

CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Senate Bill 1928 **Senator Haynes (As amended 5/9/00)**

Position: **Oppose**

Proponents: **CCPOA**

Opponents: **None known**

SUMMARY

SB 1928 encourages the Teachers' Retirement Board (TRB) and the Board of Administration of the California Public Employees' Retirement System (CalPERS) to not invest in foreign companies that may pose national security and human rights threats. The bill establishes a Capitol Markets Task Force Board to make recommendations to the respective retirement system boards on national security, human rights, and social concerns material to the performance of the systems' investments.

HISTORY

AB 2745 (Kaloogian), the California State Investment Transparency and Disclosure Act, encourages the California State Teachers Retirement System (CalSTRS) and CalPERS not to invest in foreign companies that pose a threat to national security and requires the respective boards to investigate and report annually, on or before January 15, to the Legislature regarding their investments in international corporations doing business in countries meeting specified criteria. The TRB adopted an Oppose position on this bill.

Chapter 341, Statutes of 1999 (SB 105—Burton) required CalSTRS to report on its investments in companies operating in Northern Ireland.

Chapter 216, Statutes of 1999 (SB 1245—Hayden) required CalSTRS to report on investments in companies that owe compensation to victims of slave and forced labor from 1929 to 1945.

SUMMARY OF LATEST AMENDMENTS

The May 9th amendments

- Prohibit members of the task force from direct personal involvement or economic interest in any financial transaction with CalSTRS and CalPERS while serving on the task force or for one year after the expiration of the member's term on the task force
- Provide that the task force will annually elect a chairperson
- Provide that the task force meets no less than quarterly

- Prohibit members of the task force from receiving a salary, compensation, or reimbursement for expenses related to their service on the task force
- Prohibit the task force from employing any permanent staff
- Specify that any expenses incurred by the task force will be paid in equal shares by CalSTRS and CalPERS

CURRENT PRACTICE

CalSTRS investments are managed by internal staff and a number of fund managers. The system's investment portfolio is diversified and includes real estate, fixed income and public and private equities. As of June 30, 1999 approximately 24 percent of the fund's investments are in international equities. About 50 percent of the system's international equity portfolio is passively invested to replicate various international stock indices.

The TRB follows a policy to support legislation and shareholder resolutions that "reduce social injury." In addition, its existing corporate governance policy is to consider social factors to the extent such factors bear on the financial advisability of the investment.

DISCUSSION

According to the author, the intent of the bill is to "address the scandal related to CalPERS foreign investments and those "bad actors" on the global scene, such as those responsible for the infliction of slavery and genocide in the Sudan." The bill is intended to apply only to international investments in foreign companies by CalSTRS and CalPERS.

SB 1928 establishes a task force to make recommendations on human rights, national security and social concerns that could be material to the performance of the systems' investments. The task force includes: the Governor, Speaker for the Assembly, Treasurer, Minority Leader of the Senate, Controller, Minority Leader of the Assembly, and the President pro Tempore of the Senate, or their respective designees.

SB 1928 is unclear on the types of recommendations the task force would make and on what basis. It appears that task force recommendations with respect to national security and human rights concerns would not be based on the impacts of these issues on investment performance. Given the fiduciary obligation of the TRB to act exclusively on behalf of all CalSTRS members and beneficiaries, any actions by CalSTRS board members also on the task force that resulted in a cost to the retirement fund would be inconsistent with that fiduciary duty. If the TRB acted on the basis of those recommendations, and the action turned out to be contrary to the fiduciary interests of CalSTRS members, the TRB members could be individually liable. Second, SB 1928 puts the Treasurer, the Controller, and the Governor in a position of sitting on a task force that makes recommendations to a board that they also are members or have representatives on. Third, prohibiting a task force member from having any financial interest in a transaction of either system would largely preclude the member from holding any investments, given the breadth of the holdings of the two systems.

FISCAL IMPACT

Benefit Program Costs – No impact on current benefit programs.

Administrative Costs – The bill provides that “any expenses” incurred by the task force will be paid in equal shares by CalSTRS and CalPERS. Presumably, task force members would want considerable information on any matters concerning national security, human rights and other social concerns, in order to make recommendations to the system. The cost of compiling that information could be significant.

The bill does not require any specific action by CalSTRS, however, to the extent that the TRB acts upon recommendations of the task force, significant investment costs could be incurred. For example, the failure to meet investment diversification goals in cases where the TRB follows task force recommendations, could lead to investment losses or result in significant transaction costs to the system.

POSITION

Oppose. The bill creates a task force with the authority to make recommendations to the TRB relating to national security, human rights, and social concerns, as these concerns impact investment performance. Recommendations from the task force to the TRB could conflict with the TRB's primary fiduciary responsibility to all CalSTRS members and their beneficiaries, a responsibility not shared by the task force.