BILL NUMBER: SB 783 (Pan) as amended June 14, 2018

SUMMARY

SB 783 makes a request by the Legislature to the University of California to establish the Pension Divestment Review Program to assess, at the request of specified legislative parties, any legislative proposal for the divestment or restriction of pension fund investments and prepare a written analysis containing relevant data, as prescribed, regarding the effects of the proposal on public employee pension funds and public policy.

BOARD POSITION

Oppose. The board voted to oppose this bill out of concern that the proposed program would not have the knowledge of CalSTRS and its investment policies necessary to effectively evaluate the impact of legislative proposals regarding divestment and that its work could be considered duplicative of the CalSTRS own analysis.

REASON FOR THE BILL

As stated in the findings and declarations, there are an increasing number of legislative proposals seeking to require or pressure public employee pension funds to divest from or restrict specified investments. These proposals can often result in increased costs and reduced returns to a public employee pension system, which is inconsistent with the fundamental purpose of the system to maximize investment returns in order to ensure the payment of pension benefits. Additionally, divestment proposals are often ineffective methods of conveying California's concerns about public policy.

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 also states 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.

Current law, Education Code section 22330, also requires the board to provide the Legislature with an analysis of the asset and liability implications of each bill that would affect the investment strategy of the system, the funding of the plan, or the benefit structure of the plan and stipulates that neither fiscal committee of the Legislature can hear the bill until the analysis has been provided to the committee.

This Bill:

Specifically, SB 783:

- Makes a request by the Legislature to the University of California to establish the Pension Divestment Review Program to assess divestment proposals.
- Defines “divestment proposal” as a bill or constitutional amendment, introduced or amended in the Legislature that would require a public employee pension fund to divest assets or restrict the fund from investing based on specific criteria or by reference to an external benchmark.
- Specifies that a request to the program to assess a divestment proposal may be made by the chairperson of the Assembly PER&SS Committee, the chairperson of the Senate PE&R Committee, the Speaker of the Assembly or the President pro Tempore of the Senate.
- Stipulates the written analysis will contain relevant data, as prescribed, with respect to the proposals effect on public employee pension funds and public policy.
- Requires the program to use the services of a certified actuary or other person with relevant knowledge and expertise to determine the financial impact, as recommended by the California Actuarial Advisory Panel.
- Requires the program to collaborate with experts in the public pension fund investment profession and use the university’s resources that specialize in providing objective financial and policy analysis of complicated policy and economic issues.
- Requires the program to provide its written analysis to the appropriate policy and fiscal committees of the Legislature no later than 60 days after receiving a request and to make the analysis publicly available.
- Establishes the Pension Divestment Review Program Fund in the State Treasury and specifies the moneys in the fund, upon appropriation by the Legislature, are to be available to support the program.
- Appropriates $2 million from the General Fund to the Pension Divestment Review Program Fund for the 2018-19 fiscal year and notes that it is the intent of the Legislature that future appropriations to the fund shall be part of the annual budget act.
- Requires the program to submit a report to the Governor and the Legislature on or before January 1, 2020, regarding implementation of the bill.
- Specifies that this bill does not require the board to take any action unless it is consistent with its fiduciary responsibilities as described in Section 17 of Article XVI of the California Constitution.

Generally, the board opposes legislative efforts to restrict 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. CalSTRS has policies and procedures in place for thoroughly vetting and assessing investment risks, works with its external managers to recognize and manage the risks and, where appropriate, directly engages with portfolio companies.

This legislation is intended to establish a dispassionate, analytical process using clear criteria to evaluate divestment proposals for effectiveness, both in terms of cost and achievement of the intended policy objective, and to identify the effect on public pension funds. The method would be similar to the existing process under the California Health Benefit Review Program (CHBRP) to evaluate legislative proposals to mandate health insurance coverage and would assist in ensuring the Governor and the Legislature receive current, accurate data and information when considering a divestment proposal.

The bill declares that pension fund engagement strategies are often an effective means by which pension fund trustees or representatives are able to reduce economic and political risk to the fund. In accordance with CalSTRS divestment policy and consistent with fiduciary responsibilities, the goal of CalSTRS engagement activities must always be to resolve or mitigate issues that pose an economic risk to the fund, not to influence policies unrelated to economic considerations.

LEGISLATIVE HISTORY

AB 1996 (Thomson, Chapter 795, Statutes of 2002) requested, until January 1, 2007, that the University of California (UC) assess legislation proposing mandated health care benefits and prepare a written analysis as specified. Requested the UC to develop and implement conflict-of-interest provisions. Provided up to $2 million in funding from annual fees imposed on health care service plans and insurers. Requested the UC report to the Governor and the Legislature by January 1, 2006, on the bill's implementation.

SB 1704 (Kuehl, Chapter 684, Statutes of 2006) requested, until January 1, 2011, that the UC establish CHBRP to assess legislation proposing mandated benefits or services or proposing to repeal mandated benefits or services and to prepare a written analysis as specified. Authorized the continued assessment of fees.

SB 125 (Hernandez, Chapter 9, Statutes of 2015) requested, until June 30, 2017, that CHBRP assess legislation affecting health insurance benefit design, cost sharing, premiums and other health insurance topics and requested that the impact on essential health benefits and the California Health Benefit Exchange be included in the analysis. Authorized the continued assessment of fees.

AB 114 (Budget, Chapter 38, Statutes of 2017) extended the operation of CHBRP until July 1, 2020, and authorized the continued assessment of fees.

PROGRAM BACKGROUND

ESG Policy

CalSTRS has its own well-established and longstanding process for thoroughly vetting the environmental, social and governance (ESG) risks of potential investments set forth in the board's Investment Policy for Mitigating ESG Risks. As a key component of that process, the board has developed a list of 21 Risk Factors, which help staff to identify and evaluate investment risks relating to the existence of certain conditions with the potential to hurt long-term profits.

Divestment Policy

In addition to the CalSTRS ESG policy, the board has adopted a divestment policy, focusing on engagement, to respond to external or internal initiatives to divest of specific companies or industries. 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.

The funded status of the system is not taken into consideration in divestment proposal decisions, rather the overall risk and potential impact to the investment portfolio is evaluated and considered. 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.

FISCAL IMPACT

Program Cost – None identified.

Administrative Costs/Savings – None identified.

SUPPORT

Association of California School Administrators
California Retired Teachers Association
California State Association of Counties
California State Retirees
California Teachers Association

OPPOSITION

CalSTRS
CalPERS
California State Controller
350 Bay Area

ARGUMENTS

Pro: Creates an objective, analytical process for evaluating divestment proposals in order to provide the Governor, Legislature and all interested parties with current, accurate data and information when considering the proposal.

Con: Connects the funded status to divestment decisions when investment decisions must maximize the investments and minimize the risk of loss without regard to funded status.

Creates a program that may not have the knowledge of CalSTRS and its investment policies necessary to effectively evaluate the impact of legislative proposals regarding divestment.

Potentially duplicates the work of CalSTRS own analysis.

LEGISLATIVE STAFF CONTACT

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