



Board of Administration

Agenda Item 10b

November 18, 2020

Item Name: Options for Retaining Fiduciary Counsel

Program: Board Governance

Item Type: Information

Executive Summary

At the Board President's request, management has identified several options for selecting and utilizing external fiduciary counsel, including the possibility of moving from a single fiduciary counsel to a pool of counsel, for the Committee's discussion and consideration.

Background

CalPERS' History of Retaining Fiduciary Counsel

The Board has reserved the power to select CalPERS' external fiduciary counsel since at least 1990. Historically, fiduciary counsel has advised the Board and management on a variety of issues involving fiduciary liability and responsibility. These issues have focused on the Board's and management's fiduciary duty to CalPERS members and issues involving the application of California Constitution article XVI, section 17 (as amended by Proposition 162) and other trust law principles to various situations. CalPERS' external fiduciary counsel responds to requests for legal opinions and advice from the Board and management, directed through CalPERS' General Counsel. CalPERS pays outside fiduciary counsel for actual work performed, in arrears.

Historically, CalPERS has retained either one or two firms as fiduciary counsel. In the last few selection cycles, the Board has selected just one firm to serve in this role. On occasion and when circumstances have required more specialized advice (such as investment-related fiduciary advice), CalPERS has retained other firms on an ad hoc basis. The Board selected CalPERS' current fiduciary counsel in March 2017.

In that last selection process, CalPERS released a solicitation in August 2016. Thirteen firms responded with proposals. In November 2016, two Board members (the then-Board President and Controller Yee's designee) met with the Legal Office team to review and evaluate the proposals. The most significant factors considered were the firm's experience and expertise in advising public pension plans on fiduciary issues; the individual credentials, experience, and expertise of the firms' proposed lead attorneys; whether the firms' proposed lead attorneys were

based in California; CalPERS' experience (if any) with the firms; and the reasonableness of the firms' proposed fees. As a result of that review, the team recommended that the full Board interview two firms, Nossaman LLP and Seyfarth Shaw LLP. After the interviews, the Board selected Nossaman. That was in March 2017. Nossaman's current contract runs through March 2022.

Reasons for Retaining External Fiduciary Counsel

When CalPERS needs specific expertise to fulfill its responsibilities, it is permitted – and sometimes required – to consult with experts in the field. Just as the Investment Committee and the Investment Office rely on outside consultants and experts, the Board and management occasionally seek expert advice from external fiduciary counsel.

Fiduciary legal representation is a specialized area of the law that can be difficult to replicate internally. Because firms that concentrate in this area represent multiple public pension plans, they can provide a broader and more diverse perspective. In addition, they provide an independent opinion on fiduciary matters that can be particularly helpful on controversial issues.

All public pension systems with which management has spoken employ external fiduciary counsel. Accordingly, the retention of external fiduciary counsel appears to be the industry norm and a best practice.

Legal Services Contracts are Exempt from Competitive Bidding

Contracts for legal services are handled differently from other CalPERS contracts because they are exempt from competitive bidding requirements under California law. Despite this exemption, CalPERS has historically issued solicitations requesting proposals from potential candidates to encourage competition among firms, to obtain competitive pricing of legal services, and to create a diverse pool of providers.

Analysis

Management has identified four potential options related to the selection and use of fiduciary counsel on a going-forward basis:

Option 1: Retain the Status Quo

The first option is to retain the status quo through the end of the incumbent's contract term, March 2022, and begin a new selection process in the fall of 2021, in time to have a replacement (or the incumbent) in place when the existing contract terminates.

Potential Advantages:

- Continuity of advice.
- Efficiencies insofar as the incumbent has knowledge of the full range of CalPERS' extant and recent fiduciary issues.
- Cost savings from existing contract relative to new contract and from theoretical "volume discount."

Potential Disadvantages:

- Less flexibility to select counsel for specific issues and projects.
- Could be problematic if existing counsel has a conflict in a particular situation.

Option 2: Issue a New Solicitation and Select a Single Firm

The second option is to commence a new selection process by issuing a new solicitation and then select a single firm to serve as fiduciary counsel. This firm could be the incumbent or it could be a new firm. No back-up or other firms would be retained. If the need arises for specialized fiduciary expertise that is not available from the selected counsel, CalPERS would obtain it on an ad hoc basis.

Potential Advantages:

- Efficiencies insofar as the selected counsel would retain or develop knowledge of the full range of CalPERS' extant and recent fiduciary issues.
- Cost savings relative to a multi-firm approach from theoretical "volume discount."

Potential Disadvantages:

- If new firm selected, cost could be greater than existing contract.
- Cost of new counsel's "ramp-up" time to learn about CalPERS and its fiduciary issues.
- Less flexibility to select counsel for specific issues and projects.
- Could be problematic if selected counsel has a conflict in a particular situation.

Option 3: Issue a New Solicitation and Select Multiple Firms to Participate in a Fiduciary Pool

The third option is to commence a new selection process but select multiple firms to participate in a pool of fiduciary counsel. Earlier this year, CalSTRS moved to this model from its previous reliance on a single firm for fiduciary advice. Under this option, CalPERS would be able to select between the firms in the pool on any given fiduciary issue.

Potential Advantages:

- More immediate access to firms with specific expertise on particular fiduciary issues.
- Immediate availability of counsel in the event one or more of the firms in the pool has a conflict on a particular issue.

Potential Disadvantages:

- Cost could be greater than existing contract.
- Cost of multiple counsel's "ramp-up" time to learn about CalPERS and its fiduciary issues.
- Potential inefficiency from lack of any single firm being aware of the full range of CalPERS' extant and recent fiduciary issues.

Option 4: Issue a New Solicitation and Select Primary and Back Up Fiduciary Firms

This is a variant of Option 3 under which CalPERS would issue a new solicitation but would select a primary fiduciary counsel who would be the default option for fiduciary services but would be backed up by a second firm that would be available in the event the primary firm has a conflict or is otherwise unavailable.

Potential Advantages:

- Efficiencies insofar as the selected primary counsel would develop knowledge of the full range of CalPERS' extant and recent fiduciary issues.
- Cost savings relative to a multi-firm approach from theoretical "volume discount."
- Immediate access to alternative counsel if primary counsel has a conflict or is otherwise unavailable.

Potential Disadvantages:

- Cost could be greater than existing contract.
- Lost efficiencies from not having a single firm as only fiduciary counsel.

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