

Bill Number: AB 17 (Davis) as amended on May 11, 2011

SUMMARY

AB 17 requires CalSTRS to define the terms emerging investment manager and emerging broker firm by regulation and to report to the Legislature annually on or before August 1, 2012 on the ethnicity and gender, as specified, of investment managers who participated in managing the CalSTRS external fund management contracts and brokerage firms which provided brokerage services to the fund's internally and externally managed portfolio in the immediate preceding fiscal year. CalSTRS is also required to develop and report to the Legislature a plan and strategy for participation of emerging investment managers and brokerage firms as specified by the bill. This provision would expire on January 1, 2018.

PURPOSE OF THE BILL

AB 17 is intended to encourage equal opportunity and participation of women and minority-owned business in the management of pension fund assets. AB 17 aims to support economic growth and prosperity in California through inclusion and requires California's pension systems to develop a plan for using emerging managers in the management of pension fund assets that are consistent with the system's fiduciary duties and responsibilities.

BOARD POSITION

Neutral. It is the policy of the Board to be neutral on legislation that does not significantly or adversely impact the benefits or services through the funds administered by CalSTRS or the administration of the retirement plans.

SUMMARY OF AMENDMENTS

May 11, 2011 amendments:

- Removed the requirement that CalSTRS include in its report plans and strategies to increase the participation of emerging investment managers and brokerage firms, as specified, that are internally and externally managed by investment managers that manage publicly traded and include highlights of those firms that are at least 51 percent minority or woman owned.
- Removed the emerging investment manager and emerging brokerage firm definitions.
- Requires CalSTRS to report to the Legislature on the ethnicity and gender for the investment managers with whom it has contracted in the immediately preceding fiscal year.
- Added language specifying that the requirement to identify investment firm ownership should be restricted only to privately held firms, and the breakdowns of investment officer composition by firm should be restricted to those managers who participate in the management of CalSTRS portfolios.

- Requires the CalSTRS board to define emerging investment manager and emerging brokerage firm by regulation

LEGISLATIVE HISTORY

AB 1913—Davis (Held in Committee 2010) required the board report on the ethnicity and gender of investment managers who participated in managing CalSTRS' portfolio and develop and include plans and strategies to increase the participation of these classes of managers until such managers managed at least 10 percent of the board's actively managed portfolio.

Chapter 320, Statutes of 2000 (SB 2122—Ortiz) authorized and encouraged CalSTRS and CalPERS to cooperate and share information that may assist them in developing and implementing appropriate investment strategies, with the advice of investment experts, as specified. Specified that confidential information or documents relating to investments in the possession of either system would not lose their confidential status due to the fact that the information or documents are shared with the other system or with investment advisors.

Chapter 9, Statutes of 2000 (AB 869—Keeley) established a Community Reinvestment Act for California insurers by creating an affirmative obligation for insurers to invest in low-income communities. Made legislative findings that California Organized Investment Network (COIN) in the Department of Insurance (DOI) efforts to encourage insurer commitment to safe investments that benefit low-income communities have resulted in insufficient economically targeted investments; that IMPACT Community Capital, a for-profit insurance industry investment intermediary designed to make economically targeted investments, has also resulted in insufficient investments in comparison to the amount of premiums collected in the state. Established an affirmative and continuing obligation for California insurers to make economically targeted investments in low-income communities.

PROGRAM BACKGROUND

Pension funds around the country have recently begun pursuing strategies to increase the diversity of their investing managers, recognizing these emerging managers as a source of untapped economic value. In this vein, the CalSTRS board and staff have been pursuing strategies to expand the diversity of investment management, both internally and externally. In 2003, the board adopted Strength as one of CalSTRS Core Values, elaborated as ensuring the strength of CalSTRS by embracing a diversity of ideas and people, and set forth an objective to increase the diversity of investment managers, by focusing efforts on emerging managers. CalSTRS defines an emerging manager in terms of the size and longevity of the fund managers, without regard to gender or ethnicity. As a direct result of this effort, women and minorities now manage more than \$3 billion of assets for CalSTRS. CalSTRS has received national recognition, including several awards, for its efforts and actions to expand diversity within its investment portfolio and is seen as an industry leader and best practice model.

This dedication to diversity has brought about the development of a business plan to formalize the commitment to diversity within CalSTRS investment portfolio, and to make a statement to the industry that this is a long-term effort. The business plan is designed

to provide the Investment Committee, investment staff, and external consultants a plan of action for the next five years. The purpose of this business plan is to formalize the programs CalSTRS currently has in place, to set new goals, and establish a long-term plan. Diversity will be further interwoven across CalSTRS' entire investment portfolio and program—thus, making it a truly comprehensive plan.

ANALYSIS:

Existing Law:

Proposition 162, The California Pension Protection Act (Act), amended the State Constitution in 1992 and grants the board of the state's public employee retirement systems sole and exclusive fiduciary authority and responsibility over the assets of the public pension system. The Act provides that the retirement board shall have sole and exclusive responsibility to administer the system in a manner that is consistent with those exclusive fiduciary responsibilities and duties.

The Act also grants that the Legislature, by statute, may continue to prohibit certain investments by a retirement system when it is in the public interest to do so, provided that the prohibition satisfies the standards of fiduciary care required of the retirement system.

This Bill:

AB 17 requires CalSTRS to define the terms emerging investment manager and emerging brokerage firm by regulation and to report to the Legislature annually on or before August 1, 2012 on the ethnicity and gender, as specified, of investment managers who participated in managing the CalSTRS external fund management contracts and brokerage firms which provided brokerage services to the fund's internally and externally managed portfolio in the immediate preceding fiscal year. CalSTRS is also required to develop and report to the Legislature a plan and strategy for participation of emerging investment managers and brokerage firms as specified by the bill. This provision would expire on January 1, 2018.

If AB 17 were enacted CalSTRS would need to obtain the necessary information needed for the annual mandated reports to the Legislature. CalSTRS is capable of collecting most of the information requested at an annual cost of approximately \$50,000. The measure requires CalSTRS to identify a privately held investment firm's ownership composition and to report on the gender and ethnic composition of firms that managed a portion of CalSTRS' portfolio and contracted with them in the immediately preceding fiscal year.

CalSTRS has been working diligently to increase participation of women and minorities in the management of its investments in accordance with its fiduciary responsibility. This has been done in a neutral way that affords opportunities without making distinctions based upon race or gender. CalSTRS plans to continue its practice of increasing diversity through the normal course of business in conjunction with the investment goals aimed to achieve the maximum return at a prudent level of risk and in accordance with its fiduciary responsibilities. CalSTRS' current investment policies seek to address the historic inequities of disadvantaged groups in a neutral manner. As a result, although

CalSTRS would report the information as required by AB 17 if the bill is enacted, CalSTRS will manage its emerging manager program in accordance with the policies established by the board.

FISCAL IMPACT

Program Cost – None.

Administrative Costs/Savings – One time cost of approximately \$3,000 to develop a form and for database modification to capture data elements. Ongoing costs associated with annual reporting are approximately \$70,000.

SUPPORT

California State NAACP (Sponsor)

OPPOSITION

N/A

SUPPORTING ARGUMENTS**PROS:**

- Encourage participation of women and minorities in the management of CalSTRS investments.

CONS:

- Staff time will be necessary to track the required reporting criteria

LEGISLATIVE STAFF CONTACT

Melissa Gear
Legislative Advocate,
CalSTRS Legislative Affairs,
(916) 414-1982
mtanner@calstrs.com

Mary Anne Ashley
Acting Director,
CalSTRS Governmental Affairs and Program Analysis,
(916) 414-1981
mashley@calstrs.com