CalSTRS Report for July 2019
By Pat Geyer, CalRTA Representative to CalSTRS

Summary

1. The Investment Committee consensus was to plan for a 6.75% or 7% return on investments. The Investment Policy and Management Plan was approved.
2. The Committee heard public comments from members from the Oakland city schools who were concerned with the climate change and requested that CalSTRS divest from fossil fuels.
3. The CalSTRS fund was $236.9 billion, a record high.
4. The Board heard the Pension Solution computer project update. The cost through the end date of February 2022 is $304.8 million.
5. Construction on the Headquarters Expansion Project will begin in August, so the next CalSTRS Board meeting will see the beginning of the project.

Audits and Risk Management Committee

The Committee heard a progress report on the independent financial statement Auditor’s Letter. The letter reported three deficiencies of internal controls. (1) Completeness and accuracy of member data. Management plans to implement the New File Format and penalty and Interest visibility. (2) Enhance the member data risk/control. Management is developing a new approach to member data. The risk management training class is expected to be complete and disseminated by the end of 2019. (3) Audit Services continue to execute its proposed 2918 audit plan. This program is completed. (4) Unfunded Commitments - maintain an unfunded commitment listing. Management considers this completed.

The Committee heard a progress report on the 2019 Internal Audit. Staff completed 24 of the 84 audits of school districts. 70 audits are still in progress. The common audit findings are: (1) un-reported post retirement earnings (45% of the audits), (2) misreported earnings (81% of the audits), and (3) misreported unused sick leave/excess sick leave (54% of the audits). CalSTRS continues to work with school districts to help prevent data problems.

Client Advisory Committee

Joycelyn Martinez-Wade presented the Legislative update:

AB33 (Bonta) which prohibits CalSTRS and CalPERS from making additional investments in a private prison company, is held in the Assembly. (CalSTRS opposes AB33).
AB181 and AB462 (Rodriquez) requires CalSTRS and CalPERS to submit annual report on the status of participation of emerging managers within the systems’ investment portfolios, is in the rules committee. (CalSTRS supports AB181 and AB 462).

AB 462 (Rodriguez) requires CalSTRS and CalPERS to submit an annual report on status of participation of emerging managers within the investment portfolios. (CalSTRS supports, bill in the Rules Committee).

AB706 (Low) removes the 3-year limit within which an employee of a community college district must transfer unused sick leave to another employer. Bill sent to Governor.

AB1452 (O’Donnell) makes changes to provisions regarding membership in the Defined Benefit Program and Cash Balance Benefit Program. (CalSTRS sponsor) Bill held in the suspense file.

June Kim gave a report on the Investment Workforce which is working to get diversity in Wall Street and to get gender equality in hiring. It holds workshops for high school and college students and also works with investment managers.

**Compensation Committee**

The following are administrative changes: (1) Innovative Strategies and Risk has been moved to Director of Strategy and Risk rather than under the Director of RMS, Innovation& Risk. (2) Performance criteria and benchmark for Infrastructure has been eliminated. It will be in other Real Assets and measured under Inflation Sensitive. (3) Performance criteria for Engagement will include the Associate Portfolio Manager classification. (4) Private Equity definition has been updated to reflect best measurement for added value.

The Committee heard a discussion of better aligning the Compensation Program with the Collaborative Model. (1) Align better with performance, (2) Emphasis on long-term and beyond 3 years, (3) Include appropriate measures. Chris Ailman explained that costs are more complicated with such investments as real estate. The challenge is how to apply income from investments such as real estate and stocks to CalSTRS staff. Part of staff pay may come from investment returns.

**Investment Committee**

The Committee heard a report on Asset Allocation. The presentation discussed different investment portfolios, reviewed different returns and the liability implications. The Investment Committee consensus was to plan for a 6.75% or 7% return on investments.

Next the Committee heard a report on the 2019-20 business plans. It is projected that the management costs will increase; however, by bringing more investments “in house” rather than hiring outside managers CalSTRS will keep the cost increases down. Present, 2018-19 CalSTRS investment management costs are approximately $225,000,000. That is an increase from $125,000,000 in 2003-4. Discussion followed. Concerns were that by bringing management “in house” CalSTRS might not get some good deals. The CalSTRS Investment Business plan was approved.
The Investment Policy and Management Plan was approved. Generally, wording was brought up-to-date of present policy. In the California Investments Policy the State Law sections were deleted. Chris Ailman, Chief Investment Officer was reluctant to have the State Law sections deleted because one does not know when State Law will change.

The Committee heard public comments from members from the Oakland city schools who were concerned with the climate change and requested that CalSTRS divest from fossil fuels.

The Private Equity Policy’s long term benchmark was changed from the Russell 3000 to the Morgan Stanley Capital International (MSCI) All Country World Index. This better represents the global nature of the Private Equity asset class.

Chris Ailman, Chief Investment Officer reported that the CalSTRS fund was $236.9 billion, a record high. The CalSTRS fund is “on target” with asset allocation. Returns have been good, but interest rates have been flat – no changes. The key risks are China and U.S. trade.

The 10 student interns working at CalSTRS were introduced. They are from local (mainly) and other major universities.

A proposed Risk Budget was discussed. A risk budget specifies a targeted level of risk or variation relative to a benchmark. It could apply to the total fund or to individual asset classes.

Employees from the Hotel Marriott spoke about their labor relations concerns.

**Teachers’ Retirement Board**

The Board considered amendments to the format for monthly reports (Pension Solution computer project). The following is a summary of the comments received and staff response. (1) Increased cost to school districts and county offices due to the system change. CalSTRS staff recommends an additional waiver period of 6 months for districts to make the change. (2) Leaves of absence requirements unclear. CalSTRS staff affirms that the language does not create additional obligations. When the leave type of absence is unknown put information is “Other Approved Leave of Absence”. (3) Annual Total Compensation field had concerns. CalSTRS staff recommends an amendment which affirms that the regulations do not create any additional obligations for employers. (4) The list of Service Types is not complete. Staff recommends clarifying by referencing the Educations Code. (5) Duplicative Fields. Staff will clarify the requirements for community college instructors. (6) Expected Pay Periods. Staff will specify an “Intermittent” field value for service that cannot be performed for a full school term.

The Board heard the Pension Solution computer project update. The cost through the end date of February 2022 is $304.8 million. Next the Board heard the requirements of AB 2052 requiring all employers to submit payments by electronic funds transfer. AB 2052 only impacts 92 employers. 42 of those are already making payments electronically. Staff will work with the remaining 50 employers that have not made the transition.
The Board heard a summary of State and Federal legislation affecting CalSTRS.

1. AB 181 and AB 462 which require CalSTRS and CalPERS boards to submit annual reports are now two-year bills. (CalSTRS supports)
2. AB 644 the CalSTRS bill making technical changes is on the Governor’s desk.
3. AB 706 which removes the 3-year limit for an employee of a community college district to transfer unused sick leave to another employer is on the Governor’s desk.

The Board heard a presentation of the Annual Business Plan for 2019-20. The goals are: (1) Ensure a well-governed, financially sound trust fund, (2) Digital transformation – Pension Solution Computer Project, (3) Strengthen services to members, employers, stakeholders – the new building, (4) Organizational Strength – the new computer program.

Jack Ehnes, CEO introduced the 13 winners of the 2019 Virtuoso awards. These individuals have delivered superior, sustained performance. They are Cassandra Mallett-Beck, Gabriel Portugal, Dale Coffey, Gabriel Gandara, Jennifer Ellis, Kathleen Holiday, Melissa Wiese, Minday Selby, Nicole Snyder, Particia Falloon, Paul Rios, Rosie Rodrequez, Santie Moller,

Construction on the Headquarters Expansion Project will begin in August, so the next CalSTRS Board meeting will see the beginning of the project. The open parking lot will be closed, so entrance will have to be through the garage.

CalSTRS has launched an unclaimed property website for unclaimed teachers’ retirement funds-https://www.calstrs.com/post/unclaimed-property. The next meeting of the CalSTRS Board and Committees will be September 4, 5, 6.