

MACFARLANE PARTNERS

SENT BY EMAIL

March 29, 2007

California State Teachers' Retirement System
7667 Folsom Boulevard
Sacramento, CA 95826

Re: Proposed new regulations in the form of Sections 24010, 24011, 24012 and 24013 in new Article 14, Chapter 1, Division 3 of Title 5 of the California Code of Regulations ("CCR"), "Prohibitions on Certain Campaign Contributions", and to amend current Section 20520 of Article 3, Chapter 1, Division 3, Title 5 of the CCR

Ladies and Gentlemen:

We manage pooled investment funds in which CalSTRS is an existing limited partner. We have reviewed copies of the proposed new regulations addressing the issue of campaign contributions. We understand the Board's purpose in this endeavor and, of course, will abide by all regulations pertaining to our activities.

There are some areas that we recommend be clarified to maintain CalSTRS' position as a pre-eminent institutional investor. Such clarification will benefit CalSTRS, as the ambiguity in the proposed regulation and side letter provision may impair CalSTRS' ability to take advantage of its size and scale in the market place, and ultimately may impede CalSTRS' ability to participate in top-tier investment funds.

- 1) Section 24011(c) states that those found to be in violation shall be subject to "termination of existing business with CalSTRS." We recommend that this rule be clarified to exclude existing partnerships in which CalSTRS is a limited partner. If CalSTRS attempts to withdraw or cease making required capital contributions to an existing partnership, it will not only be in violation of the applicable partnership agreements, which typically prohibit withdrawal by limited partners, but it will also jeopardize the ability of these partnerships to meet investment obligations, thereby potentially damaging the interests of all other limited partners, which, for the most part, are other pension plans, endowments and foundations that are not subject to the proposed regulations. In such a case, CalSTRS may be subject to claims for damages from the other limited partners in these partnerships and to other penalties as provided in the applicable partnership agreements.
- 2) With respect to CalSTRS' option to withdraw from partnerships or to stop funding capital contributions, we recommend that additional details regarding the withdrawal or cessation be included in the side letter to ensure equitable results for all affected

limited partners and to preserve CalSTRS' desirability as a capital investor. These details should include that, at the time of withdrawal or cessation: a) any capital called, but not yet funded, at the time of withdrawal or cessation will be contributed to the partnership by CalSTRS; b) CalSTRS will honor and fund its pro-rata share of capital contribution obligations, such as outstanding balances on the partnership subscription credit line and accrued management fees, as of the date of cessation or withdrawal; and c) CalSTRS will honor and fund its pro-rata share of capital contributions for investments for which the partnership has already made binding commitments.

- 3) In Section 24013, it would be beneficial to clarify that the regulation will be effective on and after the date of adoption, and will not apply retroactively.
- 4) Exhibit A-1 to the Side Letter as drafted makes no mention that the contribution prohibition limit is \$1,000. Instead, it asks only for disclosure on contributions in excess of \$250. To avoid ambiguity, we recommend that the Side Letter specifically state that the prohibition is \$1,000.

If you have any questions or concerns, please feel free to contact me at 415-356-2500. I hope that these comments are helpful and will assist you in devising an effective, equitable policy.

Sincerely,



Sylvia Melikian
Principal & Portfolio Manager