



July 19, 2017

Marcie Frost, Chief Executive Officer
Henry Jones, Chair, Investment Committee
California Public Employees' Retirement System
400 Q Street
Sacramento, CA 95811

Xavier Becerra, Attorney General
Office of the Attorney General
1300 I Street
Sacramento, CA 95814

Betty Yee, Controller
California State Controller
Executive Office
300 Capitol Mall, Suite 1850
Sacramento, CA 95814

John Chiang, Treasurer
California State Treasurer
915 Capitol Mall C-15
Sacramento, CA 95814

Re: Request to Evaluate Divestment of CalPERS Investment that Pays President Trump's Business in Likely Violation of the U.S. Constitution

Dear Ms. Frost, Mr. Jones, Attorney General Becerra, Controller Yee, and Treasurer Chiang:

We ask that you evaluate whether the California Public Employees' Retirement System's ongoing payment of management and performance fees to the CIM Fund III, which in turn directly pays President Trump's hotel management company, violates CalPERS's fiduciary duties to its beneficiaries and the Domestic Emoluments Clause of the U.S. Constitution; and if appropriate, to divest.

I. CalPERS's payments to President Trump's company.

As recently reported in Reuters,¹ CalPERS is a significant investor in the CIM Fund III real estate fund. About half of the total \$2.37 billion investment in CIM Fund III comes from public pension funds, and CalPERS is by far the largest public pension fund invested in the fund, with an initial commitment estimated at approximately \$700 million—well over twice as much as the next largest funds.²

In 2015, CIM Fund III acquired the Trump SoHo hotel in New York, NY. While CIM Fund III has apparently not made a capital call from investors since 2014, CalPERS is reportedly required to pay management and performance fees to CIM Fund III, with the most recent quarterly payments due on or about January 31, 2017 and on or about April 10, 2017. According to a public records request response, CalPERS has paid \$1.7 million in fees to the General Partner of CIM Fund III between January 1, 2017 and March 31, 2017.³ Over the past several years, CalPERS has paid \$6 to \$9 million per year in management and performance fees to CIM Fund III—about half of the total fees paid by all public pension funds. CIM Fund III in turn reportedly has a contract with President Trump's hotel management company, Trump International Hotels Management LLC (part of a larger network known as the Trump Organization), to manage the hotel. Under this agreement, CIM Fund III pays President Trump's company 5.75% of gross hotel operating revenue. Furthermore, CIM Fund III pays operating and overhead charges on the unsold hotel suite units (about two-thirds of the total units). In 2015, CIM Fund III paid \$3.16 million directly to President Trump's company under this contract. The fees being paid to the Trump Organization by CIM Fund III are derived, at least in part, from the

¹ Julia Harte, *Exclusive: A New York hotel deal shows how some public pension funds help to enrich Trump*, Reuters, Apr. 26, 2017, <http://reut.rs/2pyu2QG>.

² The next largest public pension fund investors in CIM Fund III are the New York State Common Retirement Fund and the Teacher Retirement System of Texas, each of which initially committed \$225 million. The other nine public pension funds that are invested in CIM Fund III made initial commitments ranging from \$15 to \$75 million.

³ On June 26, 2017, Free Speech for People filed a request under the California Public Records Law to obtain information about whether such payments have been made. This request has been designated Public Records Request #3239. CalPERS has not provided responses to the full record request, but did provide the total amount paid from January 1 to March 31, 2017.

performance and management fees that CalPERS is required to pay to CIM Fund III.

II. CalPERS’s ongoing payments to CIM Fund III which subsidize a company owned by President Trump may violate the U.S. Constitution.

While not all relevant facts are publicly available, based on initial reporting, it appears that CalPERS’s ongoing payments to CIM Fund III, which CIM Fund III in turn relays in part to President Trump’s company, may violate CalPERS’s duties and the U.S. Constitution.

The arrangements between CalPERS and CIM Fund III, and between CIM Fund III and Mr. Trump’s company, may have been entirely lawful and appropriate before January 20, 2017. But the situation has changed since the inauguration of Mr. Trump as president. The U.S. Constitution’s Domestic Emoluments Clause provides: “The President shall, at stated Times, receive for his Services, a Compensation, which shall neither be encreased nor diminished during the Period for which he shall have been elected, and he shall not receive within that Period *any other Emolument from the United States, or any of them.*”⁴ This provision, which is not waivable by Congress, prohibits any state from providing additional sources of income to the President.

At the Founding, the term “emolument,” from the Latin *emolumentum* (profit), was understood broadly. For example, Samuel Johnson’s influential 1755 dictionary defined “emolument” as “Profit; advantage.”⁵ Unfortunately, CalPERS’s ongoing payments to CIM Fund III are giving President Trump a “profit” from the state of California—more specifically, from its state workers.

We recognize that CalPERS made its initial capital investment in CIM Fund III well before President Trump was elected, and that this investment was lawful at the time. And payments made by CalPERS to CIM Fund III *before* President Trump’s inauguration certainly do not raise any constitutional questions. However, ongoing regular payments of millions of dollars to a real estate fund that transfers a significant portion of those fees directly to

⁴ U.S. Const., art. II, § 1, cl. 7 (emphasis added) (also known as the Presidential Compensation Clause).

⁵ Samuel Johnson, *A Dictionary of the English Language* 690 (1755). This broad meaning” is also supported by the sixteen occurrences of the word in William Blackstone’s Commentaries on the Laws of England, <https://balkin.blogspot.com/2017/05/emolument-in-blackstonescommentaries.html>.

President Trump's company may constitute an unconstitutional emolument from California. And as the supreme law of the land, the U.S. Constitution is part and parcel of the law of California.⁶

These facts appear distinct from a previous Domestic Emoluments Clause question regarding California pension fund payments: President Reagan's state pension from his service as governor. In 1981, the U.S. Department of Justice's Office of Legal Counsel opined that President Reagan's receipt of his California pension did not violate the Domestic Emoluments Clause.⁷ There, President Reagan's California retirement benefits were *not* found to constitute compensation. Furthermore, President Reagan was being treated no differently than any similarly situated private citizen who had worked for the state of California. Here, it appears that President Trump's company is being actively compensated, with fees generated from CalPERS, for managing a hotel.

President Trump has had more than enough opportunity to remedy the problems presented by his ownership interests in the Trump Organization, but he opted against taking that opportunity. On November 30, 2016, the U.S. Office of Government Ethics announced that the “[o]nly way to resolve these conflicts of interest is to divest.”⁸ The nearly ten-week transition period between the presidential election and the presidential inauguration gave Mr. Trump sufficient opportunity to resolve these issues in numerous ways.⁹ For example, he could have liquidated the business and invested the proceeds in a diversified mutual fund or a true blind trust.¹⁰

⁶ See U.S. Const. art. VI, cl. 2 (“This Constitution . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.”); Cal. Const. art. XX, § 3 (state officials’ oath to “support and defend the Constitution of the United States”).

⁷ See Larry L. Simms, Office of Legal Counsel, U.S. Dep’t of Justice, *President Reagan’s Ability to Receive Retirement Benefits from the State of California* (June 23, 1981), <https://www.justice.gov/file/22681/download>.

⁸ Michael D. Shear & Eric Lipton, *Ethics Office Praises Donald Trump for a Move He Hasn’t Committed To*, N.Y. Times, Nov. 30, 2016, <http://nyti.ms/2gK988R>.

⁹ See Richard Painter & Norman Eisen, *Donald Trump will still be violating the Constitution as soon as he’s sworn in*, Wash. Post, Dec. 13, 2016, <http://wpo.st/9EZN2>.

¹⁰ See Norman Eisen, Richard W. Painter & Laurence H. Tribe, *5 Ways You’ll Know if Trump Is Playing by the Rules*, Politico, Jan. 10, 2017, <http://politi.co/2iCgLj2>.

But despite every opportunity, neither Mr. Trump nor the Trump Organization has done anything remotely adequate to address these serious concerns. Instead, on January 11, 2017, the Trump Organization’s tax law firm announced a plan to transfer *management* control of the Trump Organization to Mr. Trump’s sons and a senior executive, without removing Mr. Trump’s *ownership* stake.¹¹

In addition, Mr. Trump has apparently transferred his ownership stakes in various Trump business entities to “The Donald J. Trump Revocable Trust.” This trust, of which Mr. Trump’s son and the Trump Organization’s chief financial officer are trustees, has as its purpose “to hold assets for the ‘exclusive benefit’ of the president,” and uses Mr. Trump’s Social Security number as its taxpayer identification number.¹² Furthermore, in February 2017, the trust was amended so that Mr. Trump “shall distribute net income or principal to Donald J. Trump at his request,” or whenever his son and a longtime employee “deem appropriate.”¹³ The terms of this revocable trust mean that Mr. Trump can draw upon funds paid to any of the Trump Organization entities at any time.

This is not a “blind trust.” Mr. Trump knows which businesses his trust owns, and how his actions as President may affect their income and value—including Trump SoHo. The trust is run not by an independent trustee, but by his own son and a longtime executive. And he can revoke the trust at any time.¹⁴ This arrangement does not diminish Mr. Trump’s interest and ability to enrich himself through presidential actions affecting his business entities, and to shape U.S. policy to preserve and promote his business assets, including Trump SoHo.

¹¹ See *Donald Trump’s News Conference: Full Transcript and Video*, N.Y. Times, Jan. 11, 2017, <http://nyti.ms/2kHSolf>.

¹² Susanne Craig & Eric Lipton, *Trust Records Show Trump Is Still Closely Tied to His Empire*, N.Y. Times, Feb. 3, 2017, <https://nyti.ms/2kytJIP..>

¹³ Drew Harwell, *Trump can quietly draw money from trust whenever he wants, new documents show*, Wash. Post, Apr. 3, 2017, <http://wapo.st/2nQOjgK>.

¹⁴ See Craig & Lipton, *supra*, <https://nyti.ms/2kytJIP>.

III. CalPERS's duties to its participants and to the law.

Under California law, all state employees are required to participate in the California Public Employees' Retirement System, with mandatory salary deductions being subtracted from their compensation to fund that system.¹⁵ CalPERS participants do not have the ability to select the funds in which their mandatory salary deductions are invested. Rather, the CalPERS board has "plenary authority and fiduciary responsibility for investment of moneys and administration of the system."¹⁶ Plenary authority, however, does not mean unconstrained authority.¹⁷ For example, CalPERS has a fiduciary duty to provide timely, accurate, and "complete and unambiguous" information to its members.¹⁸ And courts have ruled that, despite the primary duties of CalPERS board members to provide for the interests and benefits of its members and beneficiaries, minimizing employer contributions, and defraying administrative expenses, CalPERS has a duty to follow the law.¹⁹

This is magnified by the fact that the money used for this investment comes from mandatory deductions from the paychecks of public employees. These employees are thus forced to indirectly subsidize President Trump beyond the Constitution's mandate of a fixed salary, and have not been given the opportunity to decide whether they wish their paychecks to contribute to this scheme. Indeed, given serious allegations that the Trump Organization violated federal campaign finance law by making corporate contributions to the 2016 presidential campaign,²⁰ ongoing mandatory employee subsidization of President Trump's company and its corporate political activity may implicate the First Amendment rights of CalPERS participants against compelled political speech.²¹

¹⁵ Cal. Gov't Code § 20281. Many local government employees in California are required to participate as well. *See id.* §§ 20460 *et seq.*

¹⁶ Cal. Const. art. 16, § 17.

¹⁷ *See Westly v. Cal. Pub. Employees' Ret. Sys. Bd. of Admin.*, 105 Cal. App. 4th 1095, 1109 (2003).

¹⁸ *City of Oakland v. Pub. Employees' Ret. Sys.*, 95 Cal. App. 4th 29, 40 (2002).

¹⁹ *City of Pleasanton v. Bd. of Admin. of the Cal. Pub. Employees' Ret. Sys.*, 211 Cal. App. 4th 522, 544 (2012).

²⁰ Jonathan Easley, *GOP lawyer files FEC complaint against Trump*, The Hill, Dec. 9, 2015, <http://bit.ly/1mbSp0R>.

²¹ *See generally Knox v. Serv. Employees Int'l Union*, 567 U.S. 310 (2012); *Aboud v. Detroit Bd. of Educ.*, 431 U.S. 209 (1977); Benjamin I. Sachs, *Unions, Corporations, and Political Opt-Out Rights After Citizens United*, 112 Colum. L. Rev. 800, 866-69 (2012).

IV. CalPERS's next steps.

CalPERS should not participate in this scheme by using public employees' money to pay a fund that pays Mr. Trump.

CalPERS's Total Fund Investment Policy emphasizes that CalPERS "wants companies in which it invests to meet high corporate governance, ethical, and social standards of conduct."²² And CalPERS has long led the way in consideration of environmental, social, and governance issues in investments. In 2000, CalPERS instructed managers of its internally managed funds to divest from tobacco, and on December 19, 2016, CalPERS voted to expand the tobacco investment ban to externally managed portfolios and to its affiliate funds.²³ While the tobacco restrictions reduced financial returns, CalPERS ultimately viewed tobacco divestment "through multiple lenses encompassing a wide range of differing perspectives."²⁴ As State Treasurer (and board member) John Chiang explained, "No public pension fund should associate itself with an industry that is a magnet for costly litigation, reputational disdain, and government regulators around the globe."²⁵ CalPERS also holds its trustees, administrators, and all other fiduciaries to "the highest ethical standards."²⁶

In general, CalPERS policy tends to prefer corporate engagement over divestment.²⁷ For example, CalPERS staff have advised against divesting from the Dakota Access Pipeline on the theory that "[i]nvestors that divest lose their ability as shareowners to influence the company to act responsibly," and that divestment "removes any opportunity for CalPERS to exert influence over a company through direct shareholder engagement – including any ability to effect changes in company behavior to strengthen management

²² See CalPERS, *Total Fund Investment Policy* 17, <https://www.calpers.ca.gov/docs/total-fund-investment-policy.pdf> (Apr. 18, 2016).

²³ See CalPERS, *CalPERS Votes to Expand Tobacco Investment Ban to External Managers and Affiliate Funds*, <https://www.calpers.ca.gov/page/newsroom/calpers-news/2016/votes-expand-tobacco-investment-ban> (Dec. 19, 2016).

²⁴ *Id.*

²⁵ *CalPERS should not take up the tobacco habit again*, Sacramento Bee, Apr. 6, 2016, <http://sacb.ee/5WC6>.

²⁶ CalPERS Beliefs 2, <https://www.calpers.ca.gov/docs/forms-publications/calpers-beliefs.pdf> (May 2015).

²⁷ See *Total Funds Investment Policy*, *supra*, at 17-18.

of environmental and human capital factors.”²⁸ Similarly, CalPERS’s corporate engagement policy for climate change explains that CalPERS “firmly believe[s] that active and direct engagement as a first line approach is the best way to resolve issues.”²⁹

However, engagement with the underlying company is not a simple matter in this case. A state entity such as CalPERS using its business relationship with a company owned by the President as leverage to “engage” is one of the very dangers that the Domestic Emoluments Clause was designed to prohibit. Any management and/or performance fee payments made by CalPERS to CIM Fund III after January 20, 2017 constitute participation in a scheme that enriches the President with public employees’ money.

It is also important to note that CalPERS’s position here is more akin to a principal than a mere passive investor. CalPERS has worked closely with CIM Group on other business projects, most notably the development of a new tower on Capitol Mall in Sacramento,³⁰ and is here more akin to an owner of Trump SoHo than a passive investor in a fund. The flow of money and value from CalPERS through CIM Fund III to Trump International Hotels Management LLC to President Trump cannot continue.

²⁸ CalPERS Investment Comm., *Assembly Bill 20 (Kalra) Dakota Access Pipeline: Divestment* 5, <https://www.calpers.ca.gov/docs/board-agendas/201702/invest/item06b-00.pdf> (Feb. 13, 2017); see also *Total Fund Investment Policy*, *supra*, at 17 (“Investors that divest lose their ability as shareowners to influence the company to act responsibly.”)

²⁹ CalPERS, *The Importance of Corporate Engagement on Climate Change* 4-5, <https://www.calpers.ca.gov/docs/corporate-engagement-climate-change.pdf>.

³⁰ Rob Turner, *Massive new tower proposed for Capitol Mall could end up as city’s tallest*, Sactown Magazine, <http://www.sactownmag.com/Blog/2016/Massive-new-tower-proposed-for-Capitol-Mall-could-end-up-as-citys-tallest/> (Feb. 3, 2016).

We respectfully request that CalPERS work with other pension fund investors in CIM Fund III to demand that CIM Fund III sell the Trump SoHo property and terminate its relationship with the Trump Organization based on the Trump Organization's ongoing participation in a corruption scheme that violates the Constitution; or, alternatively, that CalPERS divest its interest in CIM Fund III.

We are available to discuss this request with you further at your convenience, and we look forward to hearing from you. Thank you for your consideration.

Sincerely,

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