**BILL NUMBER: AB 1735 (Wieckowski) as amended March 19, 2012**

## SUMMARY

AB 1735 authorizes the Teachers' Retirement Board (board) to establish the desired competencies, set conditions of employment and performance standards, and establish the compensation, as specified, for the Chief Operating Officer (COO) (currently designated as Chief of Staff) and Chief Financial Officer (CFO), and allows the board to recruit for these positions from broader sources.

## BOARD POSITION

**Sponsor.** Expanding the board's authority is consistent with the board's commitment to improve the delivery of benefits and services and to provide more effective and efficient administration of the retirement plan.

## SUMMARY OF AMENDMENTS

The March 19, 2012, amendments:

- Limit the salary for the COO and CFO to 150 percent of the Governor's salary.
- Make technical changes.

## PURPOSE OF THE BILL

This bill seeks to enhance CalSTRS ability to preemptively plan for the succession of vulnerable top level executive positions, particularly those responsible for managing the increasingly complex financial and operational components of the largest teacher pension fund in the nation. This bill also seeks to improve CalSTRS ability to attract and retain employees for key executive positions that require specialized and critical expertise and competencies, as well as set executive compensation that is consistent with compensation paid for comparable services within selected peer groups that include the private financial service sector and other public retirement systems.

## ANALYSIS:

### Existing Law:

Under current law, recruitment for most CalSTRS executive level classifications is limited to the state civil service candidate pool. This limitation constrains CalSTRS ability to recruit highly qualified candidates very likely to exist in the private sector or with other public entities that possess essential depth and breadth of specialized knowledge, skills, abilities and competencies required for positions responsible for overseeing and leading vital operational, administrative and financial activities of the organization.

In the past, recognizing the difficulty of recruiting experienced senior pension and investment staff, the Legislature provided the board authority to establish position specifications and set compensation for certain key positions. Currently, the board has flexibility in recruiting and compensating senior investment and actuarial staff and has authority to establish position specifications and set compensation for the Chief Executive Officer (CEO), System Actuary, Chief Investment Officer (CIO), General Counsel and designated managerial investment officers and portfolio managers. Conversely, as noted previously, recruitment for both the COO and CFO is subject to the state civil service standards and classifications. There are other state agencies that have been granted authority to establish classes of positions and set compensation in order to attract and retain highly qualified employees and meet the needs of the agency.

**This Bill:**

AB 1735 gives the board authority to establish desired competencies, performance standards and compensation for the vital positions of the COO and CFO, along with the ability to recruit from external sources. This authority allows the board to competitively recruit from a larger and more highly qualified candidate pool. AB 1735 limits the salaries of the COO and CFO to 150 percent of the Governor's salary, which equates to a maximum of just under $261,000.

## LEGISLATIVE HISTORY

AB 2260 (Committee on Public Employees, Retirement and Social Security, Chapter 207, Statutes of 2010) clarified which executive level staff are restricted from performing post-employment activities that influence various actions and proceedings of the board.

AB 1584 (Hernandez, Chapter 301, Statutes of 2009) expanded the prohibition on high level officers and investment staff, who had been in those positions for less than five years, from acting as agents before the board or staff for a period of two years after leaving the retirement system, by removing the five year limitation and including board members, deputy executive officers and assistant officers as staff subject to these provisions.

AB 1317 (Mullin, Chapter 333, Statutes of 2007) authorized the board to determine compensation for the general counsel position.

AB 224 (Negrete McLeod, Chapter 351, Statutes of 2005), among other provisions, specified that the CEO, System Actuary, CIO and investment mangers do not receive annual Merit Salary Adjustments.

SB 269 (Soto, Chapter 856, Statutes of 2003) allowed the board to determine the compensation of certain actuarial and investment positions and provided these determinations must be guided by the principles contained in statutes governing the creation of salary ranges for each class or position.

## PROGRAM BACKGROUND

Financial and investment transactions of public pension plans have more complicated regulatory requirements associated with them, and the responsibility to understand those transactions has increased significantly over the past several years. Moreover, the ongoing debate over public and private retirement security has intensified with the volatility of financial markets, and demands a greater understanding of the political and social environment in which public pension plans operate. In addition, stakeholders and the general public expect greater transparency and accountability in public pension plans. Finally, recent independent financial reports and audit quality assurance reviews indicate weaknesses in procedures and internal controls within CalSTRS. Addressing these issues by CalSTRS requires the focused attention of senior executive management. The COO and CFO are the CalSTRS senior management most responsible for managing these issues in the organization.

One of the board's top strategic objectives is to address and proactively plan for the succession of the CEO and other key senior executive staff. The board recognizes the value of retaining institutional knowledge by developing potential successors internally. Internal succession of the CEO, as desired by the board, would likely come from the COO, CFO and/or the CIO, and therefore, the skills of the incumbents must be on par with those of the CEO. Additionally, in leading all of the operational and administrative functions of CalSTRS, the COO has immense accountability for the management of risk. Moreover, the CFO is responsible for leading all financial activities, which includes pension financial accounting and analysis, investment analysis and all financial system activities. Both positions require specialized knowledge, skills and competencies in order to effectively carry out the complex duties of the positions.

Proper business operations require that the increased needs of the organization be reflected as CalSTRS develops its succession strategy. When recruiting for these positions, it is very likely that the most highly qualified candidates would come from large financial institutions in the private sector, endowments or other large public pension systems. However, under existing state civil service laws, CalSTRS is limited to recruitment for these positions from the state civil service candidate pool where required competencies are much less likely to exist.

## FISCAL IMPACT

Program Cost – No impact on benefit costs.

Administrative Costs/Savings – Unknown savings based on future financial and operational risk avoidance due to board's increased ability to attract, recruit and retain the most highly qualified employees, preemptively plan for succession and ensure that staff with skills requisite for managing risk and overseeing vital operational, administrative and financial functions are in place in order to secure the financial future of CalSTRS.

## SUPPORT

CalSTRS

## OPPOSITION

None known.

## ARGUMENTS

Pro: Increases CalSTRS ability to attract, recruit and retain staff with highly specialized knowledge, skills and competencies requisite to the vital leadership positions of the COO and CFO.

Enables CalSTRS to recruit from a larger candidate pool for the critical expertise needed for these positions.

Supports CalSTRS succession planning efforts.

Provides more effective and efficient administration of the retirement plan and assures the prompt delivery of benefits and related services.

Assists the board in meeting its fiduciary obligation in retaining employees in key senior executive and management positions and in securing the financial future of CalSTRS.

Con: May be viewed as a compensation issue and, therefore, be problematic at this time given the heightened attention to and scrutiny of public pension systems and the ongoing pension reform debate.

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