



California State Teachers'
Retirement System
7667 Folsom Boulevard
Post Office Box 15275
Sacramento, CA 95851-0275

916.229.3706 Tel
www.calstrs.com

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March 6, 2007

The Honorable Barney Frank
Chairman, House Financial Services Committee
2129 Rayburn H.O.B
Washington, D.C. 20515-6050

Dear Chairman Frank:

This letter is sent on behalf of the members of the California State Teachers' Retirement System (CalSTRS). As you are aware, CalSTRS is the second largest public pension system in the United States, with over \$158 billion in assets that are managed on behalf of over 794,812 members and beneficiaries. CalSTRS paid \$6.3 billion in benefits to CalSTRS members and their families in 2006. Our domestic equity portfolio currently comprises \$68 billion in investments; CalSTRS invests in over 2,800 stocks domestically. CalSTRS assets are professionally managed and invested on a long-term basis using sound investment policies that have produced strong investment returns averaging 11.74 percent annually since 1985.

Clearly, the fortunes of CalSTRS are inextricably linked with the domestic market. CalSTRS has been actively involved with the operation and oversight of the domestic market for well over twenty-five years, at both the federal and state level. We have taken the time to communicate and personally meet with the responsible regulatory, oversight and legislative bodies, including the SEC, in order to protect the assets that our beneficiaries and participants will have to depend upon in retirement, disability or death. We are long-term investors by necessity. We have been providing benefits to California's public school teachers since 1913. Because of the long-term nature of our liabilities, the majority of our assets are dependent upon the domestic market.

In December 2006, Fred Buenrostro of CalPERS and I met with you and discussed some of our concerns related to executive compensation and proxy access. CalSTRS has long believed that the pay-for-performance link that investors need is missing from the limited review of compensation plans that shareholders are allowed. We have always supported the idea that shareholders should have a meaningful voice in the way the boards of directors establish and approve executive pay. We applaud the SEC's efforts regarding increased transparency but we are aware that disclosure alone does not consider the whole problem associated with executive pay. We believe that advisory votes by shareholders on executive compensation, such as those that have been required in the UK since 2003, and

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in Australia since 2005, and now introduced by you in the bill, H.R. 1257, on March 1, 2007, go a long way to giving shareholders a meaningful voice on this matter.

Your legislation takes a responsible, balanced approach. As written, the bill does not set pay or even any limits on pay, but allows necessary feedback from shareholders to the boards of directors of companies on the pay plans that they have offered to management. We are also in full support of the provision in the bill that allows for a separate advisory vote on change-in-control payments that become exercisable when negotiations begin involving the sale or purchase of a company. As you know, these so-called change-in-control payments often happen when executives negotiate employment deals that involve no true change in control or even work responsibilities. CalSTRS employs a calculation based on the percentage of the deal that shareholders will have to pay to effect these transactions and regards anything in excess of five percent as excessive. However, we are not currently able to vote on these agreements separately and must now consider this factor along with the investment merits of any deal presented.

Shareholders were amenable to these payments when they were begun twenty years ago because we did not want management interest in opposing deals to negate investment transactions that made sense for shareholders. However, the bounties that are routinely paid today, even in friendly, negotiated transactions, represent a disavowal of the fairness and alignment of interest doctrines that motivated shareholders in the past. Our domestic portfolio is benchmarked against a customized version of the Russell 3000, however, even with this optimization, CalSTRS holds on average 2,800 stocks in its domestic portfolio. Because pension plans and other institutional investors such as CalSTRS are invested so broadly across the domestic equities market, we often are shareholders in both parties to the transaction. Accordingly, these fees are particularly pernicious because they transfer value from the shareholders' pockets without contributing any added value to the surviving corporate entity.

Advisory votes on matters like these would give shareholders and the boards of directors valuable input on these payouts: Often well-in-advance of the triggering event. At the moment, shareholders have to use a very big blunt instrument in order to register displeasure regarding executive pay; they can vote against members of the Compensation Committee. The advisory vote allows all parties an opportunity to address the concerns in the packages and head off the necessity for the hammer on the nail approach of voting against Compensation Committee directors. Despite having had the practice around since 2002, there have been very few negative votes in the UK advisory compensation plans. The most notable is still the GlaxoSmithKline vote, and that vote happened in 2003. The advisory vote allows boards to address shareholder concerns without forcing them to engage in micromanagement or present disruption to the board by allowing members to be voted off over items that, if properly handled, would result in an adjustment as opposed to a coup. This solution is better for all the parties in the corporate pyramid; shareholders are

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well aware that distraction has a cost to the health of their investments. The more of these matters that are handled in a predictable governance setting, the less likely that untoward market impact will be visited on the stocks. The presence of legislation like this removes the need for shareholders to begin a foot-soldier campaign, submitting resolutions to one company at a time, experiencing delays on the issue because of possible director fears of being a first mover or any kind of outlier against their peer board members. H. R. 1257 puts all of the companies, their boards of directors and their shareholders, on the same plate, with the same equipment, and with the same information.

We believe that this feedback to the boards of directors would strengthen the accountability that shareholders require on this issue. The boards of directors would have a partner in its efforts to review executive compensation and the presence of a vote on a discrete issue leaves little room for confusion or argument on its meaning. We wanted to register our support for your actions and offer to help either by providing written testimony or by appearing before or meeting with the members of your Committee if you believe that such efforts would be helpful. Please feel free to contact me to discuss this letter or any other matter that you believe would benefit the public school teachers of California.

Sincerely,

A handwritten signature in black ink that reads "Jack Ehnes". The signature is written in a cursive, flowing style.

Jack Ehnes
Chief Executive Officer