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June 4, 2018

The Honorable Bill Huizenga
Chairman
Subcommittee on Capital Markets,
Securities, and Investment
Committee on Financial Services
United States House of Representatives
Washington, D.C. 20515

The Honorable Carolyn B. Maloney
Ranking Member
Subcommittee on Capital Markets,
Securities, and Investment
Committee on Financial Services
United States House of Representatives
Washington, D.C. 20515

Dear Chairman Huizenga and Ranking Member Maloney:

Subject: May 23, 2018 Hearing Entitled "Legislative Proposals to Help Fuel Capital and Growth on Main Street"

On behalf of the California Public Employees' Retirement System ("CalPERS"), I write to respectfully express our views about several issues that were considered during the Capital Markets, Securities, and Investment Subcommittee hearing on May 23, 2018, entitled "Legislative Proposals to Help Fuel Capital and Growth on Main Street."¹ We respectfully request that this letter be included in the hearing record.

CalPERS is the largest public, defined benefit pension fund in the United States, with \$351.80 billion in global assets, as of market close May 29, 2018, and equity holdings exceeding 10,000 companies. CalPERS manages investment assets on behalf of more than 1.9 million California public employees, retirees and beneficiaries. As a global, institutional investor with a long-term investment horizon, CalPERS depends on the integrity, transparency and efficiency of the financial markets, as well as access to reliable and accurate information in order to make investment decisions. The investment objective of CalPERS is to provide long-term sustainable, risk-adjusted returns.

We appreciate the Subcommittee's consideration of a number of legislative proposals that are designed to address regulatory impediments that impact the ability of "Main Street" businesses, early-stage and small companies, as well as emerging growth companies ("EGCs"), to access capital, which is vitally important to business and productivity growth, job and wealth creation, sustainable community and economic development, and innovation. CalPERS provides this much-needed capital by investing in public companies, primarily as a long-term investor. The benefits of access to capital accrue to the direct recipients of investments and to the geographic areas in which they are located. As such,

¹ House Financial Services Committee, Hearings,
<https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403426>.

we have long supported efforts to promote capital formation and more liquid financial markets to spur sustainable growth in the real economy, while at the same time fostering greater transparency and protecting investor rights.

As the Subcommittee considers efforts to stimulate capital formation, particularly for small and medium sized enterprises, we respectfully urge you to also consider the potential implications of these initiatives for an investor such as CalPERS, as well as other providers of capital. In this regard, we would like to take this opportunity to provide our views about the following topics: corporate governance; potential enhancements of the Jumpstart Our Business Startups (“JOBS”) Act; the need for additional research on EGCs and smaller issuers; corporate financial reporting; and equity market structure reform.

Corporate Governance:

As embodied in the CalPERS Governance & Sustainability Principles (the “Principles”),² we firmly embrace accountable corporate governance. In CalPERS’ experience, it is critical for capital providers, particularly institutional investors, to have the ability to actively engage with company management, and the shareholder proposal process promotes such engagement. For this reason, we are opposed to efforts to substantially revise the resubmission thresholds for shareholder proposals under Securities and Exchange Commission (“SEC”) Rule 14a-8. Because large companies comprise a larger portion of investors’ equity portfolios than small companies, large companies are more likely to receive shareholder proposals. According to the ISS Voting Analytics database, S&P 500 companies received some 659 proposals in 2017, which equaled 77 percent of the 852 proposals that Russell 3000 companies received and corresponded to the S&P’s coverage of the Russell 3000’s market capitalization. Of particular note, only 3.7 percent of shareholder proposals in the ISS database were filed at companies with a market capitalization below \$1 billion.

Given the small number of shareholder proposals that are filed at reporting companies in the U.S. with the overwhelming majority being filed at S&P 500 companies, it appears as though there is no shareholder proposal crisis at small companies that needs to be addressed. Historically, small shareholders initiated many of the campaigns for enhancements at large companies that were eventually adopted as best corporate practices. There is no need to restrict shareholder proposals, which would make it more difficult for shareholders to file proposals and have them appear in proxies. Therefore, we oppose efforts to prevent or further restrict shareholders from exercising their rights as owners. We emphasize that this is not a matter of “shareholder activism.” Rather, shareholder engagement is critical to the exercise of our fiduciary responsibilities and to the pursuit of our aforementioned investment objectives.

We oppose efforts that would establish a burdensome regulatory regime for proxy advisory firms or grant issuers undue influence over the proxy recommendation process. The

² CalPERS Governance & Sustainability Principles, Apr. 17, 2017, <https://www.calpers.ca.gov/docs/forms-publications/governance-and-sustainability-principles.pdf>.

proposed changes would force institutional investors to pay significantly more to comply with our fiduciary obligations to vote our shares. We have heard the concerns about perceived “conflicts of interest” in the proxy advisory industry, but have not seen credible examples. We are concerned about imposing conflict of interest management requirements when existing SEC requirements appear to be effective in this area. Among other things, we are also concerned that proposed reforms would present additional barriers to entry for new proxy advisory firms rather than enhance competition. Proxy advisory firms and other data providers play a useful role in efficiently providing institutional investors with independent research and analysis to help us execute our voting decisions. Accordingly, we oppose efforts to subject proxy advisory firms to new, duplicative and overly burdensome regulatory requirements.

We support the current quarterly filing regime. Certain 8-K filings are no substitute for 10-Qs. Although an argument can be made that people trade on the 8-Ks, such an argument holds simply because the 8-Ks are released prior to 10-Q filings. The 10-Qs provide substantial and important information and serve as a great historical resource. Any modification of standard quarterly filings should be preceded by significant study with ample opportunity for investor input.

These views are consistent with the underlying tenet of the Principles: fully accountable governance structures produce, over the long term, the best returns to shareowners.

Enhancements to the JOBS Act:

The JOBS Act provides a number of benefits to EGCs, including those related to the submission of confidential registration statements to the SEC, as well as scaled disclosures concerning executive compensation and audited financial statements. As a significant capital provider, we believe that the current five-year exemption for EGC status is a well thought out compromise, given that many institutional investors were against any exemption in the first place. Further, we are only aware of anecdotal evidence that an extension of the exemption for EGC status would benefit certain companies, and we have seen no convincing evidence that there would be a market benefit to such extension. Large accelerated filers have large market capitalizations and should report accordingly. To be clear, the proposal would provide exemptions to very low revenue producing (but highly valued) companies while forcing companies with more substantial revenues to continue to comply with standard reporting. It appears that the wrong market behavior would be rewarded if the proposed exemption is given to low revenue producing companies with high market capitalizations.

Additional Research on EGCs and Other Small Public Companies:

We favor proposals that are designed to promote additional research and coverage of small companies, and we support enabling the SEC to examine why pre-IPO research has not materialized following enactment of the JOBS Act. We note that the findings of these studies would help to inform and guide additional proposals and increase the likelihood of success for small publicly-traded companies.

Corporate Financial Reporting:

Any proposals that would broaden eligibility for definition of a “smaller reporting company” (“SRC”) should take into consideration (and should be balanced against) the critical information needs of investors. An SRC currently qualifies as such if it has a public float of less than \$75 million. We have long felt that financial reporting disclosures need to be meaningful, understandable, timely, comparable, and consistent to enable open and honest dialogue as well as informed decision-making. Consequently, any proposal to expand the number of registrants that qualify as SRCs must be consistent with the aforementioned principles in order to ensure investor protection.

Equity Market Structure:

CalPERS has consistently supported efforts to make reasonable reforms to the U.S. equity markets, and believes that such initiatives should mitigate risks to the markets and advance the interests of long-term investors. In recent history, technological advancements and regulatory actions have sought to increase market competition and lower trading costs. Unfortunately, this has resulted in increased market complexity and various unintended consequences, and long-term investors have often borne the cost. We note that proposals to improve liquidity and market quality by increasing the ticket sizes of EGCs and small capitalization stocks have raised important concerns about trading activity and volatility. CalPERS believes that such proposals should be carefully examined to assure that they are constructed in a manner that maximizes their utility while at the same time diminishes costs and risks to investors.

Thank you for considering our views. We welcome the opportunity to work with you on ways to protect investors while fostering a favorable regulatory environment for “Main Street” businesses and smaller companies so that they are able to access capital, innovate, grow and create jobs. Please do not hesitate to contact Gretchen Zeagler, Assistant Division Chief of Federal Policy at (916) 795-2911, if we can be of any assistance.

Sincerely,

MARCIE FROST
Chief Executive Officer