

**Testimony of Marc Carrel, Chair  
Jewish Public Affairs Committee of California  
before the  
California Legislative Joint Oversight Hearing of the  
Assembly Public Employees, Retirement and Social Security Committee and the  
Senate Public Employment and Retirement Committee  
on  
“The Implementation of the California Public Divest from Iran Act (AB 221 (Anderson))”  
Sacramento, CA  
February 24, 2010**

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Messrs. Chairmen and Members of the Committees:

**Introduction**

My name is Marc Carrel, and I am the Chair of the Jewish Public Affairs Committee of California. JPAC is the largest single-state coalition of Jewish organizations in the nation representing Jewish communities and nonprofit organizations across California. I should note that several of our board members are members of either CalPERS or CalSTRS, myself included. I was formerly a state employee and am a vested member of CalPERS.

I am pleased to be here to discuss the implementation status of Assembly Bill 221 that JPAC supported in 2007 and has continued to watch since then.

After several meetings with top executives from both CalPERS and CalSTRS, we have been both frustrated by the inaction, and dismayed by the persistent excuses offered for why the largest state employees pension fund in the nation and the largest teachers pension fund in the nation, feel it is acceptable to ignore a law that did not just pass both houses overwhelmingly – it passed without a single “No” vote.

## Overview of AB 221

AB 221 effectively sets forth three requirements of the funds.

- First is **Identification**. By June 30, 2008 each fund was required to determine which companies were subject to divestment because the companies had business operations in Iran's energy sector. Each fund issued a report listing the firms – and while the list has changed slightly over time – there are about 23 CalSTRS investments and 24 CalPERS holdings that this law would apply to.
- The second phase is **Notification**: Within 90 days after identification, the funds are required to request the identified companies take “substantial action” to remove themselves from doing business in Iran's energy sector, and the funds are supposed to continue to review the activities of those companies every 90 days thereafter. Any identified company that fails to complete substantial action within one year shall be subject to subdivision (h), which contains the final step...
- **Liquidation**. If no “substantial action” is taken by the companies within a year of notification, then the Fund is required to divest their holdings in those companies within 18 months. Note that this is the law's deadline to completely divest.

## Analysis

So AB 221 lays out this detailed timeline and action plan. The Funds are required to determine if companies have taken substantial action or made sufficient progress toward substantial action within one year after the initial notification – which would be no later than September 28, 2009. Companies failing to complete substantial action within one year are subject to subdivision (h).

That subsection requires the Funds to completely divest from those companies within 18 months of the initial notification – in other words, no later than March 28, 2010 for companies originally identified last year.

Both CalPERS and CalSTRS have ignored this requirement. They have not reported whether companies have taken substantial action or progress. And they have not provided any information on actions taken by companies along this timeline and whether they plan to divest from any identified company.

In the August 25<sup>th</sup> letter CalPERS wrote to Chairman Hernandez, on page 2, paragraphs 3 and 4, the letter seems to say that based on legal advice from fiduciary counsel and the financial impact of liquidating those investments that due to its fiduciary duty CalPERS will not divest.

Based on conversations JPAC representatives have had with CalPERS officials, their position seems to be that:

- AB 221 allows consideration of fiduciary duty,
- fiduciary duty does not allow them to incur costs,
- divestment always involves costs, and therefore
- no divestment.

So they are using their own interpretation of fiduciary duty – one that disallows any divestment whatsoever – even though costs are incurred every day by CalPERS and CalSTRS in the regular course of maintaining their portfolio.

### **Fiduciary Duty**

Under Article XVI, Section 17 of the California Constitution

“The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.”

In other words incurring reasonable costs to administer a fund is expected in the regular course of business.

Putting aside the issue of whether the costs incurred to sell these investments is a violation of fiduciary duty, one has to ask whether **holding** these investments is a violation of fiduciary duty.

On April 21, 2008, the CalPERS Board adopted their most recent Statement of Investment Policy for Global Proxy Voting where they explained fiduciary duty:

“The CalPERS Board of Administration functions as fiduciaries. As fiduciaries, they must discharge their responsibilities in accordance with the twin duties of loyalty and care. The duty of loyalty requires the Board and other CalPERS fiduciaries to act solely in the interest of members and beneficiaries. Under the duty of care, the Board and other CalPERS fiduciaries must manage Fund assets as a "prudent investor."...More explicitly, CalPERS fiduciaries must seek to maximize investment returns, while minimizing risk of loss.”

(Note that while “minimizing risk of loss” is mentioned, incurring administrative costs is not.)

So under this definition, CalPERS and CalSTRS are arguably **violating** their fiduciary duty since the companies identified as doing business in Iran’s energy sector are at risk of losing significant value if increased sanctions are imposed by Congress and the Obama Administration. And this is not an idle concern as both Houses of Congress have passed separate sanctions bills which are now being reconciled in conference committee.

### **Investing in Iran Now**

Iran’s economy is in a vulnerable state. International isolation, inadequate foreign investment, declining oil production, rising domestic energy consumption, high inflation, and political unease all have contributed to Iran’s economic condition. In 2001, the SEC determined that companies with business operations in terrorist-sponsoring states (such as Iran) are exposed to a special category of risk known as Global Security Risk, a combination of risk to both share value and corporate reputation that stems from a publicly traded company’s international activities and the security-related concerns generated by connections to terrorism and weapons proliferation.

Under U.S. law, pursuant to the Iran Sanctions Act of 1996, all U.S. and foreign companies that have invested more than \$20 million in Iran’s energy sector since August 5, 1996, are liable to be sanctioned. The number of sanctionable companies is less than twenty, and all are foreign. Many of these companies are the same ones identified as investments by California’s pension funds.

Roger Robinson, CEO of RWR Advisory Group, a Washington DC-based research and consulting firm that specializes in the assessment and management of global security risk stated, “Investments in companies with certain ties to Iran encounter special reputational risks that can have an impact on share value, often in a matter that is asymmetric to the actual business activity in that country.”

Other companies – not in the energy sector, mind you, like Siemens and Lloyds of London, are pulling out of Iran due to economic pressure. But many of the companies identified by CalPERS and CalSTRS are not changing course, and continue to do business with Iran.

So as the U.S. gears up for increased “crippling” sanctions on Iran, and other companies are seeing the risk posed by doing business with Iran, and experts discuss the risk of declining valuation, CalPERS and CalSTRS continue to maintain those holdings. How is this financially prudent? And really, what is the cost of supporting terrorism?

Thirteen other US states have laws similar to AB 221.

Florida, the first state to pass Iran divestment legislation in June 2007 (just months before AB 221 passed), has pulled \$1.15 billion worth of pension money out of 24 foreign companies doing business in the energy sector in Iran and Sudan. And Georgia and Illinois have divested a combined \$200 million.

Why have California’s Funds not followed suit?

## **Conclusion**

It goes without saying that CalPERS and CalSTRS' fiduciary responsibility is critical to California public employees and teachers. But have CalPERS or CalSTRS calculated the cost of transferring investments that fall within the scope of AB 221 to other funds?

Under the "Protect Florida's Investment Act", the Florida State Board of Administration (SBA) divested from companies doing business in Iran's energy sector at an estimated 0.06% cost. Wouldn't CalPERS and CalSTRS, with their expertise, be able to achieve similar results?

CalPERS and CalSTRS opposed the bill when it was under consideration, and they have been dragging their feet ever since to remove one single cent from companies doing business with the country that the U.S. State Department, in their 2008 "Country Reports on Terrorism" called the world's "most significant state sponsor of terrorism." Maintaining investments in companies investing there is clearly not the most prudent place to invest California public employees' pension funds?

In the CalPERS report on their investment this year, on page 4, let me read to you from the report's conclusion: "CalPERS will continue to identify, monitor, [and] engage with companies in the portfolio and review their status under the Iran Act." But we don't need them, or CalSTRS, to keep monitoring. We need them to act; to divest their identified holdings.

Let me end by expressing my view that this is not really about fiduciary duty, it is about CalPERS and CalSTRS not wanting the state Legislature and Governor to tell it how to determine its investments.

Unfortunately, they don't get to make that choice. The law has been enacted, and they need to comply. CalPERS and CalSTRS need to remove their investments from companies doing business in Iran so that their investors – the public; working men and women of California – do not suffer as a result, or unknowingly assist a reprehensible regime.

Thank you.