

CalPERS
2012-17 Strategic Plan

Annual Report

July 2014

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A Message from the Board President and Chief Executive Officer



Rob Feckner



Anne Stausboll

We are pleased to provide our annual report that highlights the achievements and milestones in the second year of the CalPERS 2012-17 Strategic Plan.

The report focuses on the three strategic goals that address pension and health benefit sustainability, organizational strength, and policy engagement. The year was marked by strong progress toward strengthening our organization for generations to come.

As of June 30, 2014, we earned a preliminary 18.4 percent net rate of return on our investment portfolio, exceeding our actuarial assumed rate of 7.5 percent. The funded status, or the percentage of assets we have to pay long-term benefits, is estimated to be 76 percent as of June 30, 2014.

To ensure the long-term sustainability of the Fund, we completed our first-ever asset liability management process that took an integrated view of our assets, liabilities, and actions designed to achieve a fully funded plan.

We negotiated health care premium rates for the new calendar year that reduce premiums for a majority of our members by approximately 3 percent. We increased access and enhanced the quality, effectiveness, and satisfaction of our customer service experience and overall service delivery for members and employers.

Internally, we launched and began implementation of a new multi-year Workforce Strategic Plan that contributes to improved organizational performance and helps CalPERS recruit, retain, develop, and empower a broad range of talents against organizational priorities.

As we embark on a new year, we remain focused on our vision of being a trusted leader, respected for integrity and innovation. We hope this report provides valuable insight into the future of CalPERS and our continued efforts to serve those who serve California.

Sincerely,

Rob Feckner
President, CalPERS Board of Administration

Anne Stausboll
Chief Executive Officer

At CalPERS, we are proud to serve those who serve California. For more than eight decades, we have built and managed retirement and health security for people who invest their life's work in the state. Our Strategic Plan guides us as we deliver on the promise to serve with the highest level of commitment.

VISION

A trusted leader respected by our members and stakeholders for our integrity, innovation, and service

MISSION

Provide responsible and efficient stewardship of the System to deliver promised retirement and health benefits, while promoting wellness and retirement security for members and beneficiaries

CORE VALUES

Quality | Respect | Accountability | Integrity | Openness | Balance

Goal A: Improve long-term pension and health benefit sustainability

Strategic Objectives

- Fund the System through an integrated view of pension assets and liabilities
- Educate employers and other stakeholders to make informed decisions about retirement security and health care
- Deliver target risk-adjusted investment returns
- Ensure high-quality, accessible, and affordable health benefits
- Create a lifestyle of wellness among members and employers

Goal B: Cultivate a high-performing, risk-intelligent, and innovative organization

Strategic Objectives

- Use a focused approach to generate, test, refine, and implement new ideas
- Deliver superior, end-to-end customer service that is adaptive to customer needs
- Recruit, retain, develop, and empower a broad range of talents against organizational priorities
- Actively manage business risks with an enterprise-wide view

Goal C: Engage in state and national policy development to enhance the long-term sustainability and effectiveness of our programs

Strategic Objectives

- Clarify and communicate CalPERS' perspective on pension, health, and financial markets
- Provide education and engagement opportunities to shape policy agenda and expand impact

Goal A: Improve long-term pension and health benefit sustainability

Key Accomplishments Fiscal Year 2013-14

Completed Asset Liability Management Review

Completed an enhanced Asset Liability Management process that took an integrated view of our assets, liabilities, and actions designed to achieve a fully funded plan. The CalPERS Board approved stronger actuarial assumptions and adopted an asset mix that reduces investment risk to help stabilize pension costs over time.

Achieved Strong Investment Returns

Earned a preliminary return of 18.4 percent on our investments, net of fees, well above our actuarial discount rate of 7.5 percent. The Fund was valued at \$300.3 billion dollars, as of June 30, 2014. Investment gains were driven by strong returns in public and private equity, real assets, and fixed income investments.

Implemented Innovative Health Care Approaches to Reduce Costs

Negotiated health care premium rates for the 2015 calendar year that reduce premiums for more than 570,000 members by approximately three percent from last year's rates. Additionally, approximately 175,000 members will experience increases of less than three percent if they stay with their current health plan. Innovative approaches to health care, like reference pricing, integrated delivery systems, regional rate adjustments, cost transparency, and plan competition played a role in keeping premium increases low for most health plans.

Additional Achievements

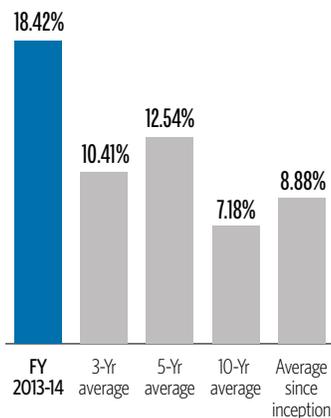
Health Care

- Implemented additional phases of the Dependent Eligibility Verification Project, which verified the enrollment of more than 730,000 health dependents, realizing an estimated \$40 million in annual savings.
- Conducted focus groups and meetings with employers and employees to assess their health plan benefit needs as part of a potential expansion of health care alternatives.

\$300.3 billion

Fund value as of June 30, 2014

Average Investment Returns



30%

reduction to members' health care costs for knee and hip replacements

Additional Achievements, continued

- Partnered with Anthem Blue Cross and Castlight Health to develop an online comparison tool to be launched in July 2014, to help PPO members research costs, quality, and satisfaction of health care treatments.
- Reopened the CalPERS Long-Term Care Program to new applicants for the first time since 2008, providing continuous open enrollment and coverage that can be tailored to meet individual needs and budgets.
- Increased coordination of health care services for members with multiple chronic conditions.
- Reduced pharmacy costs to members by initiating a pharmacy review designed to improve specialty pharmacy programs and better align benefits between health plans and pharmacy benefit managers.
- Added Long-Term Care external benchmark data and analytics to the Health Care Data Warehouse to identify double billing, which resulted in additional cost savings.
- Reduced member costs for knee and hip replacements by 30 percent through the CalPERS value-based pricing program, which sets a reasonable threshold for these and other procedures such as colonoscopies and cataract surgeries.

Transparency on Pensions

- Enhanced employer actuarial valuation reports to include information about prepayment options that will permit employers to more easily make additional contributions to pay off unfunded liabilities for pension benefits more rapidly.
- Redesigned the Actuarial Valuation System to increase capabilities and streamline processes.
- Established a process to address the pension information employers need to comply with new governmental accounting standards.

Investments

- Released the second report *Towards Sustainable Investment & Operations: Making Progress* that chronicles CalPERS efforts in sustainable investing and leadership.
- Released the annual *CalPERS for California* report that showed CalPERS investments within the State of California rose to \$20.8 billion.
- Created a culture of continuous improvement in our Investment Office using the Target Operating Model to define the major functions, roles, and activities needed to achieve target rates of return without exposing the Fund to undue risk.
- Generated \$49.5 million in savings through the reduction of investment consulting and external manager fees.

\$20.8 billion

investments in California

Additional Achievements, continued

Protect Public Pension Soundness

- Protected the integrity and soundness of public pensions, the CalPERS System, and promised benefits in municipal bankruptcy cases. Represented CalPERS in the Stockton bankruptcy case, resulting in a city-proposed plan of adjustment that would preserve CalPERS pensions. Participated in mediation sessions in the San Bernardino bankruptcy case, resulting in an agreement for the city to make certain payments to deferred amounts owing that will help form a basis for the city's plan of adjustment.

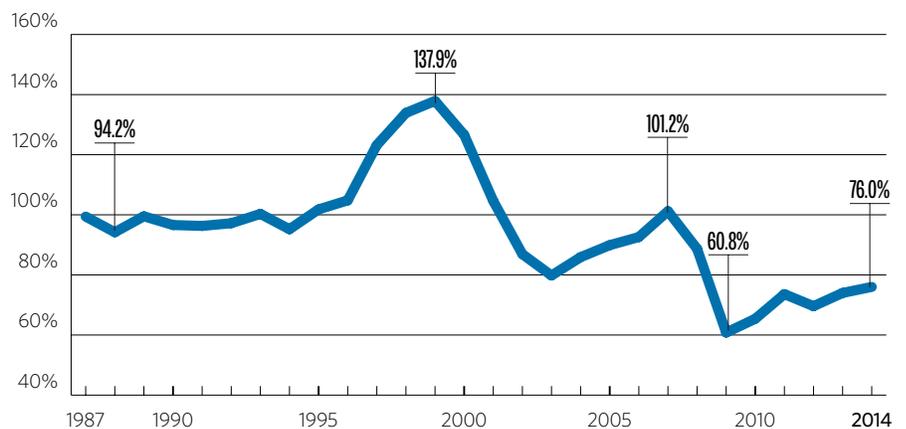
Supplemental Income Plans

- Implemented a new fund line-up of CalPERS Supplemental Income Plans that resulted in a reduction of fees for participants through a simplified menu of index funds and a tiered structure of target retirement date funds, core funds, and self-managed accounts.

Looking Ahead

- Implement new governmental accounting standards and employer reporting requirements to increase fiscal transparency and comply with new mandates.
- Conduct feasibility study of expanding local public agency health care programs.
- Further reduce investment consulting fees and cost allocation.

Public Employees' Retirement Fund — Historical Funded Status



The funded status figure shown for 2014 is an estimate as of date of publication.

Goal B: Cultivate a high-performing, risk intelligent and innovative organization

Key Accomplishments Fiscal Year 2013-14

Multi-Year Workforce Strategic Plan

Launched and began implementation of a new multi-year Workforce Strategic Plan that contributes to improved organizational performance and helps CalPERS recruit, retain, develop, and empower a broad range of talents against organizational priorities. The plan includes succession planning, knowledge transfer, an automated human resources application tracking system, as well as staff training and mentoring programs.

Enhanced Customer Service

Implemented initiatives identified on the Customer Services and Support (CSS) Service Delivery Transformation Roadmap which resulted in increased customer access, enhanced quality, and effectiveness of services while improving customer satisfaction. These enhancement efforts resulted in improved service delivery as measured through the CSS performance metric dashboard.

One Budget

Developed the One Budget model that consolidates five operating budgets and provides a holistic view of the budget process, which increases transparency of the full costs to operate and administer CalPERS pension and health systems.

Additional Achievements

Customer Service

- Developed the Employer Response Team (ERT) to resolve critical, time-sensitive issues. The ERT has resolved over 450 sensitive employer inquiries since its inception. Over 80 percent have been closed within five business days.
- Developed customer surveys for CalPERS Online and five Member Self-Service transactions (estimates, address changes, direct deposits, service retirement applications, and beneficiary designations) to capture customer views on processes, transactions, and interactions.

one budget

improves efficiencies and increases transparency

< 2 minutes

customer call wait times greatly reduced

> 9,000

members participated in Benefits Education Events

Additional Achievements, continued

- Implemented Core Competency training courses for customer service staff designed to reaffirm customer service principles and skills in analytical problem solving, business etiquette, life cycles, and effective writing.
- Conducted focus groups and testing with more than 500 members and employers to improve our website search functionality, architecture, and design.
- Implemented several action plans in the Contact Center to reduce call wait times and achieved an average call wait time of 90 seconds for the 2013-14 Fiscal Year.
- Established service level agreements, processes, and procedures for customer inquiries via social media.
- Hosted six Benefits Education Events reaching more than 9,000 members to educate them on their retirement and health care benefits.
- Increased ratings for customer service to employers, leadership engagement and visibility, and communication and engagement with stakeholders.

CERBT

- Increased the number of contracted employers participating in the California Employers' Retiree Benefit Trust program by more than 15 percent, hitting a milestone of 400 participating employers, and increasing assets under management to a total of \$3.8 billion.

Organizational Excellence

- Launched an internal social media platform called The Spark, designed to increase collaboration and communication among staff.
- Developed a set of strategic measures to assess the progress of the CalPERS Strategic Plan.
- Completed the hiring of 99 Information Technology Services Branch staff for system operations and developed individual knowledge transfer and training plans unique to each employee.
- Implemented electronic timesheets and enhanced employee wellness at work programs, which included new running classes, lunchtime yoga sessions, nutrition classes, and a walking program. Also added a health diagnostic station for employees to check blood pressure, heart rate, and body mass index.
- Increased campus security, implemented new information security protections, and expanded data loss prevention capabilities across the organization.
- Increased knowledge of investment fundamentals for investment, compliance, and accounting staff throughout the organization to better support the investment function.

Additional Achievements, continued

- Developed a new technology strategic plan to align with the enterprise strategic plan and business needs.
 - Conducted the Member-at-Large Board Election.
-

Looking Ahead

- Conduct a comprehensive executive compensation policy review.
 - Complete a global recruitment for a chief investment officer.
 - Enhance the customer experience by improving access, effectiveness, and quality of services through process improvements, people, and technology optimization.
-

A Closer Look at Our Customer Service

- Conducted over 255 classes with 2,940 employer representatives (from more than 1,400 state, school, and public agencies) on CalPERS laws and business rules to reduce errors and inquiries and improve the accuracy of members' benefits.
- Provided retirement planning, health, and program education with 1,614 classes to more than 53,700 members to help members make informed retirement and health decisions.
- Informed employers about operational and policy updates through 203 Web updates, 114 Employer Bulletins, 27 Circular Letters, and 22 computer-based education modules.
- Expanded employer education channels to include two new employer education webinars with 321 participants and an employer teleconference on the implementation of Assembly Bill 1222, which reached 80 participants in impacted public agency employers.
- Delivered 12 member education webinars, which included six new topics, to more than 11,600 participants.
- Assisted more than 69,500 members and their families with adding or changing health plans during open enrollment.

Goal C: Engage in state and national policy development to enhance the long-term sustainability and effectiveness of our programs

Key Accomplishments Fiscal Year 2013-14

Adopted Investment Beliefs

Adopted a set of 10 Investment Beliefs that provide a basis for strategic management of investments and inform organizational priorities. The Beliefs reflect CalPERS' values and acknowledge our responsibility as a long-term investor to sustain the ability to pay benefits for future generations.

Adopted Pension Beliefs

Adopted Pension Beliefs that articulate CalPERS' views on public pension design, funding, and administration. The Beliefs reflect our commitment to our core mission and will help advance the dialogue on public pensions, establish parameters for policy advancement, and will be used in communication with members, employers, policy makers, and other stakeholders.

Thought Leadership

Published three research papers:

- *CalPERS Economic Impacts in California* — highlights the vital role CalPERS plays in the state's economy.
- *The Emerging Role of Defined Contribution Plans for California Public Employees* — explores the savings and additional years of service Public Employees' Pension Reform Act employees need to retire with income comparable to Classic employees.
- *California Public Employee Retirement Benefits-Assessing Compensation Changes* — examines California state and local government salaries and retirement benefits in a national context and estimates the changing monetary value of defined benefits following the passage of the Public Employees' Pension Reform Act.

Additional Achievements

Conferences

- Hosted an Employer Forum for more than 800 representatives from public agency employers, providing employers access to education, consultation, and networking throughout the CalPERS community over a three-day event. This included opportunities to speak one-on-one with experts in the following areas: actuarial, contracts, payroll, membership, health, and social security.

> 800

representatives from public agencies attended Employer Forum

10,000+
number of shareholder votes

Additional Achievements, continued

- Held an Emerging and Diverse Manager Forum as part of our ongoing commitment to engage and strengthen relationships with emerging managers and improve implementation of emerging manager investment strategies.

Reports

- Delivered a report to the Legislature outlining the accomplishments made under our Emerging Manager Five-Year Plan.
- Released the second report *Towards Sustainable Investment & Operations: Making Progress* that chronicles CalPERS' efforts in sustainable investing and leadership.

Corporate Governance

- Engaged 19 energy sector portfolio companies to address the integration of sustainability performance factors (environmental, social, and governance) into corporate executive compensation packages and incentive plans.
- Voted over 10,000 company proxies consistent with CalPERS' Global Principles of Accountable Corporate Governance and successfully encouraged 40 companies to adopt or agree to adopt majority voting in director elections.

Policy

- Engaged state and federal policy makers on the importance of having unimpeded access to biosimilar and interchangeable biosimilar drugs to help contain health care costs.
- Engaged federal policy makers to urge bipartisan action this year to permanently repeal the Sustainable Growth Rate and transition Medicare reimbursement toward a value-based system.

Health Care

- Demonstrated thought leadership and innovation on reference pricing in the health care marketplace.

Looking Ahead

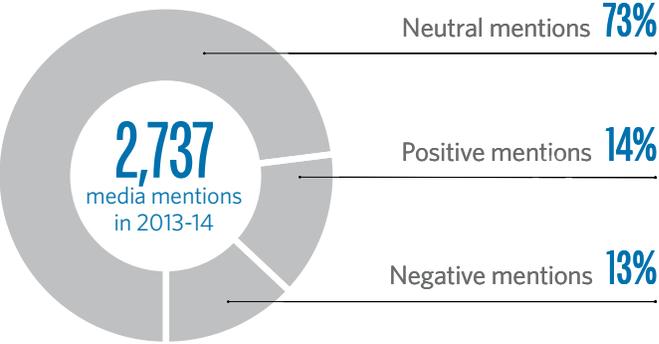
- Develop a set of priorities for financial market reform.
 - Communicate and generate awareness of Investment and Pension Beliefs.
 - Increase engagement with state and federal policy makers on health care innovations.
 - Advocate for retirement security and the value of defined benefit plans on a state and national level.
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A Closer Look at Our Economic Impacts in California

- CalPERS benefits (retirees spending their pensions) returned \$10.85 in economic activity to California for each taxpayer dollar contributed to the system.
- Total economic revenue generated by CalPERS benefits was more than \$30.4 billion.
- CalPERS benefits helped create or support 113,664 jobs throughout California.
- CalPERS benefits generated \$385 million in sales tax revenue and \$410 million in property tax revenue.
- *CalPERS for California* report showed that investments in California accounted for \$20.8 billion in Fiscal Year 2012-13, approximately 8 percent of the CalPERS portfolio. This represents an increase of 5.6 percent over the previous fiscal year.
- More than 73 percent of private equity investments in California are in areas with a high population of minority groups.

A Closer Look at Our Perception in the Media

CalPERS experienced a range of positive, neutral, and negative media mentions in the press. Negative media coverage went down significantly from the previous year, while positive mentions rose.



Conclusion

In 1921, a handful of California state employees got together and talked about setting up a retirement fund. Their goal: to make sure that the people who serve the public would be able to pay for housing, buy food, and get proper health care in exchange for a life of dedicated service.

Seven years later, CalPERS was established.

We have witnessed many changes over the years including unstable financial markets, a rapidly changing health care marketplace, and pension reform. Through the good and difficult times, our goal remains the same today: to help the people who serve California secure their financial future.

Recognizing Excellence: CalPERS Awards

- CalPERS Disability Advisory Council was awarded second place in the 2014 Disability Advisory Council of the Year Award by the Association of California State Employees with Disabilities, for dedication to the inclusion and equality of employees with disabilities, and for ensuring an environment that is accessible to all employees.
- Achieved LEED Platinum status from the U.S. Green Building Council for the Lincoln Plaza East and West buildings as a result of energy and water sustainability initiatives.
- Received the 2013 Sustainable Business of the Year Award from the Business Environmental Resource Center for work on the Energy Conservation project.
- Received the 2013 Environmental Protection Agency Energy Award for reducing energy consumption by 35 percent and generating 35 percent fewer greenhouse gas emissions.
- Ranked third for sustainable investment among the world's 1,000 largest asset owners, a 12-place improvement over the 2012 ranking.
- Received a Commendation for the Best Responsible Investment Report by a Large Pension Fund from *Responsible Investor* for CalPERS' report *Towards Sustainable Investment: Taking Responsibility*.
- Received the annual Value-Based Health Award from the Institute for Health and Productivity Management. The award recognizes organizations for excellence in health care management. CalPERS was cited for providing employees with quality care and cost savings.
- Finalist for the Sacramento Business Journal's 2014 Healthiest Employer Award.
- Board Member and Investment Committee Chair Henry Jones was honored as an Institutional Trailblazer by the Toigo Foundation for his work to advance diversity in the finance industry.
- Former Chief Investment Officer Joseph A. Dear (1951-2014) received the Chief Investment Officer Stewardship award from Institutional Investor for his contributions in the investment field.
- Chief of the Office of Public Affairs Brad Pacheco received the 2014 California State Information Officers Council Lifetime Achievement Award.
- Senior Portfolio Manager and Director of Global Governance Anne Simpson was recognized by the U.S. Green Building Council for her leadership on CalPERS environmental, social and governance efforts.

Recognizing Excellence: CalPERS Awards, continued

- Chief Information Officer Liana Bailey-Crimmins and Deputy Executive Officer of Customer Services and Support Donna Lum were featured in a *Public CIO Special Report* published by the Center for Digital Government as leaders in Next Generation Government focusing on CalPERS relationship management revolving around customer service and customer-focused innovation.
 - CalPERS Information Technology leaders Dason McJimsey and Chris Riesen were recognized for exceptional leadership by the California Chief Information Officer Academy.
 - CalPERS received a certificate for Achievement of Excellence in Financial Reporting from the Government Finance Officers Association.
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Reports and Research

- *CalPERS Commitment to Diversity & Inclusion Report*
<http://www.calpers.ca.gov/eip-docs/about/pubs/diversity-report.pdf>
- *The Emerging Role of Defined Contribution Plans for California Public Employees*
<http://www.calpers.ca.gov/eip-docs/about/pubs/defined-contribution.pdf>
- *California Public Employee Retirement Benefits – Assessing Compensation Changes*
<http://www.calpers.ca.gov/eip-docs/about/pubs/compensation-changes.pdf>
- *Towards Sustainable Investment & Operations: Making Progress*
<http://www.calpers.ca.gov/eip-docs/about/pubs/esg-report-2014.pdf>
- *CalPERS for California 2013*
<http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/invest/201406/item07d-02.pdf>
- *CalPERS California Initiative 2013*
<http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/invest/201406/item07d-03.pdf>
- *Annual Investment Report*
<http://www.calpers.ca.gov/eip-docs/about/pubs/annual-investment-report-2013.pdf>
- *Comprehensive Annual Financial Report*
<http://www.calpers.ca.gov/eip-docs/about/pubs/cafr-2013.pdf>
<http://www.calpers.ca.gov/eip-docs/about/pubs/2013-executive-summary.pdf> (Executive Summary)



**California Public Employees'
Retirement System**

400 Q Street
P.O. Box 942701
Sacramento, CA 94229-2701
www.calpers.ca.gov

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For media inquiries, please contact
(916) 795-3991 or newsroom@calpers.ca.gov.