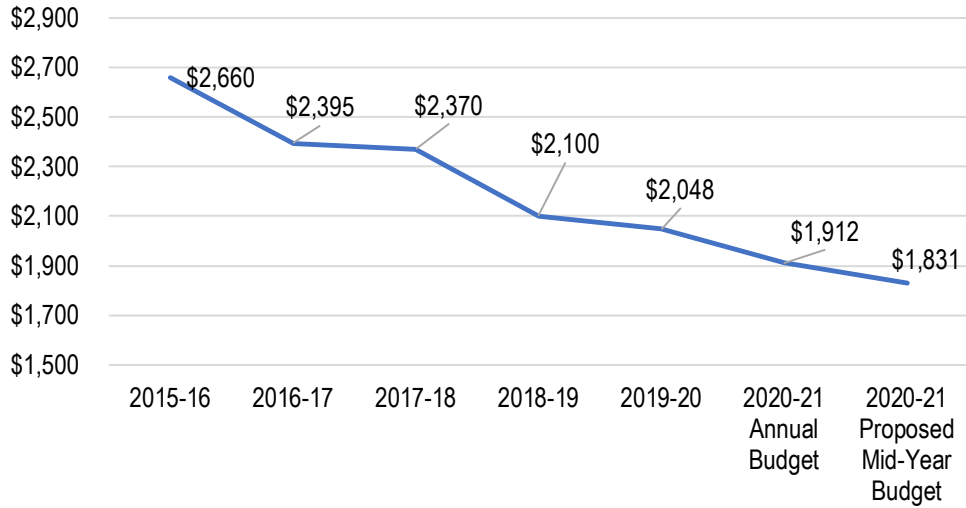
The 2020-21 Annual Budget proposed in April provided details on temporary help, which includes Seasonal Clerks, Retired Annuitants, and limited-term positions. As shown in the two tables below, CalPERS has consistently made reductions in temporary help usage over the past several years. The 2020-21 Annual Budget approved in April included nearly \$2.5 million for 61 temporary help positions. At mid-year, CalPERS proposes an additional reduction of \$1.0 million and 32 positions. CalPERS maintains its commitment to eliminating the use of seasonal clerks for non-seasonal workload by June 30, 2021.



Overtime

In addition to reductions in temporary help, CalPERS has continued to decrease overtime expenditures. The Mid-Year Budget reduces funds for overtime by an additional \$81,000.

Budgeted Overtime (in thousands)



II. Investment Operating Costs

Investment Operating Costs include expenditures incurred to support investment activities, such as consultants to inform the Board of investment initiatives or to implement 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.

At mid-year, CalPERS proposes a net increase of \$1.6 million, or 1.2 percent, in Total Investment Operating Expenses. This includes a \$0.3 million decrease in Technology Consultant expenses and a \$0.1 million decrease for Trading & Portfolio Management Systems related to delayed project implementations and consolidation of services. These decreases are offset by a \$2.0 million increase in Appraisal Fees related to renegotiated contracts and an increase in the number of anticipated limited scope appraisals that will be required.

Investment Operating Costs

(in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	% Change
Investment Consultants	\$10,000	\$ -	\$10,000	0.0%
Board Consultants	5,667	-	5,667	0.0%
Technology Consultants	8,200	(308)	7,892	(3.9%)
Total Consultant Expenses	\$23,867	(\$308)	\$23,559	(1.3%)
Audits	\$705	\$ -	\$705	0.0%
Tax Advisory Services	1,200	-	1,200	0.0%
Master Custodian Fee	11,435	-	11,435	0.0%
Fund Administration Services / Fees	3,848	-	3,848	0.0%
External Legal	5,800	-	5,800	0.0%
Appraisal Fees	8,000	2,000	10,000	20.0%
Company Expense	450	-	450	0.0%
Miscellaneous Operating Expense	300	-	300	0.0%
Total Operating Expenses	\$31,737	\$2,000	\$33,737	5.9%
Data	\$7,600	\$ -	\$7,600	0.0%
Analytics	19,581	-	19,581	0.0%
Trading and Portfolio Management Systems	38,136	(118)	38,018	(0.3%)
Business Operations Tool	3,757	-	3,757	0.0%
Other Technology Expense	178	-	178	0.0%
Total Technology Expenses	\$69,252	(\$118)	\$69,134	(0.2%)
Total Investment Operating Expenses	\$124,856	\$1,574	\$126,430	1.2%

III. Enterprise Project Costs

Enterprise Project Costs include information technology projects to improve operations, enhance services to members, and stay current with industry trends and practices.

There were no projects budgeted in 2020-21, and none proposed at mid-year.

IV. Headquarters Building Costs

Headquarters Building expenses include amounts necessary to operate, maintain, and improve the Lincoln Plaza Buildings and regional offices, as well as the emergency operations center, Front Street parking lot, and warehouse space.

At mid-year, CalPERS proposes a \$1.3 million decrease to the Headquarters Building Costs Budget. This includes a \$0.8 million decrease in Operating Costs resulting from reduced, renegotiated management fees and administration costs, a reduction in required engineering, security, and janitorial services, and lower expenses at the offsite emergency operations center. There is also a \$1.2 million decrease in Non-Operating Costs due to delaying non-critical building improvements, and reduced need for data wire, voice, and furniture installations for team member relocations. These decreases are offset by a recalculation of estimated parking revenues used to offset operating costs. More specifically, parking revenue is down given the remote work environment and closure of Lincoln Plaza to visitors.

Headquarters Building Costs

(in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	From Annual % Increase/(Decrease)
Operating:				
Utilities	\$2,403	\$ -	\$2,403	0.0%
Engineering Services	4,168	(152)	4,017	(3.6%)
Janitorial	3,657	(125)	3,533	(3.4%)
Landscaping	890	(20)	871	(2.2%)
General Maintenance	1,195	(20)	1,175	(1.7%)
Security	2,881	(159)	2,721	(5.5%)
Property Mgmt. & Administrative Fees	1,593	(175)	1,418	(11.0%)
Café Plaza	249	-	249	0.0%
Offsite Expenses ¹	867	(34)	833	(3.9%)
Emergency Operations Center (EOC) ²	509	(50)	459	(9.9%)
Operating Other ³	2,936	(28)	2,908	(1.0%)
Total Operating Expenses	\$21,350	(\$763)	\$20,587	(3.6%)
Non-Operating:				
Owner Improvements ⁴	2,363	(182)	2,181	(7.7%)
Building Improvements ⁵	2,946	(1,003)	1,944	(34.0%)
Furniture & Fixtures	289	-	289	0.0%
Building Insurance	571	-	571	0.0%
Total Non-Operating Expenses	\$6,169	(\$1,185)	4,985	(19.2%)
Subtotal Expenses	\$27,519	(\$1,947)	\$25,572	(7.1%)
Less: Revenue ⁶	(1,680)	653	(1,028)	(38.8%)
Total HQ Building Expenses	\$25,839	(\$1,295)	\$24,545	(5.0%)
Less: Amount included in Admin. Budget	(1,501)	(41)	(1,542)	2.7%
Total Headquarters Building Budget	\$24,338	(\$1,335)	\$23,003	(5.5%)

¹ Offsite expenses include Front Street parking, warehouse space, and regional office security and maintenance.

² EOC expenses include leasing costs, utilities, janitorial, security, landscaping, and generator maintenance.

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

⁴ Owner Improvements include enhancements made to support operations and the movement of divisions, units, and/or staff within CalPERS.

⁵ Building Improvements include structural alterations and repairs and related project management.

⁶ Estimated revenue from parking and the Subway and Montessori daycare leases.

V. 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. At mid-year, CalPERS proposes an increase of \$6.2 million, or 0.9 percent, driven by Opportunistic Strategies base fees. These fees are expected to increase to reflect new investment strategies designed to leverage market disruptions caused by the pandemic.

Investment External Management Fees

(in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	% Change
Global Equity	\$33,438	\$ -	\$33,438	0.0%
Fixed Income	13,439	-	13,439	0.0%
Real Assets	223,566	-	223,566	0.0%
Absolute Return Strategy	300	-	300	0.0%
Private Equity	300,000	-	300,000	0.0%
Multi Asset Class	1,500	-	1,500	0.0%
Opportunistic Strategies	5,413	6,187	11,600	53.3%
External Mgmt - Base Fees	\$577,655	\$6,187	\$583,843	1.1%
Global Equity	\$4,043	\$ -	\$4,043	0.0%
Fixed Income	2,879	-	2,879	0.0%
Real Assets	101,329	-	101,329	0.0%
External Mgmt - Performance Fees	\$108,250	\$ -	\$108,250	0.0%
Total External Mgmt Fees	\$685,906	\$6,187	\$692,093	0.9%

VI. Third Party Administrator Fees

CalPERS contracts with Third Party Administrators to support the delivery of health and pension services. The fees cover administration, recordkeeping, and communication with participants. At mid-year, CalPERS proposes a decrease of \$10.0 million, or 3.2 percent, in Third Party Administrator Fees. This includes a \$3.9 million decrease in Health Program fees based on updated enrollment projections, a \$5.2 million decrease in Pharmacy Benefit Manager fees resulting from a newly negotiated contract, and a \$0.9 million decrease for the Long Term Care Program due to continued enrollment declines.

Third Party Administrator Fees

(\$ in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	From Annual % Increase/(Decrease)
Health Program	\$ 264,996	\$ (3,912)	\$ 261,084	(1.5%)
Pharmacy Benefit Manager	23,802	(5,214)	18,588	(21.9%)
Total, Health	288,798	(9,126)	279,672	(3.2%)
Long Term Care Program	20,314	(921)	19,392	(4.5%)
Supplemental Income Plan	3,450	-	3,450	0.0%
California Employers' Retiree Benefit Trust (CERBT)	90	-	90	0.0%
California Employers' Pension Prefunding Trust (CEPPT)	18	-	18	0.0%
Total Third Party Administrator Fees	\$312,670	(\$10,047)	\$302,623	(3.2%)

I. Administrative Operating Costs by Branch

Following is the allocation of proposed Administrative Operating Costs by branch. While all branches have decreases resulting from statewide compensation reductions, the CalPERS-directed position and OE&E reductions result in varying percentage changes depending on the affected program area. For example, the reductions attributable to the electronic distribution of PERSpective publications and holding a virtual Ed Forum are seen in Communications and Stakeholder Relations.

Administrative Operating Costs by Branch

(\$ in thousands)	2020-21 Authorized Annual Budget	Mid-Year Adjustments	2020-21 Proposed Mid-Year Budget	From Annual % Increase/(Decrease)
Actuarial Office	\$ 13,488	\$ (2,197)	\$ 11,291	(16.3%)
Communications and Stakeholder Relations	17,298	(4,641)	12,657	(26.8%)
Customer Services and Support	109,248	(12,752)	96,496	(11.7%)
Enterprise Compliance Office	3,470	(837)	2,633	(24.1%)
Executive Office	8,379	(860)	7,519	(10.3%)
Financial Office	37,530	(5,499)	32,032	(14.7%)
General Counsel	39,361	(3,757)	35,605	(9.5%)
Health Policy and Benefits Branch	33,716	(5,315)	28,402	(15.8%)
Investment Office	94,972	(11,220)	83,752	(11.8%)
Operations and Technology	162,554	(21,624)	140,931	(13.3%)
Pro-Rata Assessment	25,765		25,765	0.0%
Total Administrative Operating Costs	\$ 545,782	(\$68,701)	\$ 477,081	(12.6%)

II. Administrative Operating Costs by Fund

The table below displays the allocation of proposed Administrative Operating Costs to the trust funds and state funds.

Administrative Operating Costs by Fund

(\$ in thousands)	2020-21 Authorized Annual Budget	2020-21 Proposed Mid-Year Budget	Change from Annual	
			\$ Increase / (Decrease)	% Increase / (Decrease)
Administrative Operating Costs				
Public Employees' Retirement Fund (PERF)	\$ 436,705	\$ 376,782	\$ (59,923)	(13.7%)
Public Employees' Contingency Reserve Fund (CRF)	34,199	31,630	(2,569)	(7.5%)
Public Employees' Health Care Fund (HCF)	49,193	45,497	(3,696)	(7.5%)
Long-Term Care Fund (LTCF)	8,994	7,872	(1,122)	(12.5%)
Annuitants' Health Care Coverage Fund (AHCCF)	6,341	5,758	(583)	(9.2%)
Deferred Compensation Fund (IRC 457)	1,870	1,672	(198)	(10.6%)
Supplemental Contributions Program Fund (SCP)	117	105	(12)	(10.5%)
Judges' Retirement Fund (JRF)	1,926	1,713	(213)	(11.0%)
Judges' Retirement Fund II (JRF II)	2,203	1,986	(217)	(9.9%)
Legislators' Retirement Fund (LRF)	497	438	(58)	(11.7%)
Replacement Benefit Custodial Fund (RBF)	633	625	(8)	(1.3%)
California Employers' Pension Prefunding Trust (CEPPT)	5	4	(1)	(22.0%)
Old-Age & Survivors Insurance Fund (OASI)	1,054	954	(100)	(9.5%)
Reimbursements	2,044	2,044	-	0.0%
Total Administrative Operating Costs	\$ 545,782	\$ 477,081	\$ (68,701)	(12.6%)
<i>Statewide Pro-Rata Assessment</i>	\$ 25,765	\$ 25,765	\$ -	0.0%
<i>CalPERS Administrative Costs</i>	\$ 520,016	\$ 451,316	\$ (68,701)	(13.2%)

III. 2021-22 Operating Costs Projection

As part of its budget process, CalPERS monitors the out-year impact of fiscal decisions to estimate future operating cost expenses. In response to the COVID-19 pandemic, the Mid-Year Budget includes both permanent and one-time operating cost reductions. Because there is uncertainty regarding many factors, the revised 2021-22 Operating Costs projection reflects current decisions only. For example within the Administrative Operating Costs Budget, the 2021-22 projection includes the restoration of \$19 million in one-time personal services and OE&E reductions, as well as another \$1 million for upcoming board elections. The Investment Operating Costs budget identifies a \$3.2 million increase; \$2.0 million consistent with the current year increase in appraisal fees, and another \$1.2 million for Trading and Portfolio Management Systems based on current contractual agreements. At this time there are no known Enterprise Projects, and CalPERS is holding Headquarters Building Expenses at the updated 2020-21 Mid-Year amount.

During the development of the 2021-22 Annual Budget, CalPERS will analyze all operating cost budgets and make decisions based on updated facts, assumptions, and priorities.

2021-22 Projection

(in thousands)	2020-21 Proposed Mid-Year Budget	2021-22 Projected Budget	2020 to 2021 Change	
			\$ Increase / (Decrease)	% Increase / (Decrease)
Administrative Operating Costs	\$ 477,081	\$497,537	\$20,456	4.3%
Investment Operating Costs	126,430	129,630	3,200	2.5%
Enterprise Projects Costs	-	-	-	0.0%
Headquarters Building Costs	23,003	23,003	-	0.0%
Total Projection	\$626,514	\$650,170	\$23,656	3.8%
Authorized Positions	2,839.0	2,839.0	-	0.0%