BILL NUMBER: AB 1410 (Nazarian) as introduced February 27, 2015

SUMMARY

AB 1410 seeks to encourage the government of Turkey to acknowledge, and to reach resolution on reparations for survivors of, the Armenian Genocide by requiring the CalSTRS and CalPERS boards to divest of any investment vehicle issued by, owned, controlled or managed by the government of Turkey. This bill requires these boards, on or before January 1, 2017, and annually thereafter, to report to the Legislature any investments in a Turkish investment vehicle and the sale or transfer of those investments, subject to the fiduciary duty of these boards. It also indemnifies from the General Fund and holds harmless the present, former and future board members, officers and employees of and investment managers under contract with those retirement systems.

BOARD POSITION

Oppose. The board's policy is to oppose legislation that restricts its ability to invest in specific areas because, as described in its divestment policy, such restrictions could impair the board’s ability to exercise its fiduciary obligation to act exclusively for the benefit of the retirement plan members and beneficiaries. The board has a policy by which it evaluates potential divestment of assets, utilizing 21 Risk Factors that are part of the board’s Investment Policy for Mitigating Environmental, Social and Governance risks. There is no indication that investments in securities affected by AB 1410 violate any of the 21 Risk Factors.

REASON FOR THE BILL

According to the bill’s author, Turkey violates the human rights of Armenians by continuing to deny the 1915 genocide of Armenians.

ANALYSIS

Existing Law:

Under the provisions of Section 17 of Article XVI of the California Constitution, as amended by Proposition 162 of 1992, the CalSTRS board has plenary authority and fiduciary responsibility over the investment of retirement plan assets and is required to discharge its duties solely in the interests of the members and beneficiaries for the exclusive purpose of providing benefits. The board must invest the assets of the plan with the care, skill and diligence of a prudent person engaged in a similar enterprise so as to maximize the investments and minimize the risk of loss. When considering investments, the preservation of principal and maximization of income is the primary and underlying criteria for the selection and retention of securities. The Constitution states, however, that the Legislature may by statute prohibit certain investments by a retirement board when it is in the public interest to do so and provided the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board.

While there have been numerous bills and resolutions that recognized the Armenian Genocide, there are no existing California laws that require divestment from any investment vehicle issued by, owned, controlled or managed by the government of Turkey.

This Bill:

Specifically, AB 1410:

- Prohibits the board from investing in any investment vehicle issued by, owned, controlled or managed by the government of Turkey;
- Requires the board to determine which Turkish investment vehicles are subject to divestment on or before June 30, 2016;
- Specifies how the board shall address externally and actively managed comingled funds and private equity investments that may include Turkish investment vehicles.
- Requires the board to request those Turkish investment vehicles that are subject to divestment to make sufficient progress to disassociate themselves from the government of Turkey within 90 days and to take substantial action to do so within one year;
- Requires the board to liquidate investments in Turkish investment vehicles that the board determines have not taken substantial action to disassociate with the government of Turkey within 18 months after such a determination provided that doing so is consistent with its fiduciary responsibilities;
- Requires the board to report to the Legislature on or before January 1, 2017, and annually thereafter, including the following information:
    - A list of investments in Turkish investment vehicles,
    - The association between the investment vehicle and the Turkish government,
    - Reductions in Turkish investment vehicles,
    - When the investments will be reduced or the reason why the investments will not be reduced because to do so would be inconsistent with the board’s fiduciary responsibilities,
    - Investment vehicles that are found to not be Turkish investment vehicles and investments in externally and actively managed comingled funds and private equity investments that were transferred to be devoid of Turkish investment vehicles, and
    - An annual calculation of any costs or investment losses due to compliance; and
- Indemnifies from the General Fund and holds harmless the present, former and future board members, officers and employees of and investment managers under contract with those retirement systems.

LEGISLATIVE HISTORY

SB 185 (De León, 2015) would require the CalSTRS and CalPERS boards to engage with thermal coal companies, as defined, and to divest the public employee retirement funds of any investments in thermal coal companies; would prohibit additional or new investments or the renewal of existing investments in thermal coal companies; and would require an assessment of the feasibility of divesting from additional fossil fuel investments, such as natural gas and petroleum.

H.Res.154 (Dold, 2015) would call on the United States President to work toward equitable, constructive, stable and durable Armenian-Turkish relations based upon the Republic of Turkey's full acknowledgment of the facts and ongoing consequences of the Armenian Genocide and a fair, just and comprehensive international resolution of this crime against humanity.

S.Res. 410 (Menendez, 2014) would have expressed the sense of the United States Senate: (1) in remembrance of the anniversary of the Armenian Genocide on April 24, 2014, and (2) that the United States President should ensure that U.S. foreign policy reflects appropriate understanding and sensitivity concerning issues related to human rights, crimes against humanity, ethnic cleansing and genocide documented in the U.S. record relating to the Armenian Genocide. This resolution was held on the Senate Floor.

AB 761 (Dickinson, 2013) would have prohibited CalSTRS and CalPERS from investing in companies that manufacture firearms or ammunition for a recipient other than the U.S. military, subject to a process specified in the bill and consistent with previous divestment legislation, but subject to the board's fiduciary duties. This bill was held in the Assembly Appropriations Committee.

SR 18 (Leno, Adopted, 2013), in response to the Russian government taking an aggressive course of action to pass laws targeting the lesbian, gay, bisexual and transgender (LGBT) community, strongly encouraged CalSTRS and CalPERS, whenever feasible and consistent with their fiduciary responsibilities, to cease making direct investments in Russia and to encourage companies in which employee retirement funds are invested and that are doing business in Russia not to take actions that promote or otherwise enable human rights violations in Russia.

AB 1151 (Feuer, Chapter 441, Statues of 2011) required that any determination by CalSTRS that an action, as specified in the California Public Divest from Iran Act, fails to satisfy the fiduciary duty of the board be made in a properly noticed public hearing of the full board and that proposed findings be made public 72 hours before they are considered by the board.

AB 221 (Anderson, Chapter 671, Statues of 2007) enacted the California Public Divest from Iran Act prohibiting CalSTRS and CalPERS from investing in companies with business operations in Iran and requiring each pension system to sell or transfer any investments in a company with business operations in Iran. Required, when the U.S. repeals its sanctions against Iran, the pension boards notify the Secretary of State and the prohibitions and requirements in this bill be repealed.

AB 2941 (Koretz, Chapter 442 Statues of 2006) prohibited CalSTRS and CalPERS from investing in companies with business operations in Sudan that are complicit in the Darfur genocide or have specified relationships with the Sudanese government or military and required the boards of both retirement systems to divest from such companies, consistent with their fiduciary obligations.

SB 424 (Poochigian, Chapter 9, Statutes of 2005) established April 24 of each year as the "California Day of Remembrance of the Armenian Genocide" and the period beginning on the Sunday before that day through the following Sunday as the days of remembrance of the Armenian Genocide.

SJR 2 (Speier, Resolution Chapter 22, Statutes of 2005) designated April 24, 2005, as the "California Day of Remembrance for the Armenian Genocide of 1915-1923" and also memorialized the United States Congress to act likewise to commemorate the Armenian Genocide.

AB 107 (Knox, 2000) would have prohibited new or additional investments in tobacco companies by CalSTRS and CalPERS on and after January 1, 2001, and would have required divestment from existing investments by July 1, 2002. This bill was held in the Assembly with concurrence pending.

PROGRAM BACKGROUND

ESG Policy

CalSTRS has its own well-established and longstanding process for thoroughly vetting the environmental, social and governance risks of potential investments. The board adopted its Statement of Investment Responsibility in 1978, making CalSTRS an industry leader as one of the first pension funds to adopt a written policy to navigate these complex issues. In its latest incarnation, the board developed a list of 21 Risk Factors as part of its Investment Policy for Mitigating ESG Risks. The 21 Risk Factors help the board to identify and evaluate investment risks relating to the existence of certain conditions, such as recognition of the rule of law, shareholder rights, human rights, the environment, acts of terrorism and other unsustainable practices and governance crises with the potential to hurt long-term profits.

Divestment Policy

In addition to the CalSTRS ESG policy, the board has adopted a divestment policy to respond to external or internal initiatives to divest of specific companies or industries. In accordance with this policy, CalSTRS has historically taken the position that active and direct engagement is the best way to resolve issues. Divestment bears the risk of adversely affecting an investment portfolio and severs any chance to advance positive change through shareholder advocacy. Face-to-face meetings with shareowners and senior management, or the board of directors, are generally more effective in bringing about change in a corporation. Under the policy, the board will only consider divestment after all efforts at engagement have failed, and only then in cases where at least one of the 21 Risk Factors is violated over a sustained timeframe to the extent that it becomes an economic risk to the fund, creates a potential for material loss of revenue and weakens the trust of a significant portion of CalSTRS members. Finally, the divestment policy sets forth that the board will only instruct staff to divest of a security when it determines that continuing to hold a security is imprudent and inconsistent with its fiduciary duty.

Armenian Genocide

The Armenian Genocide is largely believed to have begun on April 24, 1915, when hundreds of Armenian intellectual, political, religious and business leaders were arrested and deported from Constantinople. In acknowledgment of its 90th anniversary, California enacted Chapter 9, Statutes of 2005 (SB 424–Poochigian), to recognize the

Armenian Genocide as a series of events occurring between 1915 and 1923 in which the rulers of the Ottoman Turkish Empire and its successor state, the Republic of Turkey, subjected its Armenian citizens to torture, starvation and murder. The rulers conducted massacres of able-bodied Armenian men. Additionally, the Ottoman Turkish rulers forced Armenian women, children, elderly and infirm to march from their homeland to the Syrian Desert. Approximately 75 percent of those Armenian people on these marches died. Between 1 million and 1.5 million Armenian people were killed during the three year period from 1915 to 1918. Other groups of Turkey's minority Christian population were killed during this period along with the Armenians, including Greeks and Syrians. Successive Turkish governments have failed to acknowledge the Armenian Genocide and have even lobbied other governments, organizations and institutions to prevent the genocide from being discussed or included in educational curricula.

OTHER STATES' INFORMATION

As of 2013, no other state has enacted legislation related to divestment from any investment vehicle issued by, owned, controlled or managed by the government of Turkey.

FISCAL IMPACT

Program Cost – CalSTRS exposure to debt securities issued by the government of Turkey is approximately $21 million. Global equities and innovation and risk investments subject to divestment have a potential combined market value of up to $210 million. CalSTRS may incur opportunity costs if suitable alternative investments are unavailable or if such alternative investments do not provide an investment return that meets or exceeds those of the divested securities. Any resulting costs would increase the unfunded liability and also may result in an increase in the state's contribution to the Defined Benefit Program.

Administrative Costs/Savings – Approximately $405,100 initial costs and $43,200 annual ongoing costs resulting from transaction costs for liquidating securities and additional costs related to external research services. Implementation and ongoing compliance will also require reallocation of staff resources.

SUPPORT

None known.

OPPOSITION

None known.

ARGUMENTS

Pro: Could eliminate the perception that CalSTRS is contributing to a continuing denial of Armenian Genocide by Turkey.

Con: May infringe upon the investment authority of the board.

May reduce the investable universe and adversely affect portfolio performance.

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