ACERA

Alameda County Employees' Retirement Association

BOARD OF RETIREMENT

INVESTMENT COMMITTEE/BOARD MEETING

ACERA MISSION:

To provide ACERA members and employers with flexible, cost-effective, participant-oriented benefits through prudent investment management and superior member services.

Wednesday, April 12, 2023
9:30 a.m.

LOCATION AND TELECONFERENCE	COMMITTEE MEMBERS	
ACERA C.G. "BUD" QUIST BOARD ROOM 475 14TH STREET, 10TH FLOOR OAKLAND, CALIFORNIA 94612-1900 MAIN LINE: 510.628.3000 FAX: 510.268.9574	TARRELL GAMBLE CHAIR	APPOINTED
	GEORGE WOOD VICE CHAIR	ELECTED GENERAL
The public can observe the meeting and offer public comment by using the below Webinar ID and Passcode after clicking on the below link or calling the below call-in number.	ROSS CLIPPINGER	ELECTED SAFETY
	OPHELIA BASGAL	APPOINTED
	KEITH CARSON	APPOINTED
Link: https://zoom.us/join Call-In: 1 (669) 900-6833 US Webinar ID: 879 6337 8479 Passcode: 699406 For help joining a Zoom meeting, see: https://support.zoom.us/hc/en-us/articles/201362193	JAIME GODFREY	APPOINTED
	ELIZABETH ROGERS	ELECTED RETIRED
	HENRY LEVY	TREASURER
	KELLIE SIMON	ELECTED GENERAL
	CYNTHIA BARON	ALTERNATE RETIRED[1]
	KEVIN BRYANT	ALTERNATE SAFETY[2]

[1] The Alternate Retired Member votes in the absence of the Elected Retired Member, or, if the Elected Retired Member is present, then votes if both Elected General members, or the Safety Member and an Elected General member, are absent.

[2] The Alternate Safety Member votes in the absence of the Elected Safety, either of the two Elected General Members, or both the Retired and Alternate Retired members.

Note regarding accommodations: If you require a reasonable modification or accommodation for a disability, please contact ACERA between 9:00 a.m. and 5:00 p.m. at least 72 hours before the meeting at accommodation@acera.org or at 510-628-3000.

Public comments are limited to four (4) minutes per person in total. The order of items on the agenda is subject to change without notice.

Board and Committee agendas and minutes and all documents distributed to the Board or a Committee in connection with a public meeting (unless exempt from disclosure) are posted online at www.acera.org and also may be inspected at 475 14th Street, 10th Floor, Oakland, CA 94612-1900.

INVESTMENT COMMITTEE/BOARD MEETING

NOTICE and AGENDA Wednesday, April 12, 2023

Call to Order: 9:30 a.m.

Roll Call

Public Input (The Chair allows public input on each agenda item at the time the item is discussed)

I. ACTION ITEMS: MATTERS FOR DISCUSSION AND POSSIBLE MOTION BY THE COMMITTEE

1. Discussion and Possible Motion to Recommend that the Board Adopt a New Investment Plan for ACERA's Real Estate Asset Class

   9:30 – 10:00 | Avery Robinson, Callan Inc.
   John Ta, ACERA
   Betty Tse, ACERA

2. Discussion of and Possible Motion to Recommend that the Board Approve an up to $38 Million Investment in Crestline Opportunity Fund V as part of ACERA's Private Equity Portfolio – Debt-Related/Special Situations[3], Pending Completion of Legal and Investment Due Diligence and Successful Contract Negotiations

   10:00 – 10:30 | Summer Jarratt, Crestline Inc.
   Keith Williams, Crestline Inc.
   Faraz Shooshani, Verus Advisory
   Clint Kuboyama, ACERA
   Betty Tse, ACERA

3. Discussion and Possible Motion to Recommend that the Board Approve a Revised International Equity Asset Class Structure and Phased Implementation Transition Plan

   10:30 – 11:00 | Joe Abdou, Verus Advisory
   Samantha Grant, Verus Advisory
   Eileen Neill, Verus Advisory
   Julius Cuaresma, ACERA
   Betty Tse, ACERA

Information Items: These items are not presented for Committee action but consist of status updates and cyclical reports

1. Report on Investment Made Under Delegated Authority – Genstar Capital Partners XI[3] ($40 Million)

   Faraz Shooshani, Verus Advisory
   John Ta, ACERA
   Betty Tse, ACERA

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[3] Written materials and investment recommendations from the consultants, fund managers and ACERA Investment Staff relating to this alternative investment are exempt from public disclosure pursuant to CA Gov. Code §7928.710 and §7922.000

2. The Current State of ESG

Eileen Neill, Verus Advisory
David Nelsen, ACERA
Jeffrey Rieger, ACERA
Betty Tse, ACERA

Trustee Remarks
None

Future Discussion Items
None

Establishment of Next Meeting Date
May 17, 2023 at 9:30 a.m.

Callan

April 2023

2023 – 2024
Real Estate Investment Plan

Callan LLC

Avery Robinson, CAIA
Senior Vice President

Aaron Quach
Vice President

Agenda

– Portfolio Overview

– Market Highlights

– Investment Plan Recommendations

Portfolio Objectives Overview

Real Estate Investment Program

– The ACERA Real Estate portfolio dates back to 1988. The program has evolved from a heavily concentrated, predominately direct, separately managed account-based portfolio, to a well-diversified, commingled fund-based program.

– The ACERA Real Estate portfolio is anticipated to provide the following benefits over the long term:
  - Lower the overall portfolio risk due to real estate's low correlation with other portfolio asset classes;
  - Generate a stable income stream to assist in meeting cash flow needs;
  - Provide growth through appreciation;
  - Serve as a hedge against inflation;
  - Provide an opportunity to enhance portfolio return through higher total return investments.

– The real estate program had a target allocation of 9%. As of September 30, 2022, the real estate exposure was 8.55%. When including unfunded commitments, this exposure was 9.33%.

ACERA Program Overview

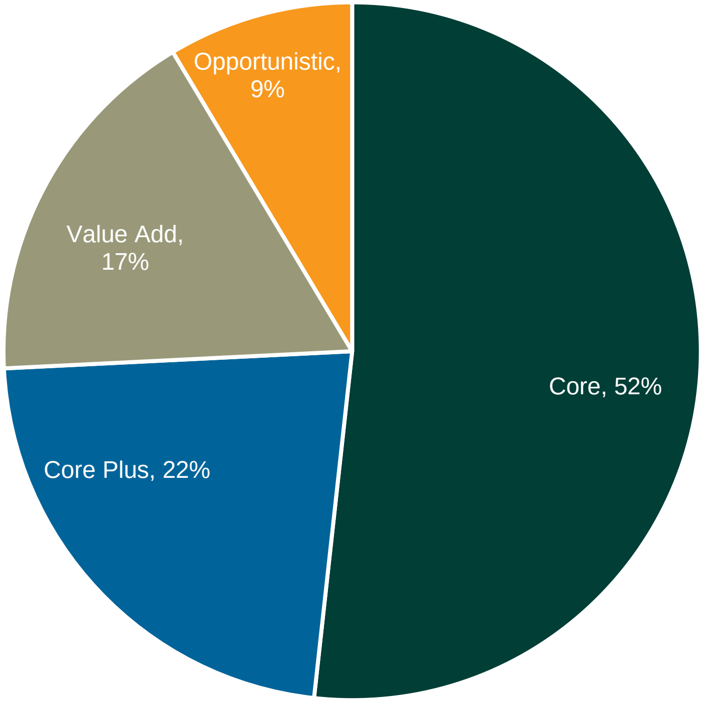
ACERA COMPLIANCE MATRIX (as of September 30, 2022)		
Investment Style Allocations	**Strategic Constraint / Guideline**	**Compliance**
Core	60% to 100%	Out of Compliance (52%)
Core Plus	0% to 30%	In compliance
Value-Added	0% to 30%	In Compliance
Opportunistic	0% to 15%	In Compliance
Return Targets (Five Year Measurement; Net/Net)	**Strategic Constraint / Guideline**	**Compliance**
Core	NCREIF Fund Index - Open End Diversified Core Equity (“ODCE”)	In Compliance
Core-Plus	NCREIF Fund Index - Open End Equity (“OE”)	In Compliance
Value-Added	NCREIF Fund Index - Open End Equity (“OE”)	In Compliance
Opportunistic	NCREIF Fund Index - Open End Equity (“OE”)	In Compliance
Total Portfolio	NCREIF Fund Index - Open End Diversified Core Equity (“ODCE)	In Compliance

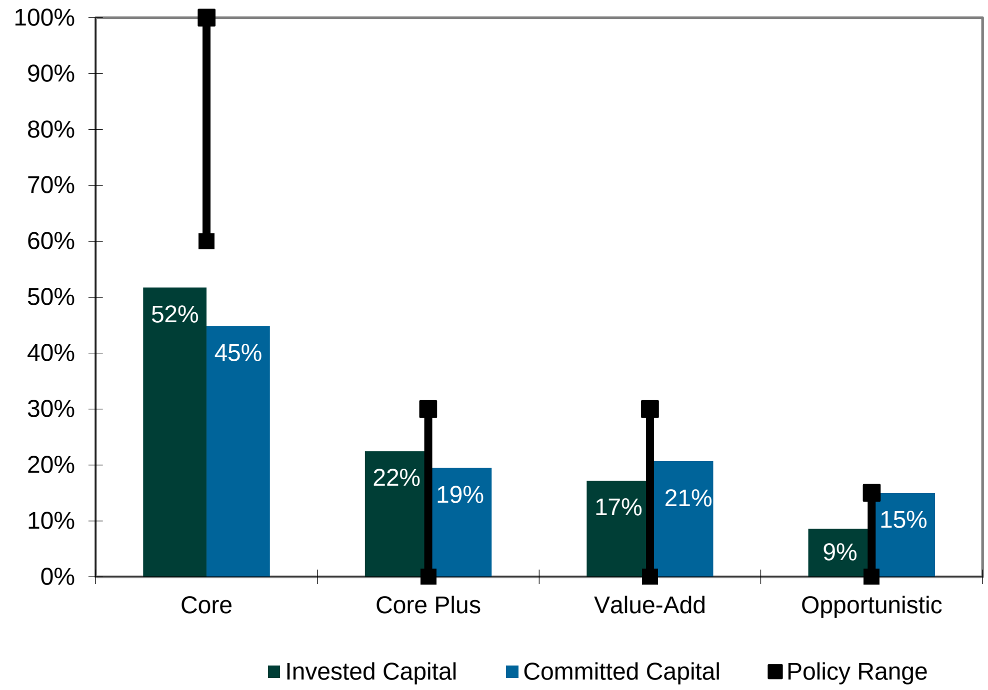
ACERA Program Overview

ACERA COMPLIANCE MATRIX (as of September 30, 2022)		
Wh	**Strategic Constraint / Guideline**	**Compliance**
Manager/Fund Diversification	No manager may represent more than 35% of ACERA's total real estate target allocation.	In Compliance
Property/Location Diversification	No property type or geographic location should represent more than 40% of program.	In Compliance
Leverage	A maximum of 40% leverage for the total portfolio.	In Compliance (29.7% LTV)
Watch List	A manager will automatically be placed on the Watch List if net of fee performance falls below the performance of the relevant manager account benchmark for three (3) consecutive quarters. Performance will be measured on a quarterly basis using the longest rolling time period possible (one-, three-, or five-year rolling returns).	In Compliance

Strategic Diversification (as of September 30, 2022)

Portfolio Overview



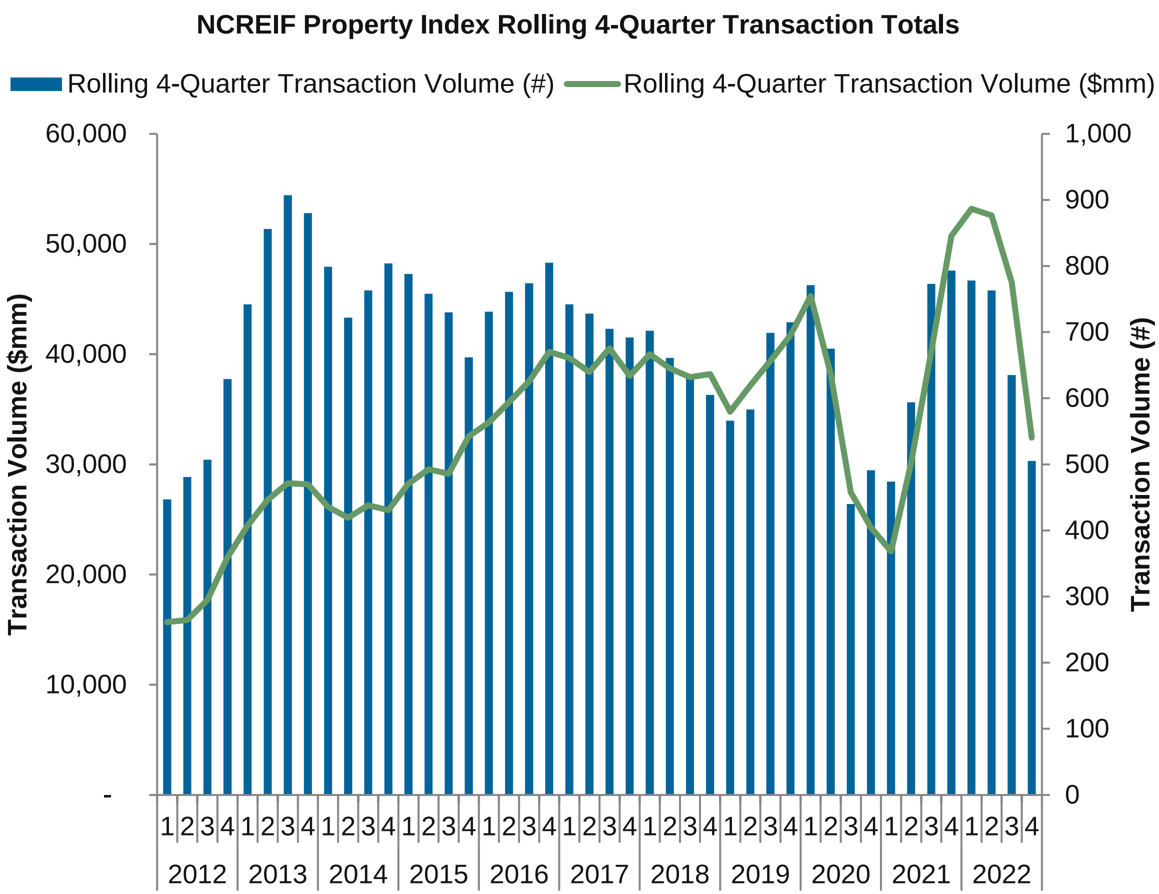


- ACERA has a predominantly core portfolio with some value-added and opportunistic exposure.
- Core real estate is below its strategic range of 60% to 100%.
- All other styles, including core plus, value-add, and opportunistic, are within their strategic ranges.

Market Observations and Highlights

Private real estate experiencing write-downs; transactions market slowing

- NCREIF NFI-ODCE saw a 4Q 2022 quarterly return of -4.97%, as valuations adjust to the rapid increase in interest rates. Certain sectors experiencing slowing demand also.
- Return dispersion by manager within the ODCE Index due to composition of underlying portfolios.
- Transaction volume continues to decrease on a rolling four-quarter basis and is now below five-year averages.
- The rise in interest rates is the driving force behind the slowdown in transactions. A bid-ask spread persists and price discovery continues to occur among market participants. Sectors that are in favor, such as multi-family and industrial, are more liquid.



Source: NCREIF

Market Capital Flow Activity

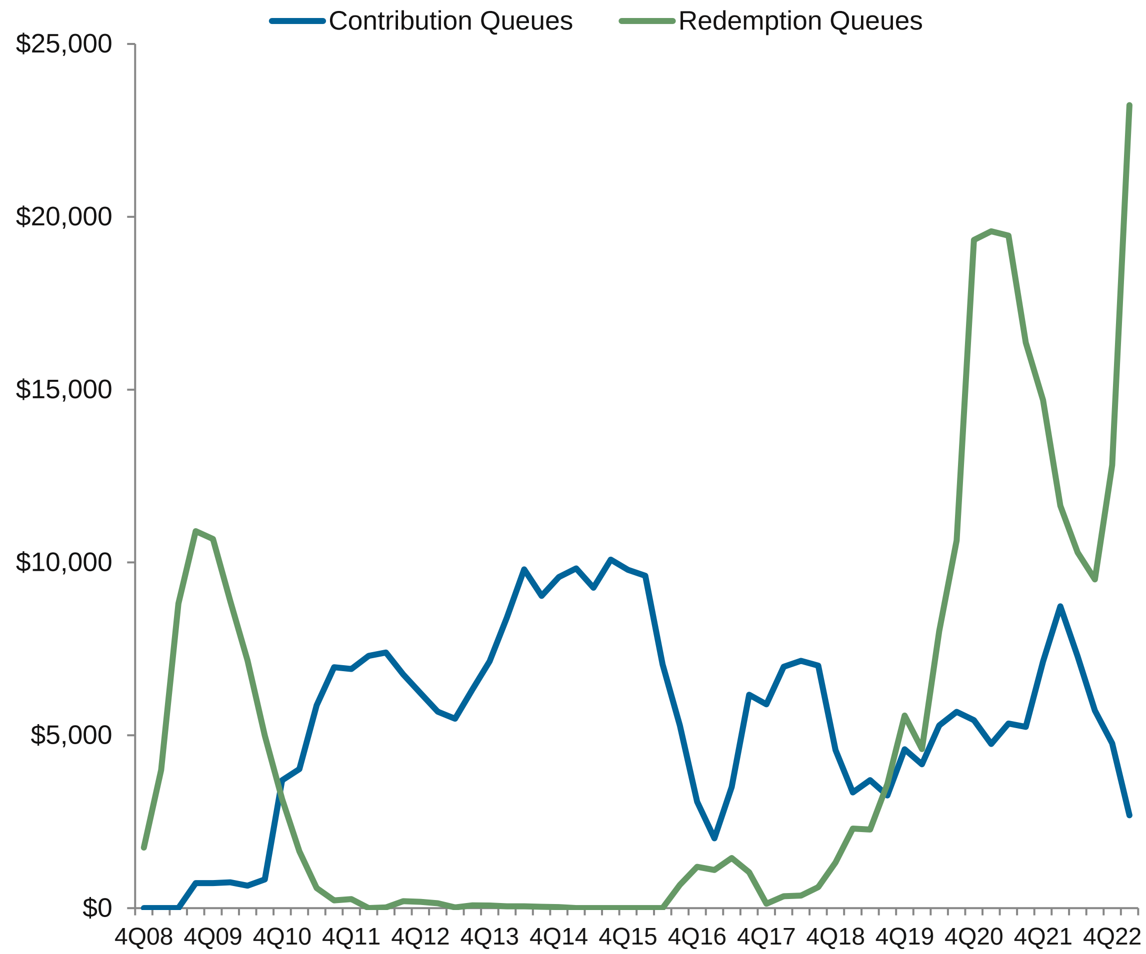
Denominator effect has driven redemption activity; rising interest rates to slow new construction

– The declines in the public markets and accompanying denominator have led to an influx of redemption requests. This has been coupled with addition, anticipated near-term real estate performance concerns. A rebound of public equity markets will relieve some of these pressures.

– Some niche property sectors are continuing to garner more interest, such as single-family rentals, medical office, and lab space.

– Net core activity has been extremely volatile during the past two years, with spikes in redemption activity in 2020 due to the COVID-19 pandemic and in 2022 due to rising interest rates.

Core Fund Contribution/Redemption Queues ($mm)



Source: NCREIF

ACERA Prior Investment Activity (2021/2022 YTD)

– There were three individual capital commitments made during 2021 and 2022 highlighted below. The strategies included both value-add and opportunistic funds.

– There is approximately $80 million in capital that remains to be drawn from these commitments.

– Continued maturing and liquidation Artemis Healthcare Fund I, CIM Urban REIT and UBS Trumbull Property Fund during 2021/2022.

Fund	Strategy	Commitment Amount ($mm)	Commitment Year
Artemis Healthcare Fund II	Value Add	$25.0	2021
CBRE Value Fund 9	Value Add	$40.0	2021
Starwood Fund XII	Opportunistic	$50.0	2022

2023 / 2024 Investment Plan Recommendations and Actions

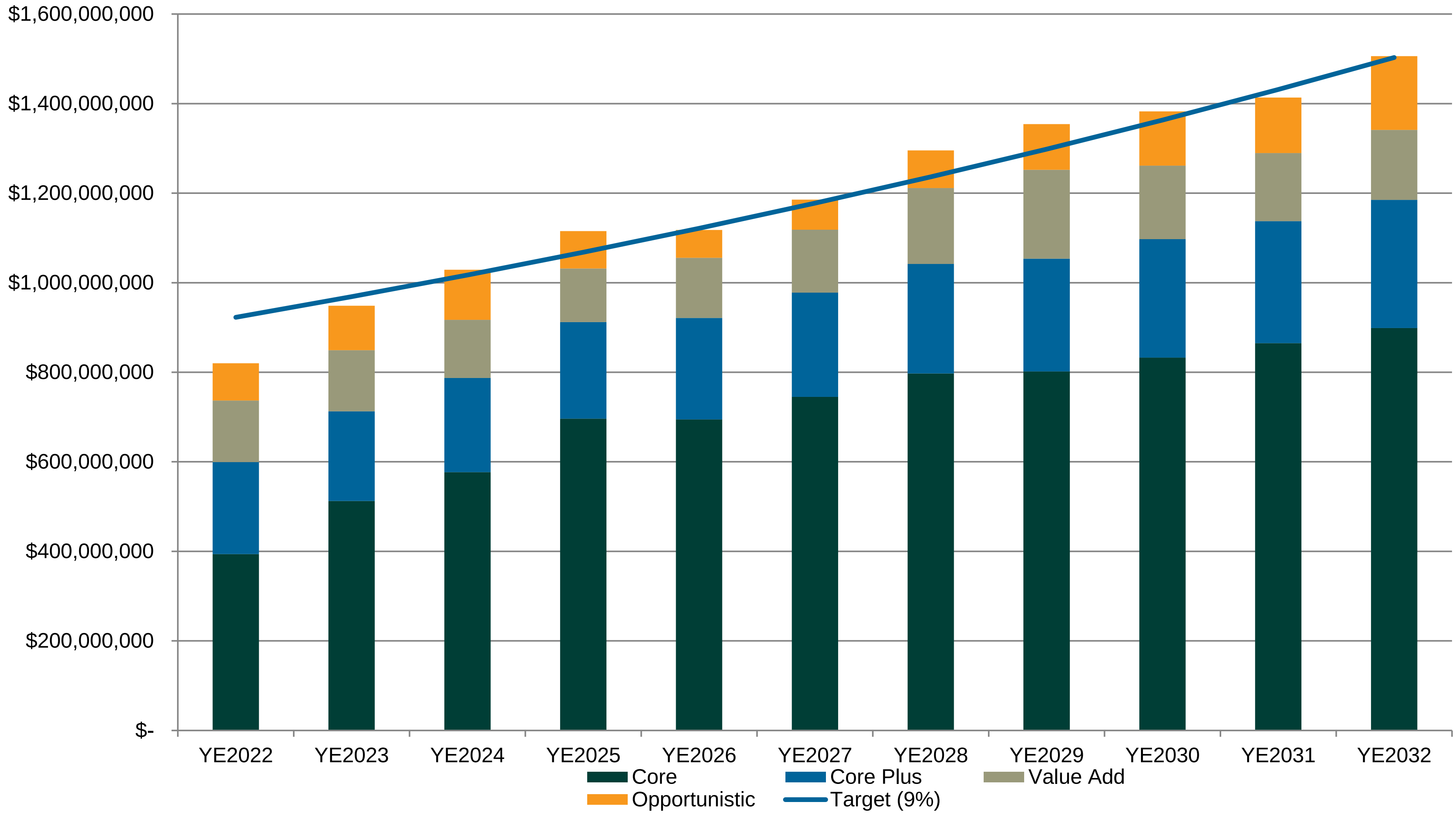
1. Callan recommends that ACERA increase its core position to bring it with the targeted range. Strategies that provide a high level of diversification in combination with the existing portfolio should be a focus. Net new commitments to core real estate totaling approximately $150 million before the end of 2024 will help maintain the real estate allocation target based on the pacing study. (9%)

2. Callan recommends that ACERA continue to explore non-core investment opportunities in order to achieve and maintain vintage year diversification as the existing fund's return capital. This recommendation is dependent on the availability and quality of non-core funds in the market. Given the existing outstanding commitments, new commitments of $50 million to $100 million each year will help achieve and maintain the real estate allocation target based on the pacing study.

3. Callan recommends ACERA continue to seek emerging manager opportunities per the ACERA Emerging Investment Manager Policy (up to 10%). There are ample compelling options within the emerging manager space, but many tend to be smaller funds with specialized focus. As such, Callan recommends consider diversified and niche opportunities with the understanding that smaller commitment amounts maybe more appropriate for smaller for niche funds.

Pacing Based on Recommended Commitments

– Based on the recommendation of $150 million to core real estate as well as continued commitments to non-core strategies, the real estate program is forecasted to remain near its 9% target.



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TO: Members of the Investment Committee

FROM: Julius Cuaresma, Investment Analyst JCC

DATE: April 12, 2023

SUBJECT: Discussion and Possible Motion to Recommend that the Board Approve a Revised International Equity Asset Class Structure and Phased Implementation Transition Plan

Recommendation:

Recommend that the Board approve a Revised International Equity Asset Class Structure and Phased Implementation Transition Plan.

Background and Discussion:

At the February Investment Committee Meeting (ICM), the Board approved changing the International Equity Asset Class Structure to 62% Developed Markets (33% passive, 29% active), 28% Emerging Markets (all active) and 10% International Small Cap (all active). Staff and Verus recommended this change, with the objective of simplifying the International Equity Structure and addressing the asset class' underperformance.

February's ICM approval process also included direction for Verus to 1) re-visit the International Developed active weightings; and 2) provide Implementation Transition Options. Verus has since re-visited the active weightings, resulting in two Structural Options for the Committee to vote on: 1) either affirm the February Board-approved Structure ("February-Approved") or 2) approve the Modification to the February-approved Structure ("Modified"). Section A below compares these Structural Options. Verus has provided two Implementation Options, "Immediate" and "Phased". Section B below compares these Implementation Options.

Section A: International Equity Structural Options 1) February-Approved or 2) Modified

Verus has provided two International Equity Structural Options, February-Approved or Modified; based on their analysis, they are indifferent between these two Structural Options. Staff supports this recommendation. Both Structural Options address the two underperforming Managers on Watchlist, Mondrian and Franklin Templeton (Tables 1 & 2).

Table 1: Mondrian Gross Performance	Trailing 5-years	Since Inception (Nov-03)	Table 2: Franklin Templeton Gross Performance	Trailing 5-years	Since Inception (Apr-11)
Mondrian	0.05%	5.84%	Franklin Templeton	-0.40%	4.55%
MSCI ACWI ex-USA	1.36%	6.04%	MSCI ACWI ex-US Small Cap	1.08%	3.98%
MSCI ACWI ex-USA Value	0.57%	5.73%	MSCI ACWI ex-US Small Cap Value	0.88%	3.92%
Source: Verus 4Q22 Investment Performance Review					

Both Structural Options involve amending the respective IMAs for Bivium and Capital Group to reflect the change in Mandates: from All Market Caps/All International Markets to only Mid-Large Caps/Developed Markets. Both respective IMAs will reflect this narrower investable asset universe; however, Bivium is further expected to implement the narrower investable asset universe with the added flexibility of holding tail Emerging Market and International Small Cap exposure from incumbent underlying Emerging Investment Managers (EIM).

The key difference between the Structural Options is that the Modified version reduces Active Manager concentration risk by balancing Capital Group down to 15% and Bivium up to 14%. Staff and Verus recently performed onsite due diligence at Bivium's offices: Bivium currently manages about $137.8M on behalf of ACERA – this represents about 4.4% of Bivium's $3.1B Firm AUM, and 6.1% of Bivium's $2.2B Diverse & Emerging Strategies Portfolio. Both Structural Options increase these concentration factors for the Committee to consider, not only ACERA as a percentage (%) of Bivium's AUM, but also Bivium as a percentage (%) of Bivium's underlying EIM AUM. That said, Bivium is also core to ACERA's EIM program; and such concentration factors are inherent characteristics when underwriting EIM investments. Please also see Verus' presentation, slide 9, for additional Bivium considerations; factoring such named considerations, Staff is comfortable in supporting Bivium's AUM increase under either Structural Option.

Section B: Implementation Transition Options 1) Immediate or 2) Phased

Both Implementation Transition Options re-structure the $2.6 B International Equity portfolio (about 25% of the Total Plan). Both Options: 1) involve multiple IMA Amendments (with Investment, Rebalancing and Transition Managers) as well as two RFP Searches (Emerging Markets and International Small Cap); and 2) start right after April's Committee Meetings. The key difference between the Options is that the: 1) Immediate Option aims to effectively run two *concurrent* RFP Searches; 2) the Phased Option aims to run two *successive* RFP Searches. Given the Investment, Legal, and Operational Due Diligence involved not just for this International Equity re-structuring, but all the Action Items on the 2023 IC Workplan, Staff and Verus recommend the Phased Option.

Conclusion:

Ultimately, both Structural Options from Section A above lead to an International Equity structure that reflects its benchmark, MSCI ACWI Ex-US IMI and the weightings to Market Cap, and Developed and Emerging Markets (Table 3). Importantly, this aligns with the object of the ACERA's General Investment Guidelines, Policies, and Procedures, as stated in Schedule VI, Section 3-b: "Diversification: Additionally, ACERA acknowledges the main tenet of capital market theory, which suggests that the capital markets represent the optimal structure for those markets and (i.e., 90%/10% U.S. Large Cap/10% U.S. Small Cap in Domestic Equities) will provide the most efficient structure (i.e., highest risk-adjusted returns) for those markets."

Table 3: Options vs. Benchmark	February-Approved	Modified	MSCI ACWI ex-US IMI
Total Developed Markets	**72%**	**72%**	**72%**
Total Emerging Markets	**28%**	**28%**	**28%**
Total Mid-Large Cap	**90%**	**90%**	**86%**
Total Small Cap	**10%**	**10%**	**14%**

Based on the recent Bivium onsite meeting, as well as recent due diligence calls, Staff supports Verus' recommendation for either Structural Option. In order to more seamlessly implement either Structural Option, Staff and Verus recommend the Phased Implementation Option.

Attachment:

#1 Investment Structure Recommendation, prepared by Verus

Verus

PERSPECTIVES THAT DRIVE ENTERPRISE SUCCESS

APRIL 12, 2023

International Equity Investment Structure and Implementation Recommendations

ACERA – Non-confidential

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2021 | LARGEST CONSULTANTS OF INSTITUTIONAL ASSETS
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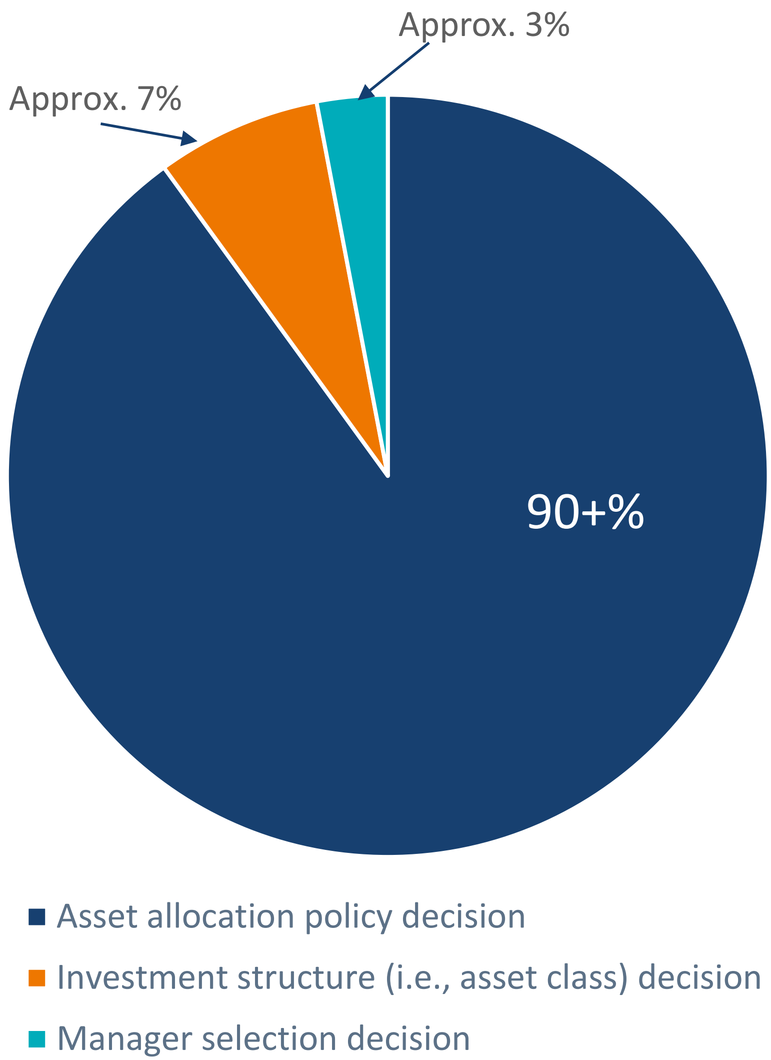
Board decision hierarchy



Summary

- Committee approved a new international equity asset class structure at February ICM to better align the portfolio with both the asset class benchmark (MSCI ACWI ex-U.S IMI) and the Board's stated investment philosophy.
- The new asset class structure accomplishes the following:

  (1) revises active/passive split from 25% to 33%

  (2) separates mandates into discreet developed markets and emerging markets

  – ensures portfolio maintains market-like exposure to these regions as well as large and small cap

  (3) eliminates style-oriented strategies

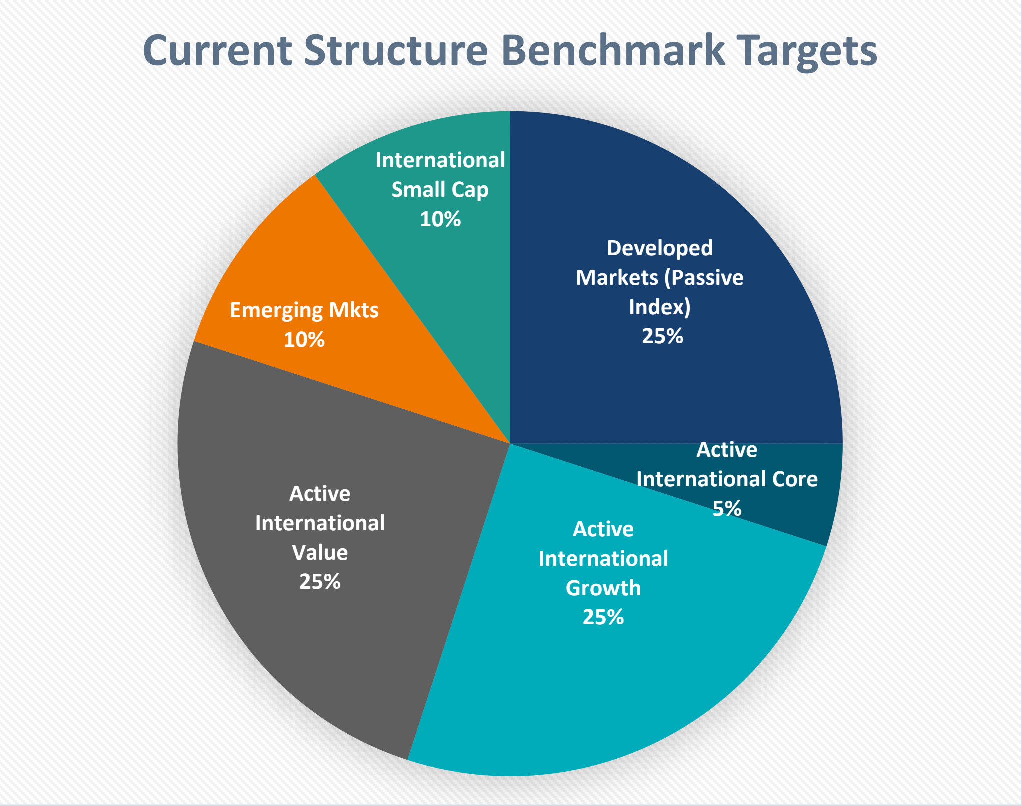
  (4) eliminates one manager; eases staff monitoring and oversight activities for the asset class

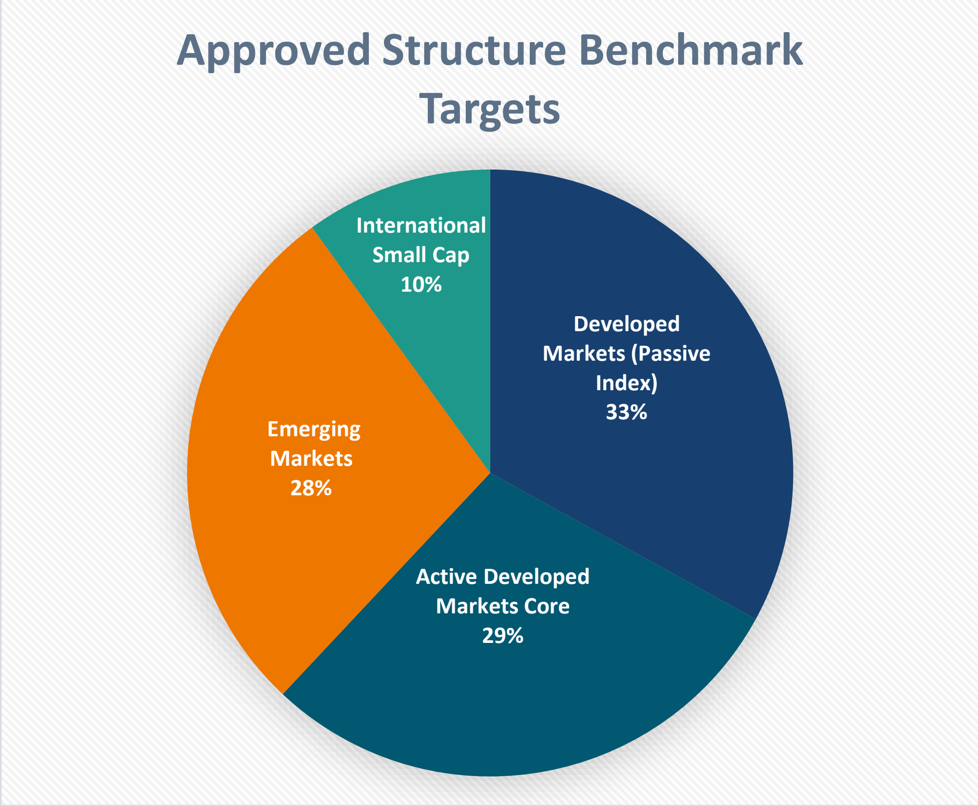
  (5) reduces single active manager risk due to smaller mandate sizes

  (6) presents opportunity to re-visit fee structures

Current ACERA international equity structure vs. Approved structure

- Target Allocation to **International Equity** is 24%
- **Asset class policy** is MSCI All Country World Index ("ACWI") ex-US IMI* Index





IMI = Investable Market Index; represents approximately 99% of each market's free-float adjusted market capitalization.

Implementation considerations
1) Asset class structure

- Direction from Committee was to re-visit active developed markets manager structure (29% of international equity asset class).
- Verus added below an alternative active developed markets manager structure (Mod #1).
- Verus is indifferent to either alternative since expected results are nearly identical (*note: results are in basis points*).

Assumed for Projection

	Alpha	Tracking Error	Information Ratio	Current	Approved	Mod #1
Bivium	100	503	0.20	5%	11%	14%
BlackRock	0	113	0.00	27%	33%	33%
Capital Group	100	453	0.22	22%	18%	15%
Mondrian	-25	443	-0.06	26%	0%	0%
William Blair	200	671	0.30	10%	14%	14%
New EME Mgr	200	618	0.32	0%	14%	14%
Franklin	0	433	0.00	10%	0%	0%
New ISC Manager	100	308	0.32	0%	10%	10%
				100%	100%	100%
			DM Exposure	76%	72%	72%
			EM Exposure	24%	28%	28%
Projected Alpha				41	95	95
Projected Tracking Error				144	236	234
Projected Information Ratio				0.28	0.40	0.41

Actual average 5-year ACERA international equity composite tracking error: 200 bps

Implementation considerations
1) Asset class structure

- There are several activities that could be undertaken immediately upon Board adoption of new international asset class structure without too much time or Staff effort:
  - — Liquidate and transfer assets from current International Value and Growth mandates to fund International Core mandate and Passive mandate
  - — Transition current International Core mandate to Developed Markets Core mandate (*see slide #8 for more details*)
  - — Transition current International Growth mandate to Developed Markets Core mandate
  - — Revise IMA's for current International Core and Growth managers to reflect new core developed markets mandates
  - — Initiate utilization of newly recommended benchmarks for active developed markets manager mandates

Implementation considerations
1) Asset class structure

- Open discussion issue is whether to fully implement new asset class structure all at once or to employ phased implementation
  - Full search implementation includes conducting search for additional active Emerging Markets and International Small Cap managers
  - Phased search implementation would conduct the Emerging Markets mandate manager search and delay the International Small Cap search to later date.
    - In interim, International Small Cap exposure will be provided by existing manager or synthetically
- ***Verus' recommendation is to move forward with phased search implementation approach***

Implementation considerations
1) Asset class structure

Immediate structure implementation	Phased structure implementation
Pros:	Pros:
• Most expeditious implementation approach	• Staff can more easily manage process and expenditure of time and effort
• Cleanest transition in terms of starting performance monitoring "clock" for new asset class structure	• Simplest implementation approach (i.e., least amount of moving parts)
Cons:	Cons:
• Staff time and effort during period of being understaffed	• Prolongs achievement of approved structure
	• Requires interim step of funding temporary passive International Small Cap manager mandate

Implementation considerations
2) Asset transition

- While transition to approved asset class structure is 100% within asset class, over 20% of assets would be subject to transition, or approximately $520 million
- Industry best practice for large and/or complex asset transitions is to employ transition management specialist
  - — ACERA has historically employed transition management specialists to conduct asset transitions
    - Another industry best practice for large public funds, like ACERA, is to retain “stable” of transition managers on contract given time sensitivity usually associated with transitions (i.e., short) and typical manager procurement period length (i.e., long)
  - — ACERA has three managers under contract for provision of transition services, if needed
    - These three managers are widely recognized by public funds as leading transition managers and conduct majority of asset transitions by institutional investors
- Staff and Verus will evaluate transition cost estimates from these 3 providers and select one firm to manage initial international equity asset class restructuring plan

Implementation considerations
3) Active developed markets managers

- As Bivium manages a fund of funds, there are unique aspects to consider in funding increased exposure and transitioning to revised benchmark
  - — All current large cap managers in Bivium fund have EAFE mandates. Thus, conversion to new World ex-U.S. benchmark can be achieved relatively seamlessly
  - — Another fund manager could transition from Emerging Markets to new World ex-U.S. benchmark without meaningful issues
  - — If Bivium deems it necessary to add new Developed Markets-only managers to receive some of the additional assets, it may take some time to open accounts in various markets. ***Thus, Verus recommends ACERA consider a phased-in transition as an accommodation***
  - — There are currently one Emerging Markets-only manager and two International Small Cap managers within the fund. ***Verus recommends Bivium be allowed to retain these managers post transition to new benchmark***
    - Their impact on fund's results will be lessened through increased assets in remaining large cap, developed markets mandates
- Converting Capital Group to new benchmark is not anticipated to be issue since firm already manages Developed Markets mandates in similar portfolio construction style

Next steps

Activity	Estimated Start Date	Estimated Completion Date	PERCENT COMPLETE	Q4 2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	Q1 2024
International Structure Allocation Decision	Q4 2022	Q2 2023	80%						
Amend IMAs for temporary EM and/or Intl SC exposure	Q2 2023	Q2 2023	0%						
Initial Transition to allocations approved in April	Q2 2023	Q2-Q3 2023	0%						
EM Search	Q2 2023	Q4 2023-Q1 2024	0%						
International Small Cap Search	Q1 2024		0%						

Recommendations

1) At February ICM, Committee requested Verus develop asset class structure alternative with modified Developed Markets manager weightings.

   — Thus, decision to be taken at this meeting is to either re-affirm asset class structure approved at February meeting or to approve modified new asset class structure.

Mandate	Feb. 2023 Approved Structure	Modified Approved Structure
Passive (Blackrock)	33%	33%
Active Core Developed Markets (Bivium)	11%	14%
Active Core Developed Markets (Capital Group)	18%	15%
Active International Value (Mondrian)	0%	0%
Active Emerging Markets (William Blair)	14%	14%
Active Emerging Markets (TBD)	14%	14%
Active International Small Cap Value (Franklin)	0%	0%
Active Core International Small Cap (TBD)	10%	10%

2) There are two implementation approaches: a) immediate transition to target structure or b) phased transition with activities spread over several quarters

   — Verus and Staff recommend phased implementation transition approach

Appendix

Overview of key terminology

Return measure

— **Alpha:** Manager portfolio's excess return versus portfolio benchmark return

Volatility measures

— **Standard deviation:** Referred to as "risk" or "volatility". It is a measure of portfolio return dispersion for a time series of individual period returns versus the mean or average return of that series.

— **Tracking error: '**Tracking error' is the standard deviation of the difference between returns of a portfolio and the portfolio benchmark. It's the volatility of a manager's excess returns (i.e., alpha).

Risk-adjusted return measures

— **Information Ratio**: Risk-adjusted *excess* returns as it is the standard deviation of manager alpha. Interpreted as the incremental return generated by the manager for the incremental risk undertaken (versus the benchmark); hence, a valid measure of manager skill.

Information Ratio

Return of portfolio minus return of benchmark divided by portfolio tracking error:

$$\frac{\textbf{(Return of the Portfolio – Return of the Benchmark)}}{\textbf{Portfolio Tracking Error}}$$

Verus

PERSPECTIVES THAT DRIVE ENTERPRISE SUCCESS

APRIL 12, 2023

Current ESG Regulatory Landscape

ACERA – Non-confidential

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2021 | LARGEST CONSULTANTS OF INSTITUTIONAL ASSETS
U.S. INSTITUTIONAL TAX-EXEMPT ADVISORY ASSETS
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Fiduciary standards for trustees – historical perspective

- Department of Labor ("DOL") Employees Retirement Income Security Act (1974) ("ERISA") – Required standard of care to ERISA beneficiaries to determine investments, or actions, based solely upon pecuniary factors (i.e., factors expected to have material effect on risk and/or return of an investment based on appropriate investment horizons consistent with plan's investment objectives and funding policy)
  - — Included "prudent person rule" later expanded to Prudent Expert Act
- Uniform Prudent Management of Institutional Funds Act (2006) ("UPMIFA") – Similar to DOL ERISA standards and developed to be applied to endowments and foundations
- DOL Fiduciary Rule (2016) – Broadened definition of fiduciary standard to include consideration of risks related to factors other than pecuniary. In 2020, then Administration reverted to historical ERISA fiduciary standard
- DOL Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights (2022) – Empowered plan fiduciaries to consider climate change and other ESG factors when making investment decisions and when exercise shareholder rights (i.e., proxy voting). Confirmed in 2023 by Congress after veto of proposed resolution to rescind standard

Federal-level

- In March 2022, SEC released proposed rule "Enhancement and Standardization of Climate-Related Disclosures for Investors"
  - Would be first mandatory ESG reporting requirements for U.S. companies
- SEC's proposed amendments to rules and reporting are meant "to promote consistent, comparable and reliable information for investors concerning funds' and advisers' incorporation of ESG factors"*
- Required disclosures would include:
  - Greenhouse gas emissions
  - Process for identifying, assessing and managing climate-related risks:
    - Oversight and governance of climate-related risk
    - Articulation of climate-related risk with material effect on business and financial statements
    - Whether company has adopted transition plan to deal with climate-rated risks
    - Measurement of physical or transitional risks to operations
  - Information on any publicly set climate-related targets or goals

**Source: SEC, May 25, 2022 press release "SEC Proposes to Enhance Disclosures by Certain Investment Advisers and Investment Companies About ESG Investment Practices" (http://sec.gov/news/press-release/2022-92)*

State-level

ESG unfavorable

- **Arizona, Florida, Idaho, Indiana, Kentucky, Mississippi, North Dakota** – require investment decisions for state retirement systems to be based only on pecuniary factors and prohibit ESG factor consideration
  - — prohibits investments in companies that boycott certain energy companies
- **Alaska, Oklahoma, Tennessee, Texas**
  - — Laws or policies that limit or prohibit transactions with companies that have called for divestment from fossil fuel industry
    - Texas -- must withdraw investments if companies do not cease boycotts
- Number of states have enacted bills to govern proxy voting practices and policies to prevent voting of proxies based on other than financial or economic pecuniary factors
  - — Led by state Treasurers' lobbying organization, *State Financial Officers Foundation,* and states' attorney generals
- Currently, 25 states oppose new DOL Rule

State-level

ESG favorable

Illinois – requires public investment leaders to incorporate ESG into their investment decisions (effective Jan 1, 2020)

Maryland – requires state retirement and pension board to consider climate risks in its investment policy and associated with its investment portfolio

Maine –first state to pass legislation mandating divestment of public assets from fossil fuels.

New Jersey – introduced legislation to prohibit investment of state retirement funds in any of the top 200 companies that hold the largest carbon content fuel reserves.

Oregon – Investment council ("OIC") approved policy formalizing importance of ESG factors in investment decisions (*OIC oversees Oregon Public Employees Retirement Fund*)

California-specific

Three proposed ESG-related bills in 2023:

- SB 252 “Fossil Fuel Divestment Act”
  - Prohibits investment in fossil fuel companies by CalPERS and CalSTRS and require liquidation of such investments
    - Prohibits CalPERS and CalSTRS from making new investments or renewing existing investments in thermal coal companies
    - Requires constructive engagement with thermal coal companies on plans to transition to clean energy generation
  - Hearing scheduled April 12, 2023
- SB 253 “Climate Corporate Data Accountability Act”
  - Requires California State Air Resources Board to develop and implement regulations requiring U.S. corporations doing business in California, and with $1 billion or more in annual revenue, to publicly report Scope 1, 2 and 3 carbon emissions to an emissions registry
    - Would include companies’ supply chains

California-specific

- SB 261 "Climate-Related Financial Risk Act"
  - Would require companies to prepare climate-related financial risk report disclosing climate-related financial risks and measures adopted to reduce and adapt to disclosed risks
    - Modeled on climate disclosure rules used by CalSTRS and many financial institutions

Summary

- ESG national debates centered around three (3) issues:
  — Perception of climate-related risks and energy transition
  — Proxy voting stances
  — Guns/ammunition
- ACERA's ESG policy is centered on ESG risk mitigation as well as ongoing monitoring and reporting of ACERA manager ESG implementation approaches
  — "ESG considerations will be evaluated, where applicable, with the goal of mitigating risk while maintaining or improving Plan returns over the long term"*

**ACERA ESG Investment Policy, updated March 2021, Section IV. ESG Mission Statement, page 4*