



Investment Committee

Item Number 4a – Open Session

Subject: Diversity in the Management of Investments

Presenter(s): LaShae Badelita

Item Type: Action

Date & Time: May 5, 2022 – 10 minutes

Attachment(s): Attachment 1 – AB 890 Reporting Requirements
Attachment 2 – AB 890 Emerging Manager Definition

PowerPoint(s): Diversity in the Management of Investments

POLICY

The Diversity in the Management of Investments report is covered under the reporting and monitoring requirements of the overall CalSTRS Investment Policy and Management Plan.

PURPOSE

The intent of this item is to receive the Investment Committee’s input and approval of the following as required by the statutes of [AB 890 \(Cervantes; 2021; “AB 890”\)](#)

- “Emerging manager” definition;
- “Diverse manager” definition and
- “Objective” regarding the participation of emerging or diverse managers responsible for asset management within the system’s investment portfolio.

BACKGROUND

Diversity in the Management of Investments

Diversity is a [core value](#) of CalSTRS: “*Strength: We ensure the strength of our System by embracing a diversity of ideas and people.*” Building teams that exhibit diversity, equity and inclusion are essential in achieving CalSTRS’ financial and return objectives. CalSTRS efforts to expand diversity in the management of investments began over 30 years ago in 1989, with the fund’s first capital commitment to emerging managers in the public equity asset class. In 2003, diversity within investments was formally established as a Strategic Initiative of the Investment Committee. As such, diversity is integrated into the overall CalSTRS Investment Policy and Management Plan. CalSTRS currently has emerging manager programs for asset classes: Global Equity, Fixed Income, Private Equity, Real Estate and Inflation Sensitive.

AB 890

Assembly Bill 890 (Cervantes) was signed into law in October 2021. According to the bill's author, AB 890 is intended to ensure transparency and promote the inclusion of women and minority-owned managers in the asset management industry. Known supporters of the bill includes the New America Alliance and Association of Asian American Investment Manager.

- **CalSTRS Board Position.** CalSTRS Board (“board”) position of AB 890 is neutral as it is the board’s policy to take a neutral position on bills that do not significantly or adversely impact the benefits or services provided through the funds administered by CalSTRS for the administration of the retirement plans.
- **CalSTRS Requirements.** AB 890 requires the board to: define the terms "emerging manager" and "diverse manager.” Additionally, AB 890 requires CalSTRS to submit an annual report, beginning March 1, 2023, on the status of achieving appropriate objectives and initiatives, as defined by the board, regarding the participation of emerging or diverse managers responsible for asset management within CalSTRS investment portfolio. The bill sunsets on January 1, 2028, unless a later enacted statute deletes prior to 2028 or extends that date. The report must be based on contracts entered into on and after January 1, 2022, and include:
 - The name of each emerging or diverse manager providing investment portfolio or asset management services, including, but not limited to, fund of funds contracts, for all asset classes;
 - The year these managers were first engaged or contracted to provide services;
 - The amount managed by each of these managers by asset class;
 - The total dollar amount allocated by the system in the applicable asset class; and
 - The total dollar amount of the asset class in the system’s investment portfolio.

HISTORY

In 2011, SB 294 (Price; 2011) required CalSTRS to define the term “emerging investment manager,” provide a five-year strategic plan for emerging investment manager participation across all asset classes and submit an annual report to the Legislature on the progress of the strategic plan beginning March 1, 2014, through January 1, 2018. SB 294 sunset in 2017.

Current bill, AB 890, reporting requirements include more specific details than was mandated under SB 294 and CalSTRS current voluntary reporting (Attachment 1). For example, SB 294 reporting requirement did not include: the name specific emerging managers; the term “diverse manager;” the year these managers were first engaged, the total amount allocated by CalSTRS to the applicable asset class or the total amount of the asset class in the CalSTRS investment portfolio.

DISCUSSION**Implementation Plan**

To meet the requirements of AB 890, CalSTRS Investments developed an implementation plan composed of five key deliverables as outlined below. CalSTRS Investments, Public Affairs, Legal and Communications are working together to complete the implementation deliverables.

AB 890: Implementation Plan		
Due Date	Milestone	Status
1 March 2022	Develop Proposed Terms: (1) Emerging Manager, (2) Diverse Manager, (3) Objective	Completed
2 May 2022	Seek CalSTRS Investments Committee approval of Proposed Definitions	In Progress
3 April 2022	Finalize Diversity, Equity, and Inclusion (DEI) Survey	Not Started
4 June 2022	Launch DEI Survey	Not Started
5 March 2023	Deliver Report to Legislature	Not Started

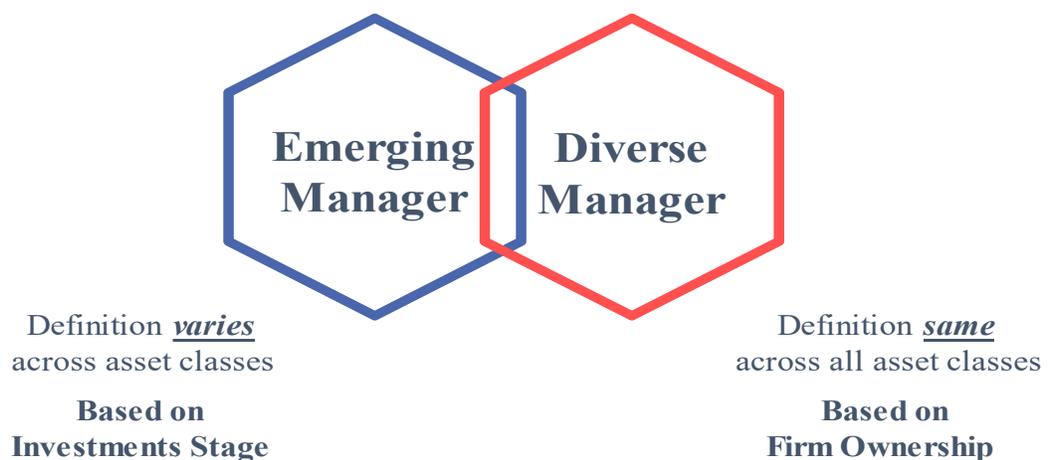
To comply with reporting requirements of AB 890, CalSTRS will survey its managers within the Investment portfolio. Survey participation will be on a voluntary basis. Applying CalSTRS Board-approved definitions of “emerging manager” and “diverse manager,” survey participants will self-identify accordingly.

Emerging Manager and Diverse Manager Terms

AB 890 requires the Board to define the terms "emerging manager" and "diverse manager." CalSTRS currently has a definition for “emerging manager,” and it is asset class specific. CalSTRS does not have a definition for “diverse manager.” Staff is recommending the Committee approve the proposed modified definition of “emerging manager” and the inaugural definition of “diverse manager.” The proposed definitions were developed with the research and input from peer institutional investors, stakeholder groups, consultants, and emerging managers. In addition, there were numerous focused discussions conducted by staff to address the essence and spirit of AB 890.

As proposed, “emerging manager” and “diverse manager” terms are not synonymous as depicted below.

AB 890: Emerging & Diverse Manager Overview



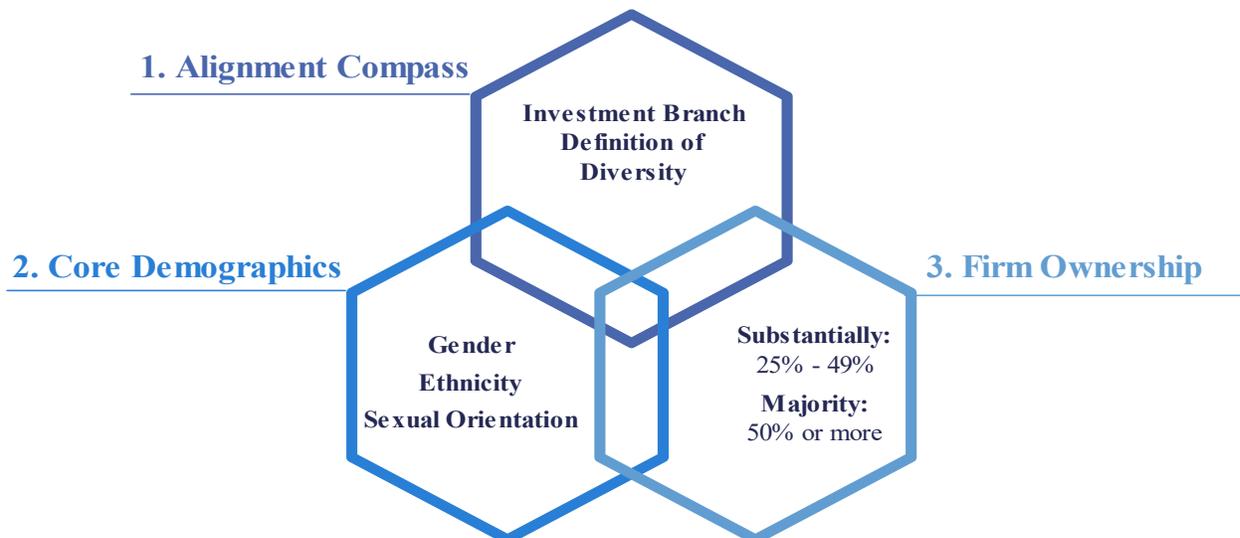
- **Emerging Manager** (Attachment 2). CalSTRS Investments proposes the term “emerging manager” continue to be based on minimum qualifications addressing: the amount of assets under management; fund lifecycle of funds; firm legal structure; non-employee ownership percentage; and other various factors including track record, private placement memorandum. The minimum qualification thresholds may vary across asset classes for reasons related to the nature of respective asset classes (e.g., private vs. public).
- **Diverse Manager Definition.** CalSTRS Investments believes diversity in firm ownership is critical to an organization’s ability to innovate and adapt in a fast-changing environment. Diversity is good for business, good for CalSTRS investments, and rapidly changing the demographic profile of the United States.

Applying CalSTRS Investments’ definition of diversity as a compass, Staff identified three core demographics (i.e., gender, ethnicity, sexual orientation) as diversity identifiers in forming the definition. As such, the proposed definition “diverse manager,” is based on firm ownership that meets one of the following tiered thresholds.

- Substantially Diverse: A firm that is 25 to 49 percent owned by women, ethnic minority group, and/or a person of the LGBTQ community
- Majority Diverse: A firm that is 50 percent or more owned by women, ethnic minority group, and/or a person of the LGBTQ group

Ethnic minority group members include individuals who are African American, Asian American, Hispanic American, or Native American, Pacific Islander, Other, and based on EEO-1 US Census classifications. LGBTQ community members include people who identify as Lesbian, Gay, Bi-sexual, Transgender, or Queer.

AB 890: Diverse Manager



Objective of Emerging Managers and Diverse Manager Participation

CalSTRS' mission is to secure the financial future and sustain the trust of California's educators. In support of the mission, Staff proposes the following objective related to the participation of emerging managers and diverse managers responsible for asset management within the system's portfolio.

- **Objective:** Consistent with its fiduciary duties, pursue and invest in emerging managers and diverse managers that generate performance that is aligned with the risk and return objectives of the applicable CalSTRS asset class.

RECOMMENDATION

Staff recommends the Investment Committee to approve the proposed definitions as required by the statutes of AB 890.

- "Emerging manager" definition; (Attachment 2)
- "Diverse manager" definition and
- "Objective" regarding the participation of emerging or diverse managers responsible for asset management within CalSTRS investment portfolio. (Refer to section above)

NEXT STEPS

Upon Investment Committee's approval of the recommendation, staff will proceed with the next steps of the AB 890 implementation plan, including the deliverable of a legislative mandated report no later than March 1, 2023.