

California Code of Regulations
Title 2. Administration
Division 1. Administrative Personnel
Chapter 2. Board of Administration of Public Employees' Retirement System

NOTICE OF PROPOSED REGULATORY ACTION

NOTICE IS HEREBY GIVEN that the Board of Administration (Board) of the California Public Employees' Retirement System (CalPERS) is proposing to take the regulatory action described below in the Informative Digest after considering public comments, objections, and recommendations regarding the proposed regulatory action.

I. PROPOSED REGULATORY ACTION

In this filing, the Board proposes to amend the Section 558.1 to Article 1 of Subchapter 1 of Division 1 of Title 2 of the California Code of Regulations (CCR). The proposed regulation would ensure that (1) CalPERS fully complies with federal and state laws around the misuse of material, non-public information and (2) CalPERS' employees and their spouses have a clear understanding of the agency's personal trading requirements.

II. WRITTEN COMMENT PERIOD

Any interested person may submit written comments relevant to the proposed regulatory action. The written comment period has been established commencing on March 1, 2019 and closing on April 15, 2019. The Regulation Coordinator must **receive** all written comments by the close of the comment period. Comments may be submitted via fax at (916) 795-4607; emailed to Regulation_coordinator@calpers.ca.gov or mailed to the following address:

Anthony Martin, Regulation Coordinator
California Public Employees' Retirement System
P.O. Box 942702
Sacramento, CA 94229-2702
Phone: (916) 795-3038

III. PUBLIC HEARING

A public hearing will not be scheduled unless an interested person, or his or her duly authorized representative, submits a written request for a public hearing to CalPERS no later than 15 days prior to the close of the written

comment period. Notice of the time, date, and place of the hearing will be provided to every person who has filed a request for notice with CalPERS.

IV. ACCESS TO HEARING ROOM

The CalPERS Auditorium will be accessible to persons with mobility impairments, and it can be made accessible to persons with hearing or visual impairments upon advance request to the CalPERS Regulation Coordinator.

V. AUTHORITY AND REFERENCE

CalPERS authority to make the proposed amendment to the California Code of Regulations derives from the CalPERS Board of Administration's plenary authority and fiduciary responsibility over the assets of the public retirement system, pursuant to the California Constitution (Section 17 of Article XVI) and the Public Employees' Retirement Law (PERL) (California Government Code, Title 2, Division 5, Part 3), including Government Code sections 20120 and 20121. The proposed amendment to section 558.1 implement, interpret and make specific Government Code sections 19990, 87200 and 87300.

VI. INFORMATIVE DIGEST

Existing law recognizes the Board's authority to regulate the personal trading of identified Covered Employees. Section 20120 and 20121 of the California Government Code permits the Board to make such rules as it deems proper. Rule 204A-1 under the Investment Advisers Act of 1940 ("Advisers Act") requires each registered investment adviser to adopt a written code of ethics. A code of ethics must require that employees comply with applicable federal securities laws and impose restrictions and monitoring requirements over the personal trading of securities by certain employees. Although CalPERS is not governed by the Advisers Act, CalPERS is still bound by the anti-fraud provisions of the federal securities laws, including the prohibition on insider trading and other forms of market manipulation. The need to ensure compliance with the federal securities laws through compliance programs and appropriate regulations was underscored in 2008 when the Securities and Exchange Commission issued a report of investigation concerning potential violations of federal securities laws by the Retirement System of Alabama (<https://www.sec.gov/litigation/investreport/34-57446.htm>), that all "access persons" report their personal securities transactions and holdings to the chief compliance officer for review. (17 CFR § 275.204A-1(a)(3)). This provision is modeled on Rule 17j-1 under the 1940 Act, which requires that investment companies have procedures in place to prevent their personnel from abusing their access to information about the investment company's securities trading and requires access persons to submit reports periodically containing information about their personal securities holdings and transactions. (17 CFR

§ 270.17j-1(c)(2)). To meet these requirements, the proposed regulation provides as follows.

First, the proposed regulation seeks to refine the definition of “Covered Persons” in a manner that more closely aligns with SEC recommendations and that addresses various functional re-organizations that have occurred in CalPERS since the adoption of the regulation in 2012.

Second, the proposed regulation seeks to align CalPERS rules with recent SEC guidance. This includes guidance around Exchange Traded Funds (ETFs) and Managed Accounts.

Third, the proposed regulation seeks to clarify areas of the previous regulation that caused confusion or were open to multiple interpretations. This includes clarifications around holding periods for derivatives, accounts held at non-designated brokerages, and certification of managed accounts.

Policy Statement Overview / Anticipated Benefits

The primary purpose and benefit of the proposed regulation is to ensure that (1) CalPERS complies with federal and state laws prohibiting the misuse of material, non-public information; and, (2) CalPERS’ employees and their spouses have a clear understanding of the agency’s personal trading requirements. The federal and state laws are designed to ensure that the marketplace for securities is fair and to deter individuals from improperly utilizing non-public information to the detriment of other market participants.

There are two principal authorizing statutes. The statutes vest in the Board management and control of the retirement system, and authorize the Board to make such rules as it deems proper, respectively. (Cal. Gov. Code §§ 20120, 20121.)

Consistency and Compatibility with Existing Regulations

CalPERS evaluated whether there were any other laws or state regulations on this topic and has concluded that the proposed regulation is neither inconsistent nor incompatible with existing law or existing state regulations.

Pre-notice Consultation with the Public

No pre-notice consultation was done with the public, as the proposed regulation does not involve complex proposals or a large number of proposals that cannot easily be reviewed during the comment period.

VII. EFFECT ON SMALL BUSINESS

The proposed regulatory action does not affect small business because it applies only to CalPERS Board members, employees, and their spouses.

VIII. DISCLOSURES REGARDING THE PROPOSED REGULATORY ACTION

- A. MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS: The proposed regulatory action does not impose any mandates on local agencies and school districts.
- B. COSTS OR SAVINGS TO ANY STATE AGENCY: The proposed regulatory action will not result in any additional costs or savings to any State agency.
- C. COSTS TO ANY LOCAL AGENCY OR SCHOOL DISTRICT: The proposed regulatory action will not result in any costs on any local agency or school district.
- D. NONDISCRETIONARY COSTS OR SAVINGS IMPOSED ON LOCAL AGENCIES: The proposed regulatory action does not impose any nondiscretionary costs or savings on local agencies.
- E. COSTS OR SAVINGS IN FEDERAL FUNDING TO THE STATE: The proposed regulatory action will not result in additional costs or savings in federal funding to the State.
- F. ADVERSE ECONOMIC IMPACT: The proposed regulatory action will not have a significant statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states.
- G. COST IMPACT ON REPRESENTATIVE PRIVATE PERSONS OR BUSINESSES: CalPERS is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed regulatory action.
- H. RESULTS OF THE ECONOMIC IMPACT ANALYSIS: The proposed regulatory action: (1) will not create or eliminate jobs within California; (2) will not create new businesses or eliminate existing businesses within California; (3) will not affect the expansion of businesses currently doing business within California; and (4) will not affect worker safety or the state's environment. As stated under the Policy Statement Overview/Anticipated Benefits section above, the benefits of the proposed regulation are to ensure CalPERS compliance with federal and state laws governing the use of material, non-public

information, as well as ensure that the personal trading of designated agency personnel complies with the foregoing.

- I. EFFECT ON HOUSING COST: The proposed regulatory action has no effect on housing cost.
- J. COSTS TO ANY LOCAL AGENCY OR SCHOOL DISTRICT WHICH MUST BE REIMBURSED IN ACCORDANCE WITH GOVERNMENT CODE SECTIONS 17500 THROUGH 17630: there are no costs to any local agency or school district which must be reimbursed in accordance with Government Code sections 17500 through 17630.

IX. CONSIDERATION OF ALTERNATIVES

In accordance with Government Code Section 11346.5(a)(13), the Board must determine that no reasonable alternative considered by the Board, or that has otherwise been identified and brought to the attention of the Board, would be more effective in carrying out the purpose for which the regulatory action is proposed, or would be as effective as, and less burdensome to, affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

The Board invites interested persons to present statements or arguments with respect to alternatives to the proposed regulations at the scheduled hearing or during the written comment period.

X. CONTACT PERSON

Please direct inquiries concerning the proposed regulatory action to:

Anthony Martin, Regulation Coordinator
California Public Employees' Retirement System
P.O. Box 942702
Sacramento, CA 94229-2702
Phone: (916) 795-3038

The backup contact for these inquiries is:

Christina Nutley, Regulation Coordinator
California Public Employees' Retirement System
P.O. Box 942702
Sacramento, CA 94229-2702
Phone: (916) 795-3038

Please direct requests concerning the copies of the proposed text (the “express terms”) of the regulations, the Initial Statement of Reasons, the modified text of the regulations, if any, or other information about processing of this regulatory action to Evan Bailey, Regulation Coordinator, at Regulation_coordinator@calpers.ca.gov.

XI. AVAILABILITY OF STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATIONS, AND RULEMAKING FILE

The entire rulemaking file is available for public inspection through the Regulation Coordinator at the address shown in section II. To date, the file consists of this Notice, the proposed text of the regulations, the Initial Statement of Reasons, the Economic Impact Assessment, and the Economic and Fiscal Impact Statement. A copy of the proposed text, the Initial Statement of Reasons, the Economic Impact Assessment, and the Economic and Fiscal Impact Statement is available at no charge upon telephone or written request to the Regulation Coordinator.

For immediate access, the regulatory material regarding this action can be accessed at CalPERS’ website at www.calpers.ca.gov.

XII. AVAILABILITY OF CHANGED OR MODIFIED TEXT

The Board may, on its own motion or at the recommendation of any interested person, modify the proposed text of the regulations after the public comment period closes.

If the Board modifies its regulatory action, it will prepare a comparison of the original proposed text and the modifications for an additional public comment period of not less than 15 days prior to the date on which the Board adopts, amends, or repeals the resulting regulation. A copy of the comparison text will be mailed to all persons who submitted written comments or asked to be kept informed as to the outcome of this regulatory action.

XIII. AVAILABILITY OF THE FINAL STATEMENT OF REASONS

The Final Statement of Reasons can be obtained, once it has been prepared, by written request to Evan Bailey, Regulation Coordinator, at the address shown above in Section II.