City and County of San Francisco
Retiree Health Care Trust Fund

Implementation Options

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Implementation Options

Background

- At the September 30, 2013 meeting, the Board requested that Meketa Investment Group research different implementation options for the Retiree Health Care Trust Fund (RHCTF), including the possibility of co-investing with SFERS.
- Staff at SFERS discussed options with the Chair of the RHCTFB and the Controller, following the SFERS November Board meeting. Meketa Investment Group also discussed the implementation options with staff at SFERS.
- Due to the statutory structure of the RHCTF, a unitized product for RHCTF co-investment in the SFERS Trust is not available. The City and County of San Francisco is permitted to withdraw funds from the RHCTF prior to its being fully funded in special circumstances. This withdrawal mechanism in the Charter precludes RHTCF assets from being co-invested along side illiquid (non-public) assets of the SFERS Trust.
- This document addresses four possible options for investing the assets of the RHCTF:
  - Direct co-investment with SFERS public portfolios (Global Equities and/or Fixed Income)
  - Co-investment in three passive investments with SFERS
  - California Employers' Retiree Benefit Trust (CERBT)
  - Independent solution
- All four of the implementation options presented in this document are likely to be short-term (less than 5 years) in nature, as the assets in the RHCTF are expected to increase rapidly through contributions over the next several years. Once assets reach a certain threshold, typically $100 to $200 million, it becomes cost-effective to invest in a more traditional structure, with commingled and separate accounts, where appropriate.

Current Status of the Retiree Health Care Trust Fund

- As of December 31, 2013, assets in the RHCTF totaled $39 million.
- All assets are held at the Office of the Treasurer & Tax Collector for the City and County of San Francisco.
- The RHCTF's actuary, Cheiron, projected asset values for the Fund through 2020 based on the July 1, 2010 actuarial valuation report. The following estimated asset values were issued in November 2012, and include estimated contributions as well as an assumed annual investment return of 7.5%:
  - FY 2014: $44 million
  - FY 2015: $66 million
  - FY 2016: $93 million
  - FY 2017: $139 million
  - FY 2018: $202 million
  - FY 2019: $286 million
  - FY 2020: $390 million
- The RHCTF is to be used to pay for the City's contribution to the health care premiums of its retirees and their survivors. In November 2013, voters passed Proposition A, which requires the RHCTF to be fully funded, or for certain budgetary criteria to be met, before payments can be made from the fund.

Implementation Option 1: Direct Co-investment with SFERS in Public Portfolios

Description

- Direct co-investment in public portfolios of SFERS; labeled either "Global Equities" or "Fixed Income."
  - "Global Equities" includes active and passive managers within U.S. Equities (12 investments managed by 11 external managers and 1 internally managed portfolio) and International Equities (13 investments managed by 11 external managers).
  - "Fixed Income" includes 11 public investments managed by 9 external managers and 1internally managed portfolio.
- Estimated management fees: 30 basis points for Global Equities and 21 basis points for Fixed Income.
- Custody fees: $25,000 annual fee includes account setup/maintenance, asset servicing, online access, monthly audit reporting, and GASB reporting. This estimated custody fee was provided by Northern Trust, the current custodian for SFERS. It should be noted that SFERS is in the middle of a custody search process.

- SFERS' strategic asset allocation includes a target allocation of 47% to Global Equity. The sub-asset class targets for Global Public Markets Equity and the underlying managers are as follows:

SFERS Sub-Asset Class	SFERS Target % of Global Equity 6/30/2013	SFERS Target % of Total Fund 6/30/2013	Number of Strategies 6/30/2013	Managers as of 6/30/2013
Passive S&P 500	16	7.5	1	SFERS S&P 500 Tobacco Free Index[1]
Enhanced S&P 500	5	2.4	1	QMA
U.S. Large Cap Value	9	4.2	1	BlackRock
U.S. Large Cap Growth	9	4.2	4	Sands Capital, Wellington, INTECH, Profit
U.S. Small Cap	6	2.8	3	Northern Trust, Bivium, DFA
U.S. Convertibles	3	1.4	2	Advent, Zazove
U.S. Equities	*48*	*22.6*	*12*	
Core International	14	6.6	3	AQR, Capital Guardian, Northern Trust[1]
Growth International	5	2.4	1	William Blair
Value International	11	5.2	2	Causeway, LSV
Small Cap International	6	2.8	2	DFA, Pyramis
Emerging Markets	11	5.2	5	Mondrian, Wellington, DFA (2), Capital Intl
International Equities	*47*	*22.1*	*13*	
Global Equity	5	2.4	0	NA
Opportunistic Strategies	0	0.0	2	(Private market manager)
Global and Opportunistic	*5*	*2.4*	*2*	
Total	*100*	*47*	*27*	

[1] Option 2 includes three passive investments from the Global Equity and Fixed Income portfolios: SFERS S&P 500 Tobacco Free Index, Northern Trust MSCI EAFE Index, and BlackRock U.S. Debt Index Fund.

- SFERS' strategic asset allocation includes a target allocation of 25% to Fixed Income. The sub-asset class targets for Fixed Income and the underlying managers are as follows:

Sub-Asset Class	SFERS Target % of Fixed Income 6/30/2013	SFERS Target % of Total Fund 6/30/2013	Number of Strategies 6/30/2013	Managers as of 6/30/2013
Internal Fixed Income	6	1.5	1	SFERS Internal
Barclays Aggregate Index Fund	6	1.5	1	BlackRock[1]
Core/Core Plus U.S. Bonds	59	14.8	4	Aberdeen (2), Stone Harbor, AFL-CIO
Commercial Mortgages	7	1.8	1	Prima
High Yield Corporates / Banks Loans	8	2.0	1	Oaktree
High Yield CMBS	5	1.3	1	Pyramis
Emerging Markets Debt	9	2.3	2	GMO, Barclays
Opportunistic Strategies	0	0.0	8	(Private market managers)
Total	*100*	*25*	*19*	

- The opportunistic strategies are private market structures, and would not be part of the co-investment option for the RHCTF.
- Net returns from the Global Equities and Fixed Income portfolios, as of June 30, 2013 are as follows:

SFERS Portfolios	Assets 6/30/13	1-Year	3-Year	5-Year	10-Year
Global Equities	$8.8 billion	19.41	13.85	3.56	7.69
Fixed Income	$4.2 billion	4.63	7.15	6.61	5.62

[1] Option 2 includes three passive investments from the Global Equity and Fixed Income portfolios: SFERS S&P 500 Tobacco Free Index, Northern Trust MSCI EAFE Index, and BlackRock U.S. Debt Index Fund.

Implementation

- This option would establish a unique relationship between SFERS and the RHCTF. SFERS does not currently have any co-investors, nor are they seeking to add co-investors. Additional discussions with SFERS, the Controller, and legal counsel would be necessary.
- Once the terms of the relationship with SFERS are agreed upon, discussions with the custodian, currently Northern Trust, would take place to determine custody services and final pricing.
- The Board would need to establish an asset allocation policy to determine the target allocations to Global Equities and Fixed Income.
- Again, private markets vehicles, and asset classes outside of equities and fixed income, would not be available.

Considerations

- The Board would retain control of the asset allocation in terms of setting targets to Global Equities and Fixed Income.
- The Board would not have control over the underlying construction of the Global Equities portfolio or the Fixed Income portfolio.
- The Board would not have the ability to hire or fire managers within the portfolios.
- Custody fees of approximately $25,000 would total 6 basis points on a $40 million asset level, 4 basis points on a $60 million asset level, and 3 basis points on an $80 million asset level.
- This option is unlikely to be a long-term solution, given the potential for different objectives and constraints between SFERS and the RHCTF, and the lack of control over the specifics of the allocations.
  - SFERS is designed to pay Pension benefits, while RHCTF is designed to pay health care and OPEB benefits. The actuarial assumed rates of return, risk tolerances, and even time horizon, may differ.

Implementation Option 2: Co-Invest in Passive Investments with SFERS

Description

- Co-investment with SFERS in three passive investments that cover broad public markets:
  - U.S. equities (SFERS S&P 500 Tobacco Free Index)
  - International equities (Northern Trust MSCI EAFE)
  - Investment grade bonds (BlackRock U.S. Debt Index Fund – benchmarked to the Barclays' Aggregate)
- Estimated management fees for 60/40 stock/bond mix are 5 to 6 basis points.
- Custody fees: $25,000 annual fee includes account setup/maintenance, asset servicing, online access, monthly audit reporting, and GASB reporting. This estimated fee for custody was provided by Northern Trust, the current custodian for SFERS. It should be noted that SFERS is in the middle of a custody search process.
- Returns from the benchmarks for these investments, as of June 30, 2013, are as follows:

Benchmark	SFERS Assets 6/30/13	1-Year	3-Year	5-Year	10-Year
S&P 500 Index	$1,439,724,000	20.92	18.28	6.82	7.11
MSCI EAFE Index	$401,868,000	18.62	10.04	-0.63	7.67
Barclays Aggregate Index	$250,707,000	-0.69	3.51	5.19	4.52

Implementation

- This implementation option would establish a unique relationship between SFERS and the RHCTF. SFERS does not currently have any co-investors, nor are they seeking to add co-investors. Additional discussions with SFERS, the Controller, and legal counsel would be necessary.
- Once the terms of the relationship with SFERS are agreed upon, discussions with the custodian, currently Northern Trust, would take place to determine custody services and final pricing.
- The Board would need to establish an asset allocation policy to determine the target allocations to U.S. equities, international equities, and investment grade bonds.

Considerations

- The Board would retain control of the asset allocation, to the extent possible, with three broad index options.
- Custody fees of approximately $25,000 would total 6 basis points on a $40 million asset level, 4 basis points on a $60 million asset level, and 3 basis points on an $80 million asset level.
- This option is unlikely to be a long-term solution, given the potential for different objectives and constraints between SFERS and the RHCTF, and the lack of control over the specifics of the allocations (e.g., the passive equity option is a tobacco-free index. This may or may not be aligned with the investment objectives of the RHCTF).

Implementation Option 3: California Employers' Retiree Benefit Trust

Description

- The CalPERS California Employers' Retiree Benefit Trust (CERBT) was established in 2007 to assist public employers in meeting retiree health and OPEB obligations.
- Currently, nearly 400 California public employers have investments in CERBT, totaling $3.2 billion.
- The CERBT offers three pre-specified portfolio strategies: Moderate, Moderately Conservative, and Conservative.

	Moderate (Strategy 1) (%)	Moderately Conservative (Strategy 2) (%)	Conservative (Strategy 3) (%)
Global Equity	66	50	32
U.S. Nominal Bonds	18	24	42
Global Real Estate	8	8	8
Inflation-linked Bonds	5	15	15
Commodities	3	3	3
Net Expected Return[1]	*7.61*	*7.06*	*6.39*
Expected Risk	*11.73*	*9.46*	*9.27*

[1] Expected risk and returns are based on CalPERS assumptions.

- All three strategies utilize the same asset classes, but in different proportions. Four of the five asset classes are passively managed. The U.S. Nominal Bonds allocation is the only asset class that is actively managed. U.S. Nominal Bonds, Inflation-linked Bonds, and Commodities are managed by the internal investment staff at CalPERS. Global Equity and Global Real Estate are managed by State Street Global Advisors (SSgA), according to parameters established by CalPERS investment staff.
- The asset allocation targets for each strategy are formally reviewed once every three years. The last review was completed in 2013.
- A flat 14 basis point administrative fee is charged by CERBT, with no additional charge for custodial and investment management services. Additionally, about 1 basis point of investment management fees is deducted from the SSgA passive investments. However, this fee is not billed separately, since it is taken automatically from the commingled investment.
- Net returns for the three CERBT strategies are as follows:

CERBT Strategy	Inception	1-Year 6/30/13	3-Year 6/30/13	5-Year 6/30/13
Strategy 1 – Moderate	June 1, 2007	11.78	11.84	4.52
Strategy 2 – Moderately Conservative	October 1, 2011	8.87	NA	NA
Strategy 3 – Conservative	January 1, 2012	5.21	NA	NA

Implementation

- According to the CERBT website, to participate in the CERBT, a Fund must do the following:
  - Hire an actuarial consulting firm to perform a valuation using the OPEB Assumptions Model prescribed by CalPERS.
  - Provide the actuarial firm with the Summary of Actuarial Information Required for CalPERS Financial Statements.
  - Complete the Certification of OPEB Actuarial Information and Funding Policy
  - Complete and provide two original signed copies of the Agreement and Election to Prefund Other Post Employment Benefits.
  - Complete the Delegation of Authority to Request Disbursements.
  - Present the Agreement and the Delegation of Authority to the employer's governing body for adoption and approval.

Considerations

- The Board would not have control over the construction of the selected strategy.
- The Board would not have the ability to hire or fire managers in the selected strategy.
- CERBT has up to 150 days to meet redemption notices.

Implementation Option 4: Independent Solution

Description

- Under an independent solution, the RHCTF would establish its own structure for custody and investment of Fund assets.
- Initially, assets would likely be invested in low-cost passive investments. Once assets increase, searches for active mandates may be conducted.
- Estimated investment management fees would range between 4 basis points and 18 basis points, based on specific passive investments. Once assets increase and minimum investments are met for active manager fee schedules, then investment fees would increase commensurate with assets.
- Custody fees are estimated at approximately $20,000 to $40,000 per year. However, a full RFP search for a custody provider should be conducted.

Potential for Passive Investments in an Independent Solution

- Passive investment strategies attempt to replicate the returns of a particular market segment. Active managers seek to outperform benchmarks (typically passive indexes) by creating portfolios that differ from the market through investing in specific securities, strategies, or sectors.
- Fee schedules for both passive and active managers are often tiered, so that more assets invested in a strategy result in a lower fee on a percentage basis. For example, Vanguard offers a discounted fee for many of its indexed strategies when assets in the strategy exceed $5 million.
- Passive and active managers offer a variety of investment vehicles, including mutual funds, ETFs, commingled funds, and separate accounts.
- Initially, the RHCTF may gain efficient exposure to capital markets through the use of passive mandates. The table below provides a range of passive fees for major asset classes, as well as estimated total fees.

	Passive Fee Range (%)	Sample Allocation (%)
Equities		
U.S. Equities	0.04 - 0.06	30
International Developed Markets	0.07 - 0.12	25
International Emerging Markets	0.12 - 0.18	5
Fixed Income		
Investment Grade Bonds	0.06 - 0.10	30
U.S. TIPS	0.04 - 0.10	10
Total Fund estimated fees	6-10 bps	

Fund Levels and Asset Class Mandates

- As assets in the Fund increase, the RHCTF may pursue active management in inefficient asset classes.
- The table below provides a general perspective of asset classes and active mandates that could be added at approximate total Fund asset levels.

$40 million	$60 million	$80 million	$100 million	$200 million
• Passive U.S. Equities • Passive Int'l Equities • Passive Fixed Income	• Active EM Equities • Active High Yield	• Active U.S. Small Cap • Active Large Cap Int'l • Active Small Cap Int'l	• Private Equity FOF or Secondary • Real Estate FOF or Secondary • Active EM Debt	• Consider direct private market investments

- Specific implementation would be adjusted after an asset allocation study is completed.

Implementation

- If the RHCTF elects to create an independent portfolio, the first step would be to conduct a search for a custodian.
- Next, the Fund would conduct a search for passive index options.
- Meketa Investment Group could conduct an asset allocation study concurrent with the custody and index provider searches.

Considerations

- Given a low starting asset value, costs may be higher, as a percentage of total Fund assets, in the first few years for this option.
- There may be more administrative and legal steps necessary to implement this option.

Summary of Implementation Options

	SFERS Co-Invest Direct (Option 1)	SFERS Co-invest Passive (Option 2)	CalPERS CERBT (Option 3)	Independent Solution (Option 4)
Investments	Two SFERS portfolios: Global Equities and Fixed Income	Three SFERS passive funds: S&P 500, MSCI EAFE, and Barclays Aggregate	Three strategies with pre-defined asset allocation targets	Choose between investable universe of passive and active funds
Initial asset classes	Global Equities (U.S., Int'l Developed and Emerging) Fixed Income (IGB, High Yield, EM Debt)	U.S. Equities, International Developed Market Equities, Investment Grade Bonds	Global Equities, U.S. Bonds, Global Real Estate, Inflation-Linked Bonds, Commodities	Global Equities, Investment Grade Bonds, Inflation-Linked Bonds
Active/Passive Investments	Active and Passive	Passive	Active and Passive	Active and Passive
Board Authority Over:				
Asset Allocation	Yes	Yes	No (select strategy)	Yes
Asset Class Structure	No	Yes	No	Yes
Individual Managers	No	No	No	Yes
Investment Cost	~ 25 bps	5-6 bps	1 bp	6-8 bps
Custody and Admin Cost	$25k per year	$25k per year	14 bps (admin fee)	$20k - $40k per year
Est. Cost on $40 million Fund	$125,000 (31 bps)	$45k - $49k (11-12 bps)	$60,000 (15 bps)	$44k - $72k (11-18 bps)
Est. Cost on $60 million Fund	$175,000 (29 bps)	$55k - $61k (9-10 bps)	$90,000 (15 bps)	$56k - $88k (9-15 bps)
Est. Cost on $80 million Fund	$225,000 (28 bps)	$65k – $73k (8-9 bps)	$120,000 (15 bps)	$68k - $104k (8-13 bps)
Expected Implementation timeframe[1]	~ 1 Year	~ 1 Year	~ 6 months	~ 1 Year
Considerations	Access to active managers No authority over managers	Lowest cost		Customizable

[1] Legal and actuarial reviews will be a significant factor in setting the timeframe for investment. Custody, asset allocation, and investment option searches could begin once a structure is approved.

Expected Returns and Actual Performance History as of June 30, 2013

	Gross Expected Return (%)	Expected Standard Deviation (%)	Net Return 1-Year 6/30/13 (%)	Net Return 3-Year 6/30/13 (%)	Net Return 5-Year 6/30/13 (%)	Net Return 1-Year 6/30/13 (%)
SFERS[1]						
Global Equities	10.5	20.0	19.41	13.85	3.56	7.69
Fixed Income	3.6	5.0	4.63	7.15	6.61	5.62
66/34 Split	8.2	13.4				
SFERS[2]						
S&P 500	9.4	18.0	20.92	18.28	6.82	7.11
MSCI EAFE	9.9	20.0	18.62	10.04	-0.63	7.67
Barclays Aggregate	3.6	5.0	-0.69	3.51	5.19	4.52
33/33/34 Split	7.6	12.4				
CERBT[2]						
Strategy 1 – Moderate	7.76	11.73	11.78	11.84	4.52	NA
Strategy 2 – Moderately Conservative	7.21	9.46	8.87	NA	NA	NA
Strategy 3 - Conservative	6.54	7.27	5.21	NA	NA	NA
Independent Solution						
66/34 Split	8.2	13.4	NA	NA	NA	NA

[1] Meketa Investment Group 2014 Asset study inputs used for expected returns for SFERS and Independent solution. All expected returns are shown gross of fees. Historical returns for SFERS are net of fees.
[2] CERBT expected returns and standard deviation are based on CalPERS assumptions. Historical CERBT returns are net of 15 bps of fees. Expected returns are gross of fees.

Conclusion

- The four implementation options presented are all viable methods for the RHCTF to invest the portfolio.
- There are potential benefits, efficiencies, and drawbacks within each option.
- Regardless of the implementation option chosen by the Board, Meketa Investment Group recommends that one of the next steps for the Board is to establish an Investment Policy Statement for the RHCTF.

Appendices

SFERS IPS

Investment Policy, Objectives and Guidelines for the San Francisco City and County Employees' Retirement System

Mission Statement

San Francisco City and County Employees' Retirement System is dedicated to securing, protecting and prudently investing the pension Trust assets, administering mandated benefit programs, and providing promised benefits.

Approved: November 14, 2012

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INTRODUCTION

This document provides a framework for the management of the assets of the San Francisco City and County Employees' Retirement System ("SFERS" or the "System"). The purpose of the Investment Policy Statement ("IPS") is to assist the Retirement Board (the "Board") to effectively supervise and monitor the assets of SFERS (the "Plan"). Specifically, the IPS will address the following issues:

- The goals of the investment program;
- The policies and procedures for the management of the investments;
- Specific asset allocations, rebalancing procedures and investment guidelines;
- Performance objectives; and,
- Responsible parties.

The Board establishes this investment policy in accordance with applicable Local, State, and Federal laws. The Board members exercise authority and control over the management of the Plan, by setting policy that the Investment Staff executes either internally or through the use of external prudent experts with discretionary authority subject to policies established by SFERS. The Board oversees and guides the Plan and its policies subject to the following basic fiduciary principles:

- To act solely in the interest of, and for the exclusive purpose of providing benefits to, participants and their beneficiaries, minimizing contributions thereto, and defraying reasonable expenses of administering the Plan. The Board's duty to its participants and their beneficiaries shall take precedence over any other duty.
- To act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent expert acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character with like aims.
- To diversify the investments of the Plan so as to effectively trade off the risk of loss and appropriate rates of return. Diversification is applicable to the deployment of the assets as a whole, and does not preclude the use of concentrated investment styles.

The IPS is designed to allow for sufficient flexibility in the management oversight process to capture investment opportunities as they may occur and to establish reasonable parameters to ensure prudence and care in the execution of the investment program.

INVESTMENT GOALS

SFERS' investment goals are:

- To provide SFERS participants with retirement benefits as required by City and County Charter and applicable laws. This will be accomplished through a carefully planned and executed long-term investment program.

- SFERS' assets will be managed on a total return basis. While SFERS recognizes the importance of the preservation of capital, it also adheres to the principle that varying degrees of investment risk are generally rewarded with compensating returns.

- On an annualized net-of-fee basis, over a full market cycle, the total portfolio will be expected to:
    1. Exceed the assumed actuarial rate of return (currently 7.58%[1]) over rolling five-year periods; and/or,
    2. Exceed a weighted index based on SFERS' asset allocation policy and respective asset class component benchmarks over rolling five year periods by an appropriate amount.

- To undertake all transactions for the sole benefit of SFERS members and beneficiaries, and for the exclusive purpose of providing benefits to them, minimizing contributions to the Plan and defraying reasonable administrative expenses associated with the Plan.

- To set asset allocation policy in a manner that encompasses a strategic, long-term perspective of capital markets as well as the nature and structure of SFERS' liabilities. SFERS recognizes that a strategic long-term asset allocation plan implemented in a consistent and disciplined manner will be the major determinant of the Plan's investment performance.

- To make decisions and follow investment policies which comply with "prudent expert" standards.

[1] The actuarial rate of return is being reduced to 7.50% (from 7.75%) over a three time period. The actuarial rate of return, as approved by the Retirement Board, will be 7.66% in Fiscal Year 2012, 7.58% in Fiscal Year 2013, and 7.50% in Fiscal Year 2014, and thereafter.

INVESTMENT POLICIES AND PROCEDURES

The policies and procedures of SFERS' investment program are designed to maximize the probability that the investment goals will be fulfilled.

Asset Allocation Policy

SFERS adopts and implements an asset allocation policy that is predicated on a number of factors, including:

- A projection of actuarial assets, liabilities and benefit payments and the cost of contributions;
- Historical and expected long-term capital market risk and return behavior;
- An assessment of future economic conditions, including inflation and interest rate levels; and,
- The current and projected funding status of the Plan.

This policy provides for diversification of assets in an effort to maximize the investment return of the Plan consistent with market conditions and risk tolerance. Asset allocation modeling identifies asset classes the Plan will utilize and the percentage that each asset class represents of the total fund.

Due to the fluctuation of market values, positioning within a specified range is acceptable and constitutes compliance with the policy. It is anticipated that an extended period of time may be required to fully implement the asset allocation policy, and that periodic revisions will occur. SFERS' Investment Staff ("Staff") and external consultants will monitor and assess the actual asset allocation versus policy and will evaluate any variation deemed significant.

Asset allocation policy shall be implemented through the use of investment managers (both internal and external) that will invest SFERS' assets subject to investment guidelines incorporated into the investment management agreements executed with authorized representatives of the System.

SFERS will also use passive management styles in market segments where there is a high degree of market efficiency, where low or no tracking error is desired, or to provide temporary exposure.

The long-term asset allocation targets and ranges for the investments of the Plan's assets are shown in Tab 1. These targets and ranges shall be in effect for both broad asset classes and public market sub-asset classes.

Investment Manager and Consultant Authority

The investment managers shall have full discretion to direct and manage the investment and reinvestment of assets allocated to them for management on SFERS' behalf in accordance with this document, applicable Local, State and Federal statutes and regulations, individual investment management agreements, approved investment guidelines, and executed contracts.

Consultants shall have no discretionary authority (unless such authority is delegated contractually by the Board and the Consultant) and shall be co-fiduciaries to the Plan. Consultants shall be responsible for making timely and appropriate recommendations on investment policy issues, for monitoring managers, and for reporting on manager and total fund performance (or asset class composite level performance for specialty consultants) on a quarterly basis. The Board and Staff will consider the comments and recommendations of Consultants in conjunction with other available information in making informed, prudent decisions.

Fiduciary Responsibilities

All investments must be underwritten and assets managed by a qualified investment manager acting in a fiduciary capacity to SFERS. Once retained, an investment manager must acknowledge in writing the manager's fiduciary responsibility to SFERS and acknowledge the objectives and policies contained in this Policy. It is expected that, at all times, the manager(s) will conduct themselves as fiduciaries in conformance with the California Constitution, Article XVI, Section 17 and Charter Section 12.100, unless a lesser standard of fiduciary duty is necessary because of generally prevailing industry standards for an investment of that type and nature. Any such generally prevailing industry standard shall be established upon the written advice of the investment consultant responsible for that asset class.

Commission Recapture

SFERS requires that active equity managers use good faith efforts to direct a specific percentage of brokerage transactions for Plan assets under their management through designated commission recapture brokers. SFERS also encourages its fixed-income managers, on a "best effort" basis, to utilize the services of designated commission recapture brokerage firms. It is understood that the commission recapture brokerage firms must provide the best price and execution consistent with market conditions, bearing in mind the best interests of the Plan's beneficiaries and considering all relevant factors.

SFERS will monitor on an ongoing basis the services provided by the commission recapture brokers so as to assure that the investment managers are securing the best execution of SFERS' brokerage transactions.

All rebates or credits from commissions paid to the commission recapture brokers will be realized in cash and rebated back to the Plan.

Emerging Business Enterprises

SFERS Staff, its investment managers, and its consultants shall make a good faith effort to retain and utilize the services and/or products of qualified Emerging Business Enterprises on a sub-contracting and/or joint venture basis when those services/products are provided consistent with the fiduciary responsibilities of the Board.

SFERS will also, to the extent possible, use and encourage the use by its managers of brokerage services offered by emerging brokerage firms, particularly certified San Francisco-based firms.

SFERS has also adopted a policy regarding emerging investment managers, which is included as Tab 8 of this document.

Proxy Voting

SFERS acknowledges that the ownership of equities requires proxies to be voted, and that such voting rights are a tangible asset of the System. The System commits to managing its proxy voting rights with the same care, skill, diligence and prudence as is exercised in managing its other assets, in the sole interest of the System's members and beneficiaries and in accordance with all applicable statutes.

The voting rights of individual stocks will be exercised by an assigned proxy provider under the supervision of the Investment Staff consistent with policy direction from the Retirement Board. The Board shall review the actions of the assigned proxy provider at least annually.

Securities Lending

The Board has authorized the execution of a "Security Lending Program," which will be performed by the Plan custodian or qualified third party securities lending agent(s). The program will be monitored and reviewed by the Investment Staff and will be established and governed by a written agreement. Unless otherwise designated, the income or losses generated by the lending program accrues to the Investment Cash account.

The SFERS Investment Policy and Program Overview for Securities Lending is included as Tab 12 of this document.

Custody of Assets

With the exception of assets invested in commingled funds or assets invested in an investment program approved to use one or more Prime Brokers, the assets of the Plan shall be held in a custody/record-keeping account in a master custody bank located in a national money center and in the international sub-custodian banks under contract with the custodian bank.

Staff shall be responsible for reviewing the cost-effectiveness and performance of the custodian on a regular basis (at least every five years), with input from SFERS' consultants as needed.

Derivatives

Derivatives may be employed by SFERS' investment managers (including internal managers) if permitted in the manager's written guidelines. The purpose of derivatives shall be to control portfolio risk, aid in liquidity management, augment return, and/or execute portfolio strategies in a timely and cost-effective manner. Derivatives are contracts or securities whose returns are derived from the returns of other securities, indices or instruments including, but not limited to futures, forwards, options, options on futures and private swaps. Examples of appropriate applications of derivative strategies include hedging interest rate and currency risk, executing a passive management style, maintaining exposure to a desired asset class while effecting asset allocation changes, and adjusting portfolio duration of fixed income portfolios.

Unless permitted to do so in their written guidelines, SFERS' investment managers are not allowed to utilize derivatives for speculative purposes, including creating leverage. SFERS' managers typically shall not borrow funds to purchase derivatives; any exceptions shall be specified in the investment manager's written guidelines. No derivatives positions can be established that create portfolio characteristics outside of portfolio guidelines.

Managers must ascertain and carefully monitor the creditworthiness of any third parties involved in derivative transactions.

Short Sales and Leverage

Short sales of securities and leverage may be allowed only if permitted in the investment manager's written guidelines, and shall typically be subject to expressed limits.

Rebalancing

A systematic rebalancing procedure, implemented on a regular basis when asset allocation ranges are breached, or when cash flows occur (e.g., for benefit payments or funding new investments), or for other reasons judged to be in the best interests of the Plan and its beneficiaries, will be used to maintain or to move asset allocations within their appropriate allowable ranges as delineated in Tab 1 of this Investment Policy Statement.

The Deputy Director for Investments ("DDI"), supported by the Deputy Division Directors for Public Markets and Private Markets, shall be responsible for undertaking rebalancing at the broad asset class level. The Senior Investment Officers or Senior Portfolio Managers ("SIO"s or "SPMs") shall be responsible for making rebalancing recommendations to the appropriate Deputy Division Director for their respective asset class(es) and for implementing those recommendations subject to approvals from the DDI. Rebalancing decisions will take into consideration a combination of various factors including but not limited to: cash needed for benefit payments and expenses, cash needed for investments, asset allocation shifts and weights relative to targets and permissible ranges, an assessment of capital markets conditions, and the performance, organizational and investment attributes of individual managers, including each manager's status under SFERS' Manager Monitoring and Retention Policy (Tab 7).

When broad asset class ranges are breached, the System will rebalance assets such that asset allocation is brought to within the ranges specified in Tab 1. For sub-asset classes, the SIO or SPMs will make recommendations regarding allocations to sub-asset classes within their area of responsibility, and shall rebalance according to the same rule when relevant ranges are breached. Sub-asset class targets and ranges are also delineated in Tab 1. Subject to approval by the appropriate Deputy Division Director and the DDI, Staff will also have discretion on how to redeploy assets within their asset class in accordance with applicable ranges. The Board recognizes that from time to time ranges may be breached for a period of time due to the absence of an appropriate manager and/or Staff judgment that an existing manager(s) should not be allocated additional assets, or when, in the judgment of Staff, market conditions are not favorable to rebalancing activities.

The DDI shall report to the Board monthly on the System's rebalancing activities, including any exceptions to policy.

Social Investment Procedures

Since it is necessary for adequate recognition to be given to the social consequences of corporate actions and security and portfolio investment decisions to achieve maximum long term investment returns from System assets, and since the individual decisions of Staff, Managers, Consultants, and other System fiduciaries have to be made within a framework that reflects the particular social situation and concerns of the participants and the System, the Retirement Board has adopted a set of Social Investment Procedures to guide the System. Social concerns to be addressed through investment policy shall follow the order of action as outlined in these policies. In no event shall these policies take precedence over the fiduciary responsibility of producing investment returns for the exclusive benefit of the participants. Exceptions to the restrictions on securities holdings outlined here may be made as needed to permit investment in commingled holdings deemed to be in the best interests of SFERS and its beneficiaries.

The investment restrictions based on these procedures are as follows:

Tobacco-Related Holdings

SFERS does not permit its managers (including internal management) to hold securities of US-based companies involved in the production of tobacco products. This restriction applies to both US equity holdings and to US corporate bond holdings.

The Board will periodically review the impact of this restriction on its overall performance.

Sudan Related Holdings

Because the US Congress and the State Department have found the Sudanese Government to be complicit in genocide in the Darfur region, SFERS does not permit its managers (including internal management) to hold securities of companies doing business in Sudan based on criteria established by SFERS. The Retirement Board directed Investment Staff to inform companies meeting specified criteria of SFERS' intention to divest. Companies will have 90 days to respond. Managers will be informed of companies meeting specified criteria and be given an opportunity to explain why they cannot achieve their mandate if required to divest.

The Social Investment Procedures and lists of restricted securities based on the above may be found in Tab 10 of this document. The Board will periodically review the impact of this restriction on its overall performance.

Asset Class Definitions

SFERS will utilize the following portfolio components to fulfill the asset allocation targets and total fund performance goals established elsewhere in this document.

I. Capital Appreciation – The Capital Appreciation portfolio will serve as the long term "growth" engine of the portfolio. This portfolio will be the primary source of return as well as risk (volatility) for the portfolio. The Plan's Capital Appreciation portfolio may be comprised of different market segments and approaches, including:

- **Public Market Equities –** SFERS anticipates that total returns to equities will be higher than total returns to fixed income securities over the long run, and may be subject to greater volatility. SFERS' equity holdings will be well diversified with respect to region, capitalization ranges and investment styles. The public market equity components in the Plan's asset allocation mix are:
    - **US Equities –** This segment of the portfolio will provide broadly diversified exposure to the US equity market, in both large and small cap market segments, as well as diversified exposure to different style segments (e.g., growth and value). Passive, enhanced passive, and active management strategies may be used in US equity holdings, including internal management by SFERS' Staff.
    - **International Equities –** This portfolio provides access to equity markets outside the US and

consequently plays a significant role in diversifying SFERS' domestic equity portfolio. A core international segment will concentrate on larger companies in developed non-US equity markets while a small capitalization segment will ensure exposure to the smaller companies that are primarily located in developed markets. Both passive and active management may be used in the core international equity portfolio, although active strategies will be emphasized. An emerging markets segment further diversifies the developed market segments by investing in developing markets that have lower correlations with developed economies. As specified in their investment guidelines, active managers may be given discretion to hedge currency exposure in their portfolios. The System may retain external experts to provide currency overlay management.

- **Global Equities –** A global stock portfolio will invest in both US and non-US companies, including emerging markets. Managers will have the discretion to allocate between US and non-US companies depending on their view of opportunities, valuations, and growth prospects.

- **Opportunistic strategies** may also be included in the Public Market Equity segment for the purpose of enhancing return, managing risk, and/or taking advantage of management approaches or hybrid securities that embody equity as well as other characteristics.

- **Alternative Investment Program ("AIP" or the "Program") –** This portfolio is a significant source of investment return that has lower correlation with SFERS' other asset classes. The AIP will include investments in a variety of separate account or commingled/partnership vehicles including venture capital, buyout, turnaround, mezzanine, distressed securities, co-investments and direct investments, and special situations funds. The Program is recognized to be long-term in nature and highly illiquid. Because of their higher risk and illiquidity, alternative investments are expected to provide substantially higher returns over the long term than publicly traded equity securities. Alternative investments can also include more conservative but also relatively illiquid investments, which derive their returns from owning hard and natural resource related assets such as oil- and gas-related properties and timberland.

  The primary objective of the AIP is to provide a substantial return premium (500 basis points or more) over the S&P 500 Index over rolling 10-year periods. This hurdle will be used to evaluate all alternative investment opportunities. The Program will also evaluate opportunities based on whether they diversify the Plan by investment type and by manager to reduce manager and asset-specific risks. A third objective of the program is to reduce total portfolio volatility by investing in assets with a lower correlation to public equity markets.

  The Senior Investment Officers or Senior Portfolio Managers overseeing the Alternative Investment Program, Staff (including the Deputy Division Director for Private Markets), in conjunction with the Alternative Investment Consultant, will annually update the Statement of Objectives, Policies and Procedures for the asset class and submit to the Retirement Board for approval. Additionally, the Senior Investment Officers or Senior Portfolio Managers overseeing the Alternative Investment Program, in conjunction with the Alternative Investment Consultant, will normally submit an Annual Investment Plan no later than the December meeting of the Retirement Board for Board approval. The Annual Investment Plan will recap the status of the Program and achievement of plan goals, and will identify investment initiatives for the following calendar year. Upon adoption by the Retirement Board, the Statement of Objectives, Policies and Procedures and Annual Investment Plans (Tabs 4 and 5) shall become a part of this Investment Policy Statement.

II. Capital Preservation – The Capital Preservation portfolio is intended to provide "downside protection" to the portfolio in periods of financial market duress or disinflation by providing a stable return. Capital Preservation also aids in the diversification of the Plan's assets. The Capital Preservation portfolio may be comprised of different market segments and approaches, including:

- **Public Market Fixed Income** – The primary role of the Fixed Income portfolio is to provide a stable, predictable income while diversifying SFERS' investment portfolio. SFERS' Fixed Income portfolio will be well diversified, and may include, but not limited to, both investment grade and non-investment grade holdings, US and non-US issues, developed and emerging market debt, mortgage-backed securities and direct mortgage holdings, and dollar and non-dollar denominated holdings. Internally managed fixed income as well as specialty managers may be utilized. Both passive and active management may be used in the Fixed Income portfolio. Currency exposure may be actively managed by the System's Fixed Income manager(s) as specified in the manager's guidelines. Opportunistic strategies may also be included in the Fixed Income portfolio for the purpose of enhancing return, managing risk, or taking advantage of management approaches or hybrid securities that embody fixed income as well as other characteristics.

- **Cash** – Cash will be segmented into two categories:

  - **Cash needed for Payment of Benefits and Expenses** – This is cash that will be set aside for the specific purpose of paying benefits and expenses. This cash should generally not be used to meet capital calls or other investment funding requirements. The amount of cash "set aside" for this purpose should not be less than one or more than four months funding requirement, with a target of three months.

  - **Cash Available for Investment** – This is cash which is available for investment following SFERS' Investment Guidelines contained herein. As a matter of principle, SFERS will strive to maintain a "zero cash" policy, i.e., all funds available for investment should be kept invested in accordance with this Investment Policy. Cash Available for Investment should not exceed 1% of Plan assets, with a target of 0%.

III. Inflation Hedges/Real Assets – Inflation Hedges/Real Assets are assets that provide investors with a better hedge against loss of purchasing power than traditional asset classes including equities and bonds. Moreover, these strategies maintain lower correlation to traditional asset classes, providing diversification benefits. The Plan's Inflation Hedges/Real Assets portfolio may be comprised of different market segments and approaches, including:

- **Real Estate –** SFERS' real estate program (the "Program") invests in real estate commingled funds, co-investments and separate accounts. The Program is diversified by property type and geography, exposed to properties both in the US and internationally, and includes global publicly listed real estate securities. The Program is designed to provide return from both income and capital appreciation. Real estate performance generally has low correlation with traditional public market asset classes, and therefore provides diversification benefits to the Plan. SFERS recognizes the illiquid, long-term nature of its private real estate portfolio and the role the Program plays in providing diversification to the overall portfolio. The Program is also a hedge against the possibility of severe and persistent inflation. SFERS has determined that active management will lead to returns that are superior for real estate than passive management strategies. Active management, value creation strategies, and the prudent use of third party debt are approved methods for generating the expected excess return.

The Senior Investment Officer or Senior Portfolio Manager overseeing the Real Estate portfolio, Staff (including the Deputy Division Director for Private Markets), and the Real Estate Consultant annually update the Investment Objectives, Policies and Procedures and the Annual Investment Strategy for the asset class and submit these documents to the Retirement Board for approval. The Annual Investment Plan recaps the status of the Program and the achievement of plan goals, and identifies investment strategies, projects and programs for the following fiscal year. Upon adoption by the Retirement Board, the Investment Objectives, Policies and Procedures and the Annual Investment Strategy (Tabs 2 and 3, respectively) shall become a part of this Investment Policy Statement.

GENERAL INVESTMENT OBJECTIVES AND GUIDELINES FOR PUBLIC MARKET SECURITIES

Public Market Equity Portfolios

The public equity portfolios, both internal and external, will be managed on a total return basis following specific investment styles and will be evaluated against specific market benchmarks that represent their investment style. These benchmarks will be specified in the written investment guidelines governing each portfolio. In the case of active managers where such comparisons are applicable, investment results will also be compared to returns of a peer group of managers with similar styles. These benchmarks may also be modified, as appropriate to the manager's investment style, to exclude US tobacco stocks. General equity guidelines for active managers include the following.

- SFERS' holdings by all managers in aggregate in a single stock shall not constitute more than 5% of the outstanding voting stock of any company.
- Unless authorized in guidelines, equity managers' cash holdings shall not exceed 5% of portfolio market value.
- American Depositary Receipts or other depository receipts listed on a major stock exchange or on the NASDAQ are permitted if specified in the managers' guidelines.
- Convertible securities may be held in equity portfolios if authorized in guidelines, and shall be considered equity holdings.
- Securities must be traded on a regulated stock exchange, or listed on the NASDAQ or a comparable foreign market operation.
- Forward or futures contracts for foreign currencies may be entered into for hedging purposes or pending the selection and purchase of suitable investments in or the settlement of any such securities transactions only in portfolios designated specifically to hold these types of securities (i.e., currency overlay).

Any exemption from these general guidelines requires review by Investment Staff and approval from the Board.

Fixed Income Portfolios

The internal and external fixed income portfolios will be managed on a total return basis, following specific investment styles and will be evaluated against specific market indices that represent a specific investment style or market segment. Where applicable, fixed income portfolio investment results will also be compared to returns of a peer group of managers investing with a similar style.

General fixed income guidelines for active managers include the following:

- Permissible securities shall include, but are not limited to, cash equivalents, forward foreign exchange contracts, currency futures, financial futures, government and government agency bonds, Eurobonds, mortgage backed securities (including collateralized mortgage obligations, commercial mortgages, commercial mortgage backed securities, asset-backed bonds, corporate bonds (including convertible bonds), or other securities specifically authorized by the Retirement Board and incorporated in the Manager's Investment Guidelines. If authorized in written guidelines, derivatives, including forward or futures contracts for foreign currencies, may be used to control risk and augment return, or to effect portfolio management decisions in a timely, cost-effective manner.

Any exemption from these general guidelines requires review by Investment Staff and approval from the Retirement Board.

INVESTMENT MANAGER POLICY

The selection of investment managers will be accomplished in accordance with all applicable Local, State and Federal laws and regulations. Each investment manager must function under a formal contract that delineates responsibilities, establishes guidelines, and articulates performance expectations.

Specific policies with respect to managers in non-public market segments are addressed in the Real Estate Investment Objectives, Policies and Procedures (Tab 2) and the Alternative Investments Statement of Objectives, Policies and Procedures (Tab 4).

SFERS will utilize both internally and externally managed portfolios based on specific styles and methodologies. The external managers will be expected to acknowledge in writing that they are Plan fiduciaries and will have discretion and authority to determine investment strategy, security selection and timing within their assigned mandate, and subject to IPS guidelines and any other guidelines specific to their portfolio. Performance of each portfolio will be monitored and evaluated on a regular basis relative to a suitable benchmark and, where appropriate, relative to a peer group of managers with similar investment styles.

A policy framework for Opportunistic Strategies in Global Equity and Public Market Fixed Income is included at Tab 9 of this Investment Policy Statement.

Investment managers, as prudent experts, will be expected to know SFERS' policies (as outlined in this and other appropriate documents) and any specific guidelines for their portfolios, and to comply with those policies and guidelines. It is each manager's responsibility to identify policies and guidelines that may have an adverse impact on performance, and to initiate discussion with Staff toward possible improvement of said policies or guidelines through Board action.

The Board and Staff will also review each investment manager's adherence to investment guidelines, and any material changes in the manager's organization (e.g., personnel changes, new business developments, etc.). The investment managers retained by SFERS will be responsible for informing the Board and Staff of all such material changes on a timely basis.

SFERS shall follow the Guidelines for Manager Monitoring and Retention that appears at Tab 7 in evaluating its fixed income and equity managers.

Investment managers under contract to SFERS shall have discretion to establish and execute transactions with any securities broker/dealer as the manager determines to be in the best interest of SFERS. The investment managers must obtain the best available prices and most favorable executions with respect to all portfolio transactions, keeping in mind SFERS' desire to transact with commission recapture and emerging brokers, as market conditions permit. Unless otherwise approved in writing, managers are prohibited from engaging in transactions with an affiliated broker/dealer.

Selection Criteria for Investment Managers

Criteria will be established for each manager search undertaken by SFERS, and will be tailored to SFERS' needs in each search.

In general, eligible managers will possess attributes including, but not limited to, the following:

- The firm must be SEC-registered or exempt from registration. Firms claiming exemption from registration requirements must provide appropriate documentation and disclosures indicating reasons for exemption.
- The firm or its senior investment professionals must be experienced in managing money for institutional clients in the asset class/product category/investment style specified by SFERS.
- The firm must display a record of stability in attracting and retaining qualified investment professionals, as well as a record of managing asset growth effectively, both in gaining and retaining clients.
- The firm must have an asset base sufficient to accommodate SFERS' portfolio. In general, firms should have at least $250 million of discretionary institutional assets under management, and SFERS' portfolio should make up no more than 20% of the firm's total asset base after funding. Exceptions may be made on a case-by-case basis.
- The firm must demonstrate adherence to the investment style sought by SFERS, and adherence to the firm's stated investment discipline.
- The firm's fees should be competitive with industry standards for the product category.
- The firm must comply with the "Duties of the Investment Managers" outlined herein and conform to CFA Institute/Global Investment Performance Standards for performance reporting.

When making a recommendation to retain a manager, any exceptions to these attributes for a recommended manager shall be noted to the Board in writing by Staff or the General Investment Consultant.

Criteria for Investment Manager Termination

SFERS reserves the right to terminate an investment manager at any time for any reason. Guidelines for manager monitoring and retention are included at Tab 7.

Grounds for investment manager termination may include, but are not limited to, the following:

- Failure to comply with the guidelines agreed upon for management of SFERS' portfolio, including holding any restricted issues.
- Failure to achieve performance objectives specified in the manager's guidelines.
- Significant deviation from the manager's stated investment philosophy and/or process.
- Loss of key personnel or changes in ownership structure.
- Evidence of illegal or unethical behavior by the investment management firm or its principals.
- Lack of willingness to cooperate with reasonable requests by SFERS for information, meetings or other material related to its portfolios.
- Loss of confidence by the Board or Staff in the investment manager.
- A change in the Plan's asset allocation program, which necessitates a shift of assets to another sub-asset class or sector.

The presence of any one of these factors will be carefully reviewed by SFERS' Staff and the Board, but will not necessarily result in an automatic termination.

DUTIES OF RESPONSIBLE PARTIES

Duties of the SFERS Board

The Board will adhere to the following procedures in the management of SFERS' assets:

- The Board's primary responsibility is to set the policy framework in which the implementation of SFERS' investment program will take place. Staff will be responsible for the timely implementation and administration of the Board's policy decisions.
- The Board shall formally review SFERS' investment structure, asset allocation and financial performance at least every three years, or more frequently should capital markets or the financial condition of the Plan undergo a material, long-term change necessitating such a review. The review will include recommended adjustments to the long-term, strategic asset allocation to reflect any changes in applicable regulations, long-term capital market assumptions, actuarial assumptions or SFERS' financial condition.
- The Board shall review target allocations and allowable ranges to asset class sub-sectors in the public markets portion of the Plan on at least an annual basis.
- The Retirement Board shall review SFERS' investment results at least quarterly,[2] or more often as needed, to ensure that policy guidelines continue to be met. The Board shall monitor investment returns on both an absolute basis and relative to appropriate benchmarks and peer group comparisons. The sources of information for these reviews shall include Staff, outside consultants, the custodian, the performance measurement provider, and SFERS' investment managers.
- The Board may retain investment consultants to provide such services as conducting performance and manager reviews, asset allocation, and investment research. The comments and recommendations of the consultants will be considered in conjunction with other available information to aid the Board in making informed, prudent decisions. In selecting external consultants, the Board shall consider the recommendations of Staff.
- The Board shall be responsible for taking appropriate action if investment objectives are not being met or if policies and guidelines are not being followed.
- The Board shall direct Staff to administer SFERS' investments in a cost-effective manner subject to Board approval. Investment-related costs include, but are not limited to, management, consulting and custodial fees, transaction costs and other administrative costs chargeable to SFERS.
- The Board shall be responsible for selecting a qualified custodian with advice from Staff, and from the Consultant(s) if directed by the Staff or the Board.
- The Board shall provide oversight of the effectiveness of Staff's implementation of its policy directives.

Duties of the Investment Staff

SFERS' Investment Staff plays a significant role in the management and oversight of the Plan, and is responsible for the timely implementation and administration of the Board's policy decisions. The Board shall monitor the performance of the Investment Staff in carrying out the duties, which include:

- Managing investment funds according to written investment guidelines as directed by the Board.
- Carrying out rebalancing activity in accordance with the policy stated in this document.

[2] Performance of Alternative assets and equity real estate is reviewed semi-annually.

- Monitoring external managers for adherence to SFERS' written policies and guidelines, and in accordance with SFERS' Manager Monitoring and Retention Policy for Equity and Fixed Income. Reviews for portfolios managed by external managers will focus on:
  1. Compliance with the investment guidelines.
  2. Compliance with the terms of the contracts, and the manager's ability to provide the System with timely, accurate and useful information.
  3. Manager's ability to continue to achieve its objectives given its investment process and resources.
  4. Material changes in a manager's organization. This may include, but is not limited to changes in investment philosophy, personnel or ownership, acquisitions or losses of major accounts, etc. The manager will be responsible for advising SFERS' Staff of any material changes in personnel, investment strategy, or other pertinent information potentially affecting performance.
  5. Investment performance relative to each manager's stated performance benchmark(s) as set forth in the manager's investment guidelines as well as the manager's rankings in an appropriate peer group comparison.
  6. Manager's status under the Plan's policies related to Manager Monitoring and Retention.
- Providing due diligence, oversight, and investment recommendations regarding all investment portfolios, including real estate and alternative investments, with assistance from the respective Consultant(s).
- Identifying, measuring and evaluating risk in SFERS' public market holdings.
- Evaluating and managing relationships with the Consultant(s) to the Plan to ensure that the Consultant(s) are providing all the necessary assistance to Staff and the Board as set forth in their service contracts and meeting the needs of the System.
- Making recommendations to the Board regarding retention of Consultant(s).
- Conducting manager searches with assistance from Consultant(s).
- Managing portfolio restructurings resulting from manager terminations with the assistance of Consultants, managers, or other parties, as needed.
- Conducting, directing Consultants and/or managers to conduct, or participating in any special research required to manage the Plan more effectively and in response to any questions or issues raised by the Retirement Board.
- Reviewing the cost-effectiveness and performance of the custodian on a regular basis (at least every five years), with input from SFERS' Consultants as needed or as directed by the Board.
- Monitoring and reviewing the System's securities lending program (if any) on an ongoing basis.
- Monitoring on an ongoing basis the services provided by the commission recapture brokers so as to ensure that the investment managers are securing the best execution of SFERS' brokerage transactions.
- Supporting the Board in the development and approval of the Real Estate Annual Investment Strategy and Annual Investment Plan for Alternative Investments, implementing and monitoring the Plan, and reporting at least quarterly on investment activity and matters of significance.

Duties of the Investment Managers

The duties of the Investment Managers shall include:

- Provide the Plan with a written agreement to invest within the guidelines established.
- Provide the Plan with proof of liability and fiduciary insurance coverage on an annual basis.
- Be an SEC-Registered Investment Advisor under the 1940 Act or exempt from registration, and be

recognized as providing demonstrated expertise over a number of years in the management of institutional, tax-exempt assets within a defined investment specialty.

- Adhere to the investment management style, concepts and principles for which they were retained, including, but not limited to, developing portfolio strategy, performing research, and purchasing and selling securities.
- Execute all transactions for the benefit of the Plan with brokers and dealers qualified to execute institutional orders on an ongoing basis at the best net cost to the Plan, and, where appropriate, facilitate the recapture of commissions on behalf of the Plan.
- Reconcile monthly accounting, transaction and asset summary data with custodian valuations, and communicate and resolve any significant discrepancies with the custodian.
- Maintain frequent and open communication with the System on all significant matters pertaining to the Investment Plan, including, but not limited to, the following:

1. Major changes in the Investment Manager's investment outlook, investment strategy and portfolio structure;
2. Significant changes in ownership, organizational structure, financial condition or senior personnel;
3. Any changes in the Portfolio Manager(s) or other personnel assigned to the Plan;
4. Each client which terminates its relationship with the Investment Manager, and whose assets represent 5% of the firm's AUM or $100 million, whichever is less, within 30 days of such termination;
5. All pertinent issues which the Investment Manager deems to be of significant interest or material importance to its investment process; and
6. Meet with the Staff or the Board on an as-needed basis.

Duties of the Master Custodian

The Master Custodian shall be responsible for the following actions:

- Provide complete global custody and depository services for the designated accounts.
- Manage, if directed by the Board, a Short Term Investment Fund for investment of any cash not invested by managers, and ensure that all available cash is invested in this or other fixed income vehicles approved by the Board for this purpose. If the cash reserves are managed externally, full cooperation must be provided to the external cash manager.
- Provide in a timely and effective manner a monthly report of the investment activities implemented by the investment managers and the performance of each portfolio.
- Collect all income and principal realizable and properly report it on the periodic accounting statements.
- Provide monthly and fiscal year-end accounting statements for the portfolio, including all transactions; these should be based on accurate security values for both cost and market. These reports should be provided within acceptable time frames.
- Report to SFERS' Staff situations where accurate security pricing, valuation and accrued income is either not possible or subject to considerable uncertainty.
- Reconcile monthly with SFERS investment managers on price variance and portfolio valuation.
- Provide assistance to the Plan to complete such activities as the annual audit, transaction verification or other unique issues as required by the Board.
- Manage a securities lending program to enhance income if directed to do so by the Board. The custodian may also be called upon to manage the cash collateral associated with the securities lending program. If the securities lending program is managed externally, full cooperation must be provided to the external securities lending agent.

Duties of the Investment Consultants

The selection of Consultants will be accomplished in accordance with all applicable Local, State and Federal laws and regulations. Each Consultant shall be a co-fiduciary to the Plan, and must function under a formal contract that delineates responsibilities and appropriate performance expectations.

Consultants shall have no discretionary authority (unless such authority is delegated contractually by the Board and the Consultant). They shall be responsible for making timely and appropriate recommendations on investment policy issues, for monitoring managers, and for reporting on performance results on a quarterly basis. The Board and Staff will consider the comments and recommendations of Consultants in conjunction with other available information in making informed, prudent decisions.

Each Consultant shall abide by The Code of Ethics and The Standards of Professional Conduct established by the CFA Institute (formerly the Association for Investment Management and Research) in carrying out its responsibilities with respect to SFERS. The CFA Institute Code appears at Tab 6.

The General Investment Consultant shall be responsible for the following actions:

- Make recommendations to the Board and Staff regarding investment policy and strategic asset allocation, including sub-asset class structure.
- Assist SFERS Staff in the selection of qualified investment managers, and make recommendations to the Board and Staff on manager selection and manager guidelines.
- Assist Staff in the oversight of existing managers, including monitoring changes in personnel, organization, ownership, the investment process, compliance with guidelines, and other issues likely to affect performance.
- Assist Staff in the selection of a qualified custodian (including a securities lending agent and/or a cash manager) if directed by the Board and Staff.
- Prepare quarterly performance summaries regarding SFERS' manager, composite, and total plan results and make recommendations addressing any performance issues.
- Provide topical research and education on investment subjects that are relevant to SFERS.
- Other tasks as requested by the Board or Staff consistent with the function served by the General Investment Consultant.

The Real Estate Consultant shall be responsible for the following actions:

- Make recommendations to the Board and SFERS Staff regarding investment policy and strategic asset allocation as they pertain to real estate, and regarding public market securities that are affected by real estate-related issues.
- Assist SFERS Staff in the selection of qualified real estate investment managers and make recommendations to the full Board on manager selections. This will also include selection of managers of public market securities requiring real estate expertise.
- Assist SFERS Staff in the oversight of existing managers including monitoring changes in personnel, ownership and the investment process.
- Prepare a semi-annual performance report including performance of SFERS' real estate investment managers and total real estate assets, including a check on guideline compliance and adherence to investment style and discipline.
- Provide topical research and education on real estate investment subjects that are relevant to SFERS.
- Other tasks as requested by the Board or Staff consistent with the function served by the Real Estate

Consultant.

The Alternative Asset Investment Consultant shall be responsible for the following:

- Make recommendations to the Board and SFERS Staff regarding investment policy and strategic asset allocation as they pertain to alternative investments.
- Assist SFERS Staff in the selection of qualified alternative asset investment managers and make recommendations to the full Board for selections requiring Board ratification.
- Assist in the oversight of existing managers (including any public market securities managers related to the Alternative Investment portfolio), including monitoring changes in personnel, ownership and the investment process.
- Prepare a semi-annual performance report including performance of SFERS' alternative asset managers and total alternative asset holdings, program policy guidelines, and adherence to investment style and discipline.
- Provide topical research and education on investment subjects that are relevant to SFERS, especially those that relate to alternative investments.
- Other tasks as requested by the Board or Staff consistent with the function served by the Alternative Asset Consultant.

Duties of the Proxy Consultant

- Make recommendations to the Retirement Board regarding voting of proxies.
- Assist Staff in implementation of the Retirement Board's policy on voting proxies.
- Prepare an annual report documenting proxy voting activities performed on behalf of SFERS.

Duties of the Performance Measurement Provider

- The performance measurement provider shall provide regular performance reports including performance attribution of SFERS' asset class composites and total assets, and a check on guideline compliance and adherence to investment style and discipline. Performance calculations shall conform to the CFA Institute's Global Investment Performance Standards.

Tab I
Strategic Asset Allocation

	Target Percent	Allowable Range	Composite Benchmark
Growth/Capital Appreciation	**63%**	**53-73%**	
Global Equity	*47.0%*	*40-54%*	*MSCI ACWI Investable Market Index ($, ND)*
Alternative Assets (Private Equity)	*16%*	*10-20%*	*S&P 500 + 500 bps annualized (long-term)*
Real Assets/Inflation Hedge	**12%**	**9-15%**	
Real Estate (including REITs)	*12%*	*9-15%*	*8%*
Capital Preservation/Risk Reduction	**25%**	**20-30%**	
Fixed Income	*25%*	*20-30%*	*100% Barclays Capital US Universal Index*
Cash	*0%*	*0-1%*	*90-day Treasury Bills*
Total Fund Composite	**100%**		**Benchmarks Weighted by Strategic Allocation Targets**

Note: Asset Allocation Targets Approved: October 10, 2012.

Tab I (continued)
Sub-Asset Class Targets

Global Public Market Equity

	Target Percent of Asset Class	*Sub-Asset Class Minimum*	*Sub-Asset Class Maximum*
Passive S&P 500	16%	*10%*	*22%*
Enhanced S&P 500	5%	*0%*	*7%*
US Large Cap Value	9%	*6%*	*12%*
US Large Cap Growth	9%	*6%*	*12%*
US Small Cap	6%	*4%*	*8%*
US Convertibles	3%	*0%*	*5%*
Core International	14%	*9%*	*19%*
Growth International	5%	*3%*	*7%*
Value International	11%	*7%*	*15%*
Small Cap International	6%	*4%*	*8%*
Emerging Markets	11%	*7%*	*15%*
Global Equity	5%	*0%*	*7%*
Opportunistic Strategies	0%	*0%*	*10%*
Currency Overlay *(% of the International Equity composite to be overlaid)*	*50% of Intl Equity Holdings*	*25% of Intl Equity Holdings*	*55% of Intl Equity Holdings*

Equity sub-asset class targets reviewed and approved October 10, 2012.

Fixed Income

	Target Percent of Asset Class	Sub-Asset Class Minimum	Sub-Asset Class Maximum
Internal Fixed Income	6%	0%	20%
BC Aggregate Index Fund	6%	0%	20%
Core/CorePlus US Bonds	59%	45%	70%
Commercial Mortgages	7%	5%	13%
High Yield Corporates/Bank Loans	8%	6%	10%
High Yield CMBS	5%	3%	10%
Emerging Market Debt	9%	4%	14%
Opportunistic Strategies	0%	*0%*	*10%*

Fixed Income sub-asset class targets reviewed and approved October 10, 2012.

CERBT Statement of Investment Policy

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
STATEMENT OF INVESTMENT POLICY

FOR
THE CALIFORNIA EMPLOYERS' RETIREE BENEFIT TRUST (CERBT) FUND

December 3, 2013

This policy is effective immediately upon adoption and supersedes all previous policies governing the Annuitants' Healthcare Coverage Fund, also known as the California Employers' Retiree Benefit Trust (CERBT) Fund.

I. PURPOSE

The California Public Employees' Retirement System ("CalPERS") Investment Beliefs Policy and Total Fund Statement of Investment Policy, adopted by the CalPERS Investment Committee ("Committee"), set forth CalPERS overarching investment purposes and objectives with respect to all its investment programs.

This document sets forth the investment policy ("Policy") for the policy portfolios ("Portfolios") of the California Employers' Retiree Benefit Trust ("CERBT"). The design of this Policy ensures that investors, managers, consultants, and other participants selected by CalPERS take prudent and careful action while managing the Portfolios. Additionally, use of this Policy ensures sufficient flexibility in managing investment risks and returns associated with the CERBT.

The CERBT was established March 1, 2007 for public employers to prefund their retiree health and other post-employment benefit obligations. The CERBT is currently known in statute as the Annuitants' Healthcare Coverage Fund. There are three separate Portfolios ("Strategy 1", "Strategy 2", and "Strategy 3") for the CERBT, which provide employers a choice of asset allocation strategies.

II. STRATEGIC OBJECTIVE

Each of the CERBT Portfolios shall be managed to accomplish the following:

A. Offer to employers a distinct investment alternative.

B. Invest in an asset allocation mix with targets and ranges based on a periodic asset liability management review.

C. Maintain significant diversification to temper losses from market volatility.

D. Ensure that the asset class policy ranges approved by the Committee are adhered to, and that any rebalancing is performed efficiently and prudently.

E. Maintain adequate liquidity to meet cash needs.

III. RESPONSIBILITIES

A. In addition to the Committee's responsibilities outlined in the Total Fund Statement of Investment Policy, the Committee is also responsible for approving asset classes for investment and approving a policy target allocation, permissible range, and benchmark for each asset class.

B. CalPERS Investment Staff ("Staff") is responsible for the following:

1. All aspects of portfolio management including monitoring, analyzing, and evaluating performance relative to the appropriate benchmark.

2. Providing individualized asset allocation strategy recommendations to the Committee, including selection of asset class benchmarks, Policy targets and ranges.

3. Managing the asset class allocations of the Portfolios within Policy ranges approved by the Committee, in accordance with Policy guidelines.

4. Creating internally managed funds and soliciting externally managed funds to be used in the composition of the Portfolios.

5. Identifying opportunities and making recommendations to the Committee consistent with pertinent delegations.

6. Reporting internally to the Committee concerning the implementation of this Policy. This report shall include, but is not limited to, the current market value and asset allocations compared to the Policy targets and ranges.

7. Monitoring the implementation of, and compliance with, the Policy. Staff shall report concerns, problems, material changes, and all violations of Guidelines and Policies at the next Committee meeting, or sooner if deemed necessary. All events deemed materially important will be reported to the Committee immediately. These reports shall include explanations of any violations and appropriate recommendations for corrective action.

C. The General Pension Consultant ("Consultant") is responsible for monitoring, evaluating, and periodically reporting to the Committee on the three CERBT Portfolios' performance relative to the benchmark and Policy.

D. External Managers ("Manager") are responsible for aspects of portfolio management as set forth in each Manager's contract with CalPERS and shall fulfill the following duties:

1. Communicate with CalPERS staff, as needed, regarding investment strategies and investment results.

2. Monitor, analyze, and evaluate performance relative to the agreed-upon benchmark.

3. Cooperate fully with CalPERS staff, Custodian and Consultant concerning requests for information.

IV. PERFORMANCE OBJECTIVE AND BENCHMARK

A. The benchmark for the CERBT is specified in the Benchmarks Policy.

B. CalPERS shall invest the assets of each of the CERBT Portfolios to meet or exceed the individualized benchmark designated in the Policy.

V. INVESTMENT APPROACHES AND PARAMETERS

A. Philosophy and Approach

The CERBT Portfolios shall be managed in accordance with the CalPERS Total Fund Statement of Investment Policy and in a manner consistent with the respective investment policy governing each asset class. Such policies approved by the Committee shall specify the method and parameters for implementation and provide for the ongoing monitoring of that asset class.

B. Strategic Asset Allocation Process

A comprehensive asset allocation strategy analysis shall be completed at least once every three years and will be presented to the Committee for review and approval of the Policy target asset allocation and ranges. The Chief Investment Officer ("CIO") may recommend a more frequent analysis if expected returns, risks or liability values have substantially changed since the prior analysis. The CIO may also recommend to the Committee changes in the Policy asset allocation targets and ranges. A target for cash is exempt from consideration.

C. Fund Structure/Parameters

Staff shall manage the Portfolios in accordance with the approved strategic asset allocation. CalPERS Custodian shall employ a unitized fund structure to maintain separate and distinct historical records and to produce individual net asset values (NAV's) for each asset class.

D. Policy Asset Allocation Targets and Ranges

The Committee shall approve Policy asset allocation targets and ranges expressed as a percentage of total assets. The Committee shall set Policy ranges sufficiently wide to permit efficient and flexible implementation, yet sufficiently narrow to maintain the basic risk and return relationship established by the allocation targets.

There are three separate CERBT Portfolios ("Strategy 1", "Strategy 2", and "Strategy 3"). Levels of expected return and risk vary among the Portfolios. The Policy asset allocation targets and permissible ranges are as follows:

Asset Class	**Strategy 1**		**Strategy 2**		**Strategy 3**	
	Policy Allocation	**Policy Range**	**Policy Allocation**	**Policy Range**	**Policy Allocation**	**Policy Range**
U.S Inflation Linked Bonds	5%	+/- 2%	15%	+/- 4%	15%	+/- 4%
U.S. Nominal Bonds	18%	+/- 5%	24%	+/- 5%	42%	+/- 5%
Global Equity	66%	+/- 5%	50%	+/- 5%	32%	+/- 5%
Global Public Real Estate	8%	+/- 2%	8%	+/- 2%	8%	+/- 2%
Commodities	3%	+/- 2%	3%	+/- 2%	3%	+/- 2%
Expected Return	7.10%		6.50%		5.75%	
Expected Risk	11.73%		9.46%		7.27%	
Return/Risk	0.61%		0.69%		0.79%	

Approved by the Committee, August 15, 2011.

E. Rebalancing

Adherence to the Policy asset allocation targets and ranges shall be monitored and reported to the Committee as part of the quarterly performance report. This report shall display a comparison between the Portfolios' asset class allocations and the Policy asset allocation targets and ranges. The report shall also compare the investment performance results of each asset class and the benchmark returns.

Asset class allocations shall be managed to be within Policy ranges. Cash in the portfolio will be held within a range of 0 – 1%. Allocations may temporarily deviate from Policy ranges due to employer contributions and/or extreme market volatility. If an asset class allocation exceeds the Policy range, staff shall return the asset allocation to within its Policy range in a timely manner, with the exact time period primarily dependent on transaction costs and liquidity.

Changes in Policy asset class allocations may be achieved by the movement of capital between asset classes through the trading of pooled funds or through the use of derivatives. The intent is for Policy asset class allocations to be actively managed rather than being allowed to passively drift with recent relative asset class returns.

F. Restrictions, Prohibitions and Authorized Securities

Restrictions, Prohibitions and Authorized Securities of the CERBT are defined in the policy governing each asset class or external investment manager guidelines.

All transactions involving derivatives are governed by the Global Derivatives and Counterparty Risk Policy.

VI. CALCULATIONS AND COMPUTATIONS

Investors, managers, consultants, and other participants selected by CalPERS shall make all calculations and computations on a market value basis, as recorded by CalPERS Custodian.

VII. GLOSSARY OF TERMS

Key words used in the policy are defined in CalPERS Master Glossary of Terms.

California Employers' Retiree Benefit Trust	
Approved by the Policy Subcommittee Adopted by the Investment Committee	June 15, 2011 August 15, 2011
Admin changes to update template format and to align this policy with the Global Derivatives and Counterparty Risk Policy	December 3, 2013

The California Employers' Retiree Benefit Trust was previously the Annuitants' Healthcare Coverage Fund and Attachment A of the Affiliate Fund Policy. The dates below reflect the revision history of the Affiliate Fund Policy:

Affiliate Fund Policy	
Approved by the Policy Subcommittee:	August 18, 2008
Adopted by the Investment Committee:	September 15, 2008
Revised by the Investment Committee:	December 15, 2008
Admin changes made due to Policy Review Project:	June 16, 2009
Admins changes due to adoption of Benchmark Policy:	September 28, 2009

Annuitants' Healthcare Coverage Fund (Policy consolidated into the Affiliate Fund Policy)

Approved by the Policy Subcommittee:	December 15, 2006
Adopted by the Investment Committee:	December 18, 2006
Repealed by the Policy Subcommittee:	August 18, 2008
Repealed by the Investment Committee:	September 15, 2008

CERBT Fund Facts as of Nov 2013

CERBT Strategy 1

California Employers' Retiree Benefit Trust (CERBT) | November 30, 2013

CalPERS

Objective

The objective of the CERBT Strategy 1 portfolio is to seek favorable returns that reflect the broad investment performance of the financial markets through capital appreciation and through investment income. There is no guarantee that the portfolio will achieve its investment objectives.

Strategy

The CERBT Strategy 1 portfolio is invested in various asset classes in percentages approved by the CalPERS Board. The specific percentages of portfolio assets allocated to each asset class are shown under "Composition". Generally, equities are intended to help build the value of the employer's portfolio over the long term while bonds are intended to help provide income and stability of principal. Also, strategies invested in a higher percentage of equities seek higher investment returns (but assume more risk) compared with strategies invested in a higher percentage of bonds.

Compared with other asset allocation strategies, this portfolio consists of a higher percentage of equities to bonds and other assets. Historically, equities have displayed greater price volatility and therefore this portfolio may experience greater fluctuation of value. Employers that seek higher investment returns, and are able to accept greater risk and tolerate more fluctuation in returns, may wish to consider this portfolio.

Information Provided in Lieu of Prospectus

The CERBT Strategy 1 portfolio consists of assets managed internally by CalPERS. Because it is not a mutual fund, a prospectus is not available. This summary is designed to provide descriptive information.

Assets Under Management

As of November 30, 2013, the aggregate total of assets under management for all CERBT Strategies was **$3,142,842,782.**

Composition

Asset Class Allocations and Benchmarks

The CERBT Strategy 1 portfolio may consist of the following asset class target allocations and corresponding benchmarks:

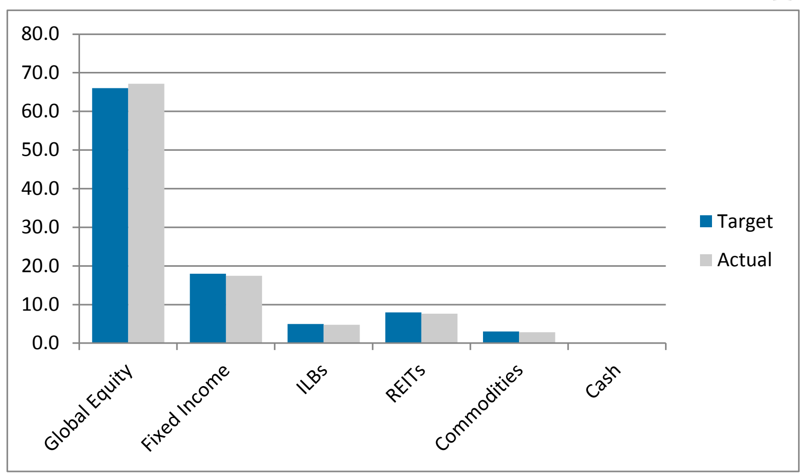
Asset Class	Benchmark
Global Equity	MSCI All Country World Index IMI (net)
U.S. Fixed Income	Barclays Capital Long Liability Index
Treasury Inflation-Protected Securities (TIPS)	Barclays Capital Global: US TIPS Index
Real Estate Investment Trusts (REITs)	FTSE EPRA/NAREIT Developed Liquid Index (net)
Commodities	S&P GSCI Total Return Index

Portfolio Benchmark

The CERBT Strategy 1 benchmark is a composite of underlying asset class market indexes, each assigned the target weight for the asset class it represents.

Target vs. Actual Asset Class Allocations

The following chart shows policy target allocations compared with actual asset allocations as of November 30, 2013. CalPERS may overweight or underweight an allocation to a particular asset class based on market, economic, or CalPERS policy considerations.



CERBT Strategy 1 Performance as of November 30, 2013							
	1 Month	3 Months	Fiscal YTD	1 Year	3 Years*	5 Years*	Since Inception* (June 1, 2007)
Returns before expenses[1]	0.43%	7.84%	9.52%	14.62%	10.78%	14.35%	3.99%
CERBT Strategy 1 Benchmark	0.37%	7.69%	9.39%	14.37%	10.72%	14.31%	3.53%

*Returns for periods greater than one year are annualized.

[1] See the Expenses section of this document.

Performance data shown represents past investment performance and is no guarantee of future results. The investment return and principal value of the portfolio will fluctuate so that an employers' account balance in the portfolio may be worth more or less than the amount invested. Current performance may be lower or higher than the performance data shown above.

CERBT Strategy 1

California Employers' Retiree Benefit Trust (CERBT) | November 30, 2013

CalPERS

General Information

What Employers Own

Each employer owns a percentage of the CERBT Strategy 1 portfolio, which invests in pooled asset classes managed by CalPERS. Employers do not have direct ownership of the securities in the portfolio.

Information Accessibility

Since the portfolio is not a mutual fund, information is not available from a newspaper source. Instead, CalPERS provides a quarterly statement of the employer's account. For current performance information, including performance to the most recent month-end, investment policy, and detailed asset allocation, please visit our website at: **www.calpers.ca.gov**.

Price

The value of the portfolio changes daily, based upon the market value of the underlying securities. Just as prices of individual securities fluctuate, the portfolio's value changes with market conditions.

Expenses

CERBT is a self-funded trust in which participating employers pay for all administrative and investment expenses. Expenses reduce the gross investment return by the fee amount. The larger the fee, the greater the reduction of investment return. Currently, CERBT expenses are accrued at an annual rate of 0.15% and charged daily to employer accounts. CERBT's actual expenses may differ from the amount currently being accrued due to factors such as changes in average fund assets or actual expenses. The expense accrual rate may change without notice in order to reflect changes in average portfolio assets or in expense amounts. The CalPERS Board annually reviews the operating expenses and changes may be made as appropriate. Even if the portfolio loses money during a period, the fee is still charged.

Portfolio Manager Information

The portfolio is managed by CalPERS Investment Office staff as directed by the CalPERS Investment Committee and Board of Administration.

Principal Risks of the Portfolio

An investment in the portfolio is not a bank deposit, and it is not insured nor guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. It is possible to lose money by investing in this portfolio. The portfolio's risk depends in part on the portfolio's asset class allocations and the selection, weighting and risks of the underlying investments. Some major risks associated with investing in equities, fixed income and other assets include:

- **Allocation Risk:** The portfolio's ability to achieve its investment objectives depends in part on the managers' skill in determining the portfolios' sector allocations and in selecting and weighting the underlying investments. The managers' evaluations and assumptions regarding asset classes and underlying investments may differ from actual market conditions.

- **Market Risk:** The value of the portfolio will go up and down based on the performance of the underlying investments in which it invests. The value of the underlying investments will, in turn, fluctuate based on the performance of the securities owned and other factors generally affecting the securities market.

- **Interest Rate Risk**: Generally, when interest rates rise, the value of an underlying investment's fixed income securities will decline. The opposite is true when interest rates decline.

- **Credit Risk**: The value of an underlying investment's fixed income securities will be adversely affected by any erosion in the ability of issuers of these securities to make timely interest and principal payments.

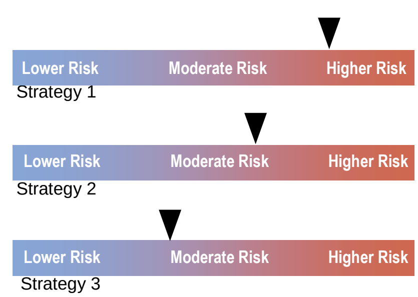
- **Foreign Risk:** Some of the underlying investments are in foreign securities, which are generally riskier than U.S. securities. As a result, the portfolio is subject to foreign risk, meaning that political events (such as civil unrest, national elections, and imposition of exchange controls), social and economic events (such as labor strikes and rising inflation), and natural disasters occurring in a country where the portfolio invests could cause the portfolio's investments in that country to experience losses.

- **Principal Loss:** Employers own a percentage of the CERBT Strategy 1 portfolio (expressed as "units"). At any given time, the value of an employer's units may be worth less than the price paid for them.

CERBT Strategy Risk Levels

CalPERS offers employers the choice of one of three investment strategies. Risk levels among strategies vary, depending upon the target asset class allocations. Generally, equities carry more risk than fixed income securities.

Asset Class Target Allocations	Strategy 1	Strategy 2	Strategy 3
Global Equity	66%	50%	32%
U.S Fixed Income	18%	24%	42%
TIPS	5%	15%	15%
REITs	8%	8%	8%
Commodities	3%	3%	3%



CERBT Strategy 2

California Employers' Retiree Benefit Trust (CERBT) | November 30, 2013

Objective

The objective of the CERBT Strategy 2 portfolio is to seek favorable returns that reflect the broad investment performance of the financial markets through capital appreciation and through investment income. There is no guarantee that the portfolio will achieve its investment objectives.

Strategy

The CERBT Strategy 2 portfolio is invested in various asset classes in percentages approved by the CalPERS Board. The specific percentages of portfolio assets allocated to each asset class are shown under "Composition". Generally, equities are intended to help build the value of the employer's portfolio over the long term while bonds are intended to help provide income and stability of principal. Also, strategies invested in a higher percentage of equities seek higher investment returns (but assume more risk) compared with strategies invested in a higher percentage of bonds.

Compared with other asset allocation strategies, this portfolio consists of a moderate allocation of equities, bonds, and other assets. Historically, funds with a higher percentage of equities have displayed greater price volatility. Therefore, this portfolio may experience comparatively less fluctuation of value compared to CERBT Strategy 1 but more fluctuation of value compared to CERBT Strategy 3. Employers that seek a moderate approach to investing may wish to consider this portfolio.

Information Provided in Lieu of Prospectus

The CERBT Strategy 2 portfolio consists of assets managed internally by CalPERS. Because it is not a mutual fund, a prospectus is not available. This summary is designed to provide descriptive information.

Assets Under Management

As of November 30, 2013, the aggregate total of assets under management for all CERBT Strategies was **$3,142,842,782.**

Composition

Asset Class Allocations and Benchmarks

The CERBT Strategy 2 portfolio may consist of the following asset class target allocations and corresponding benchmarks:

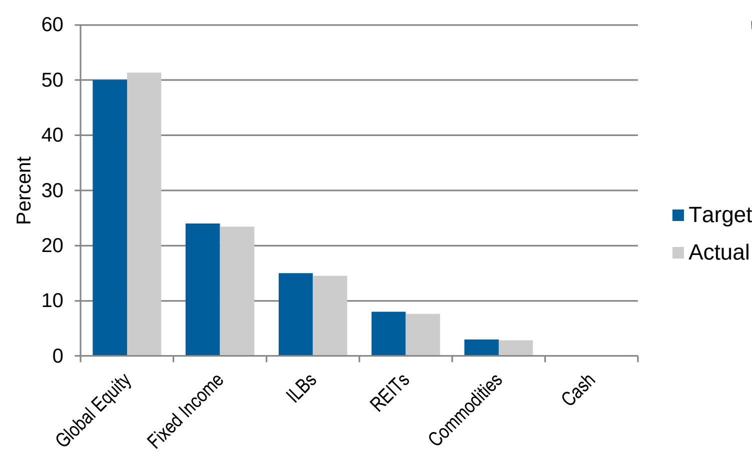
Asset Class	Benchmark
Global Equity	MSCI All Country World Index IMI (net)
U.S. Fixed Income	Barclays Capital Long Liability Index
Treasury Inflation-Protected Securities (TIPS)	Barclays Capital Global: US TIPS Index
Real Estate Investment Trusts (REITs)	FTSE EPRA/NAREIT Developed Liquid Index (net)
Commodities	S&P GSCI Total Return Index

Portfolio Benchmark

The CERBT Strategy 2 benchmark is a composite of underlying asset class market indexes, each assigned the target weight for the asset class it represents.

Target vs. Actual Asset Class Allocations

The following chart shows policy target allocations compared with actual asset allocations as of November 30, 2013. CalPERS may overweight or underweight an allocation to a particular asset class based on market, economic, or CalPERS policy considerations.



CERBT Strategy 2 Performance as of November 30, 2013							
	1 Month	3 Months	Fiscal YTD	1 Year	3 Years*	5 Years*	Since Inception* (October 1, 2011)
Returns before expenses[1]	0.04%	6.22%	7.29%	9.66%	- -	- -	12.63%
CERBT Strategy 2 Benchmark	-0.03%	6.08%	7.15%	9.27%	- -	- -	12.52%

*Returns for periods greater than one year are annualized.
[1]See the Expenses section of this document.
Performance data shown represents past investment performance and is no guarantee of future results. The investment return and principal value of the portfolio will fluctuate so that an employers' account balance in the portfolio may be worth more or less than the amount invested. Current performance may be lower or higher than the performance data shown above.

CERBT Strategy 2

California Employers' Retiree Benefit Trust (CERBT) | November 30, 2013

CalPERS

General Information

What Employers Own

Each employer owns a percentage of the CERBT Strategy 2 portfolio, which invests in pooled asset classes managed by CalPERS. Employers do not have direct ownership of the securities in the portfolio.

Information Accessibility

Since the portfolio is not a mutual fund, information is not available from a newspaper source. Instead, CalPERS provides a quarterly statement of the employer's account. For current performance information, including performance to the most recent month-end, investment policy, and detailed asset allocation, please visit our website at: **www.calpers.ca.gov**.

Price

The value of the portfolio changes daily, based upon the market value of the underlying securities. Just as prices of individual securities fluctuate, the portfolio's value changes with market conditions.

Expenses

CERBT is a self-funded trust in which participating employers pay for all administrative and investment expenses. Expenses reduce the gross investment return by the fee amount. The larger the fee, the greater the reduction of investment return. Currently, CERBT expenses are accrued at an annual rate of 0.15% and charged daily to employer accounts. CERBT's actual expenses may differ from the amount currently being accrued due to factors such as changes in average fund assets or actual expenses. The expense accrual rate may change without notice in order to reflect changes in average fund assets or in expense amount. The CalPERS Board annually reviews the operating expenses and changes may be made as appropriate. Even if the portfolio loses money during a period, the fee is still charged.

Portfolio Manager Information

The portfolio is managed by CalPERS Investment Office staff as directed by the CalPERS Investment Committee and Board of Administration.

Principal Risks of the Portfolio

An investment in the portfolio is not a bank deposit, and it is not insured nor guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. It is possible to lose money by investing in this portfolio. The portfolio's risk depends in part on the portfolio's asset class allocations and the selection, weighting and risks of the underlying investments. Some major risks associated with investing in equities, fixed income and other assets include:

- **Allocation Risk:** The portfolio's ability to achieve its investment objectives depends in part on the managers' skill in determining the portfolios' sector allocations and in selecting and weighting the underlying investments. The managers' evaluations and assumptions regarding asset classes and underlying investments may differ from actual market conditions.

- **Market Risk:** The value of the portfolio will go up and down based on the performance of the underlying investments in which it invests. The value of the underlying investments will, in turn, fluctuate based on the performance of the securities owned and other factors generally affecting the securities market.

- **Interest Rate Risk**: Generally, when interest rates rise, the value of an underlying investment's fixed income securities will decline. The opposite is true when interest rates decline.

- **Credit Risk**: The value of an underlying investment's fixed income securities will be adversely affected by any erosion in the ability of issuers of these securities to make timely interest and principal payments.

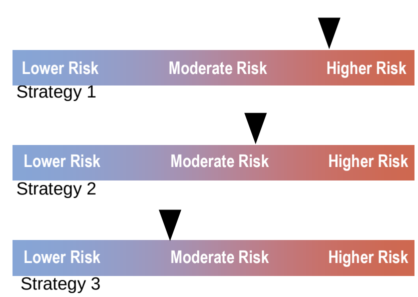
- **Foreign Risk:** Some of the underlying investments are in foreign securities, which are generally riskier than U.S. securities. As a result, the portfolio is subject to foreign risk, meaning that political events (such as civil unrest, national elections, and imposition of exchange controls), social and economic events (such as labor strikes and rising inflation), and natural disasters occurring in a country where the portfolio invests could cause the portfolio's investments in that country to experience losses.

- **Principal Loss:** Employers own a percentage of the CERBT Strategy 2 portfolio (expressed as "units"). At any given time, the value of an employer's units may be worth less than the price paid for them.

CERBT Strategy Risk Levels

CalPERS offers employers the choice of one of three investment strategies. Risk levels among strategies vary, depending upon the target asset class allocations. Generally, equities carry more risk than fixed income securities.

Asset Class Target Allocations	Strategy 1	Strategy 2	Strategy 3
Global Equity	66%	50%	32%
U.S Fixed Income	18%	24%	42%
TIPS	5%	15%	15%
REITs	8%	8%	8%
Commodities	3%	3%	3%



CERBT Strategy 3

California Employers' Retiree Benefit Trust (CERBT) November 30, 2013

CalPERS

Objective

The objective of the CERBT Strategy 3 portfolio is to seek favorable returns that reflect the broad investment performance of the financial markets through capital appreciation and through investment income. There is no guarantee that the portfolio will achieve its investment objectives.

Strategy

The CERBT Strategy 3 portfolio is invested in various asset classes in percentages approved by the CalPERS Board. The specific percentages of portfolio assets allocated to each asset class are shown under "Composition". Generally, equities are intended to help build the value of the employer's portfolio over the long term while bonds are intended to help provide income and stability of principal. Also, strategies invested in a higher percentage of equities seek higher investment returns (but assume more risk) compared with strategies invested in a higher percentage of bonds.

Compared with other asset allocation strategies, this portfolio consists of a lower percentage of equities to bonds and other assets. Historically, funds with a lower percentage of equities have displayed less price volatility and therefore this portfolio may experience less fluctuation of value. Employers that seek greater stability of value, in exchange for possible lower investment returns, may wish to consider this portfolio.

Information Provided in Lieu of Prospectus

The CERBT Strategy 3 portfolio consists of assets managed internally by CalPERS. Because it is not a mutual fund, a prospectus is not available. This summary is designed to provide descriptive information.

Assets Under Management

As of November 30, 2013, the aggregate total of assets under management for all CERBT Strategies was **$3,142,842,782.**

Composition

Asset Class Allocations and Benchmarks

The CERBT Strategy 3 portfolio may consist of the following asset class target allocations and corresponding benchmarks:

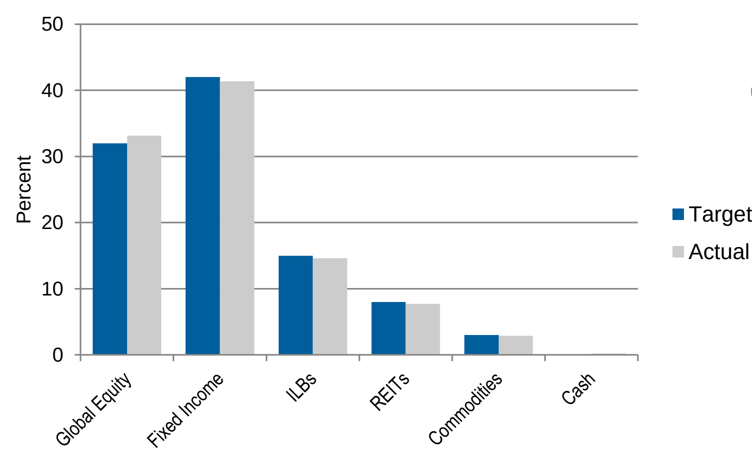
Asset Class	Benchmark
Global Equity	MSCI All Country World Index IMI (net)
U.S. Fixed Income	Barclays Capital Long Liability Index
Treasury Inflation-Protected Securities (TIPS)	Barclays Capital Global: US TIPS Index
Real Estate Investment Trusts (REITs)	FTSE EPRA/NAREIT Developed Liquid Index (net)
Commodities	S&P GSCI Total Return Index

Portfolio Benchmark

The CERBT Strategy 3 benchmark is a composite of underlying asset class market indexes, each assigned the target weight for the asset class it represents.

Target vs. Actual Asset Class Allocations

The following chart shows policy target allocations compared with actual asset allocations as of November 30, 2013. CalPERS may overweight or underweight an allocation to a particular asset class based on market, economic, or CalPERS policy considerations.



CERBT Strategy 3 Performance as of November 30, 2013							
	1 Month	3 Months	Fiscal YTD	1 Year	3 Years*	5 Years*	Since Inception* (January 1, 2012)
Returns before expenses[1]	-0.39%	4.51%	4.87%	4.39%	- -	- -	7.97%
CERBT Strategy 3 Benchmark	-0.49%	4.34%	4.69%	4.02%	- -	- -	7.79%

*Returns for periods greater than one year are annualized.

[1]See the Expenses section of this document.

Performance data shown represents past investment performance and is no guarantee of future results. The investment return and principal value of the portfolio will fluctuate so that an employers' account balance in the portfolio may be worth more or less than the amount invested. Current performance may be lower or higher than the performance data shown above.

CERBT Strategy 3

California Employers' Retiree Benefit Trust (CERBT) | November 30, 2013

CalPERS

General Information

What Employers Own

Each employer owns a percentage of the CERBT Strategy 3 portfolio, which invests in pooled asset classes managed by CalPERS. Employers do not have direct ownership of the securities in the portfolio.

Information Accessibility

Since the portfolio is not a mutual fund, information is not available from a newspaper source. Instead, CalPERS provides a quarterly statement of the employer's account. For current performance information, including performance to the most recent month-end, investment policy, and detailed asset allocation, please visit our website at: **www.calpers.ca.gov**.

Price

The value of the portfolio changes daily, based upon the market value of the underlying securities. Just as prices of individual securities fluctuate, the portfolio's value changes with market conditions.

Expenses

CERBT is a self-funded trust in which participating employers pay for all administrative and investment expenses. Expenses reduce the gross investment return by the fee amount. The larger the fee, the greater the reduction of investment return. Currently, CERBT expenses are accrued at an annual rate of 0.15% and charged daily to employer accounts. CERBT's actual expenses may differ from the amount currently being accrued due to factors such as changes in average fund assets or actual expenses. The expense accrual rate may change without notice in order to reflect changes in average fund assets or in expense amount. The CalPERS Board annually reviews the operating expenses and changes may be made as appropriate. Even if the portfolio loses money during a period, the fee is still charged.

Portfolio Manager Information

The portfolio is managed by CalPERS Investment Office staff as directed by the CalPERS Investment Committee and Board of Administration.

Principal Risks of the Portfolio

An investment in the portfolio is not a bank deposit, and it is not insured nor guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. It is possible to lose money by investing in this portfolio. The portfolio's risk depends in part on the portfolio's asset class allocations and the selection, weighting and risks of the underlying investments. Some major risks associated with investing in equities, fixed income and other assets include:

- **Allocation Risk:** The portfolio's ability to achieve its investment objectives depends in part on the managers' skill in determining the portfolios' sector allocations and in selecting and weighting the underlying investments. The managers' evaluations and assumptions regarding asset classes and underlying investments may differ from actual market conditions.

- **Market Risk:** The value of the portfolio will go up and down based on the performance of the underlying investments in which it invests. The value of the underlying investments will, in turn, fluctuate based on the performance of the securities owned and other factors generally affecting the securities market.

- **Interest Rate Risk**: Generally, when interest rates rise, the value of an underlying investment's fixed income securities will decline. The opposite is true when interest rates decline.

- **Credit Risk**: The value of an underlying investment's fixed income securities will be adversely affected by any erosion in the ability of issuers of these securities to make timely interest and principal payments.

- **Foreign Risk:** Some of the underlying investments are in foreign securities, which are generally riskier than U.S. securities. As a result, the portfolio is subject to foreign risk, meaning that political events (such as civil unrest, national elections, and imposition of exchange controls), social and economic events (such as labor strikes and rising inflation), and natural disasters occurring in a country where the portfolio invests could cause the portfolio's investments in that country to experience losses.

- **Principal Loss:** Employers own a percentage of the CERBT Strategy 3 portfolio (expressed as "units"). At any given time, the value of an employer's units may be worth less than the price paid for them.

CERBT Strategy Risk Levels

CalPERS offers employers the choice of one of three investment strategies. Risk levels among strategies vary, depending upon the target asset class allocations. Generally, equities carry more risk than fixed income securities.

Asset Class Target Allocation	Strategy 1	Strategy 2	Strategy 3
Global Equity	66%	50%	32%
U.S Fixed Income	18%	24%	42%
TIPS	5%	15%	15%
REITs	8%	8%	8%
Commodities	3%	3%	3%