CalPERS’ Governance & Sustainability Principles

Last Revised: ~~September 2019~~ November 2023

CalPERS

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Introduction

Our mission is to "deliver retirement and health care benefits to members and their beneficiaries." The California Public Employees' Retirement System (CalPERS, System) is the nation's largest defined benefit public pension fund with a duty to deliver the retirement and health benefits promised to our members. This responsibility applies not just to our current beneficiaries, but also to future members who may not retire for several decades. We therefore need to ensure that our commitments can be honored over the long-term.

A vital part of this is ensuring that our investments, which fund around two-thirds of our pension payments every year, generate the highest possible returns at an acceptable level of risk. This is a task managed by the CalPERS Investment Office, overseen by the CalPERS Board of Administration, and guided by our Investment Beliefs[1] and Core Values[2]. This responsibility is known as our Fiduciary Duty[3].

Over the years the CalPERS Principles have evolved from a guide to proxy voting in public markets, to a broader statement of our views on best practices guiding our engagement with companies, advocacy agenda with policy makers, and expectations for both our internal and external managers across the total fund.

As the governance and sustainability agenda has developed, so too have the CalPERS Principles. An important area of development has been integrating consideration of environmental and social factors alongside our governance agenda. We have given an economic framework to what is often called ESG in investing. As reflected in our Investment Beliefs, CalPERS considers that long-term value creation requires the effective management of three forms of capital – Financial, Physical, and Human. This economic approach grounds our sustainable investment agenda in our fiduciary duty to generate risk-adjusted returns for our beneficiaries.

A further important area of development has been the recognition that financial markets' safety and soundness are vitally important to CalPERS ability to achieve its risk adjusted returns. This focus on financial markets is also reflected in CalPERS' Investment Beliefs, which recognize that a long-term investment horizon is both an advantage and a responsibility. That responsibility requires that CalPERS advocate for policies that support the long-term with policy makers, companies, and investment managers.

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[1] In September 2013, CalPERS adopted a set of ten Investment Beliefs intended to guide decision-making, facilitate the management of a complex portfolio, and enhance consistency. The Investment Beliefs can be found at www.calpers-governance.org

[2] Quality, Respect, Accountability, Integrity, Openness, and Balance.

[3] CalPERS' Board and its Staff have fiduciary duties of loyalty and prudence, pursuant to the California Constitution, Article XVI, Section 17, to invest "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an enterprise of a like character and with like aims."

The current edition distills some 20 years of experience in governance and sustainability. We continue to develop our approach on new issues which are emerging and to refresh our thinking as we learn from experience.

CalPERS expects all internal and external managers of CalPERS capital to integrate the Principles into investment decision making, including proxy voting, consistent with CalPERS' fiduciary duty to seek the highest possible returns at an acceptable level of risk to fulfill our pension obligations. CalPERS recognizes that countries and companies are in different developmental stages. We are mindful of differing laws and practices in jurisdictions – of governance outcomes and need to be carefully addressed. CalPERS' investment managers will need to exercise their best judgment after taking all relevant factors into account.

We have learned that company managers want to perform well, in both an absolute sense and as compared to their peers. They also want to adopt long-term strategies and vision, but often do not feel that their shareowners are patient enough. Our experience has shown all companies – whether governed under a structure of full accountability or not – will inevitably experience both ascents and descents along the path of profitability.

We have also learned, and firmly embrace the belief that strong, accountable corporate governance means the difference between long periods of failure in the depths of the performance cycle and responding quickly to correct the corporate course.

This work has been integrated into CalPERS Investment Beliefs which address sustainable investment, risk management, and CalPERS engagement with companies, regulators, managers, and stakeholders.

We recognize that much of our experience in this area comes from investments in public equities but that our evolution to a "Total Fund" approach means these Principles may need to be suitably adapted to work across other asset classes. We continue to listen and learn in this area.

We encourage and welcome feedback on these Principles from companies, fellow investors and other stakeholders. You can submit your feedback here: https://www.calpers.ca.gov/page/contact/questions-comments-complaints.

Purpose

These Principles have been adopted by the CalPERS Board, through its Investment Committee, in order to create the framework for considerations that must be taken into account when we participate in any of the following actions:

- Executes our shareowner proxy voting responsibilities
- Engage investee companies to achieve long-term sustainable risk-adjusted returns
- Requests internal and external managers of our capital to make investment decisions on our behalf
- Advocate with policy-makers and international organizations on financial market reform.

Proxy Voting

We implement our proxy voting responsibility in a manner that is consistent with these Principles unless such action may result in long-term harm to the company that outweighs all reasonably likely long-term benefit; or unless such a vote is contrary to the interests of the beneficiaries of the System.

It is therefore important for shareowners such as CalPERS to exercise their rights to participate and make their voting decisions based on a full understanding of the information and legal documentation presented to them. Our proxy voting responsibilities cover a wide range of corporate governance issues centered around various management and shareowner proposals. Specific voting topics may include board quality, investor rights, executive compensation, corporate reporting, capital structure, environmental and social related issues. When exercising our voting rights, we will cast votes “for” or “against”, individual management and shareowner proposals consistent with the interest of our beneficiaries and consistent with the Principles.

We will vote “against”, an individual or slate of director nominees at companies that do not effectively oversee these interests. We will also withhold our vote in limited circumstances where a company has consistently demonstrated long-term economic underperformance.

As part of our commitment to transparency, we publish our proxy voting activities at over 11,000 companies’ annual general meetings.

Shareowner Engagement

We have a long history of constructively engaging companies confidentially through in-person meetings, correspondence, and by telephone. In instances where companies fail to meet the standards of conduct defined by our Principles, we may file shareowner proposals to achieve governance reforms.

We prefer constructive engagement to divesting as a means of affecting the conduct of the entities in which we invest. This is because investors that divest lose their ability as shareowners to positively influence the company’s strategy and governance.

Advocacy

We engage policy makers on regulatory and legislative reforms which support the Principles. We work directly and through our federal representatives and also partner with organizations, both domestically and internationally, to further our goals.

Governance & Sustainability Principles

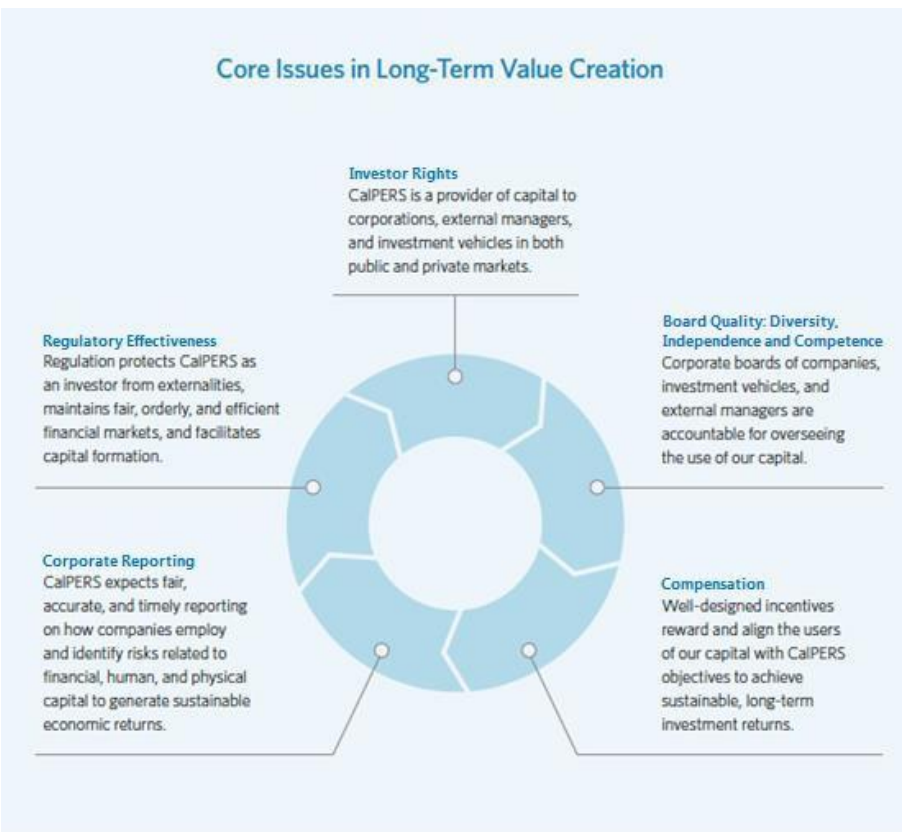
We believe that fully accountable governance structures produce, over the long term, the best returns to shareowners. While we recognize that governance best practices are constantly evolving, we believe the following accountable governance structures provide the underlying tenets that should be adopted by all companies and markets – both developed and emerging – to establish the foundation for achieving long-term sustainable investment returns.

In particular we have identified five core issues that we believe have a long-term impact on risk and return:

A. Investor Rights
B. Board Quality: Diversity, Independence and Competence
C. Executive, Director and Employee Compensation
D. Corporate Reporting
E. Regulatory Effectiveness

As demonstrated in Figure 1 below, it is important to recognize that we believe that managing these five issues is mutually reinforcing. Approaches that only tackle some areas and not others would not be compatible with these Principles.

Figure 1: Core Issues in Long-term Value Creation



A. Investor Rights

CalPERS is a provider of capital to corporations, external managers, and investment vehicles in both public and private markets – investor rights protect CalPERS interests.

We recommend that corporations adopt the following shareowner rights:

1. **One-share/one-vote**: A shareowner's right to vote is irrevocable and cannot be reduced. All investors must be treated equitably and upon the principle of one-share/one-vote.
    a. **Redress**: Minority shareowners should be protected from abusive actions by, or in the interest of, controlling shareowners acting either directly or indirectly, and should have effective means of redress. Proper remedies and procedural rules should be put in place to make the protection effective and affordable. Where national legal remedies are not afforded the board is encouraged to ensure that sufficient shareowner protections are provided in the company's bylaws.

2. **Access to Director Nominations**: Shareowners should have effective access to the director nomination process. Companies should provide access to management proxy materials for a long-term investor or group of long-term investors owning in aggregate at least three percent of a company's voting stock, to nominate up to 25 percent of the board. Eligible investors must have owned the stock for at least three years. Company proxy materials and related mailings should provide equal space and equal treatment of nominations by qualifying investors. To allow for informed voting decisions, it is essential that investors have full and accurate information about access mechanism users and their director nominees. Therefore, shareowners nominating director candidates under an access mechanism should adhere to the same SEC rules governing disclosure requirements and prohibitions on false and misleading statements that currently apply to proxy contests for board seats.

3. **Shareowner Approval Rights**: The board should ensure that shareowners have the right to vote on major decisions which may change the nature of the company in which they have invested. Such rights should be clearly described in the company's governing documents and include:
    a. **Sale or Pledge of Corporate Assets**: Major corporate decisions concerning the sale or pledge of corporate assets that would have a material effect on shareowner value. Such a transaction will automatically be deemed to have a material effect if the value of the assets exceeds 10 percent of the assets of the company and its subsidiaries on a consolidated basis.
    b. **Mergers and Acquisitions**: Material and extraordinary transactions such as material mergers and acquisitions.
    c. **Debt Issuance**: Issuing debt to a degree that would excessively leverage the company and endanger its long-term viability.

d. **Share Repurchases (buy-backs)**: The corporation's acquisition of five percent or more of its common shares at above-market prices other than by tender offer to all shareowners.
e. **Issuance of New Shares**: The board should be mindful of dilution of existing shareowners and provide full explanations where pre-emption rights are not offered.
f. **Poison Pill Approval**: No board should enact nor amend a poison pill (shareowner rights plan) except with shareowner approval or other structures that act as anti-takeover mechanisms. Only non-conflicted shareowners should be entitled to vote on such plans and the vote should be binding. Plans should be time limited and put periodically to shareowners for re-approval.
    i. **Continuing Directors**: Corporations should not adopt so-called "continuing director" provisions (also known as "dead-hand" or "no-hand" provisions, which are most commonly seen in connection with a potential change in control of the company) that allow board actions to be taken only by: (1) those continuing directors who were also in office when a specified event took place or (2) a combination of continuing directors plus new directors who are approved by such continuing directors.
g. **Significant Related Party Transaction**: Shareowners should have the right to approve significant related party transactions and this should be based on the approval of a majority of disinterested shareowners. The board should submit the transaction for shareowner approval and disclose (both before concluding the transaction and in the company's annual report):
    i. the identity of the ultimate beneficiaries including, any controlling owner and any party affiliated with the controlling owner with any direct / indirect ownership interest in the company
    ii. other businesses in which the controlling shareowner has a significant interest
    iii. Shareowner agreements (e.g. commitments to related party payments such as license fees, service agreements and loans).

    The board should disclose the process for reviewing and monitoring related party transactions which, for significant transactions, includes establishing a committee of independent directors. This can be a separate committee, or an existing committee comprised of independent directors, for example the Audit Committee. The committee should review significant related party transactions to determine whether they are in the best interests of the company and, if so, to determine what terms are fair and reasonable. The conclusion of committee deliberations on significant related party transactions should be disclosed in the company's annual report to shareowners.

4. **Majority Vote Requirements**: Shareowner voting rights should not be subject to supermajority voting requirements, except in situations where they are intended to protect minority shareowners; especially in situations where there are unequal voting rights. A majority of proxies cast should be able to accomplish the following:
    a. **Bylaw and Charter Amendments**: Amend the company's governing documents such as the Bylaws and Charter by shareowner resolution.
    b. **Director Removal**: Remove a director with or without cause.
    c. **Director Elections**: In an uncontested director election, a majority of proxies cast should be required to elect a director. In a contested election, a plurality of proxies cast should be required to elect a director. Resignation for any director that receives a withhold vote greater than 50 percent of the votes cast should be required. Unless the incumbent director receiving less than a majority of the votes cast has earlier resigned, the term of the incumbent director should not exceed 90 days after the date on which the voting results are determined.
    d. **Auditor Ratification by Shareowners**: The selection of the independent external auditor should be ratified by shareowners annually.

5. **Corporate Proxy and Voting Mechanisms**: The board should promote efficient and accessible voting mechanisms that allow shareowners to participate in general meetings either in person or remotely, preferably by electronic means or by post, and should not impose unnecessary hurdles.
    a. **Universal Proxy**: To facilitate the shareowner voting process in contested elections – opposing sides engaged in the contest should utilize a proxy card naming all management nominees and all dissident nominees, providing every nominee equal prominence on the proxy card.
    b. **Sponsoring and Implementation of Shareowner Resolutions**: Shareowners should have the right to sponsor resolutions. A shareowner resolution that is approved by a majority of proxies cast should be implemented by the board.
    c. **Proxy Confidentiality**: Proxies should be kept confidential from the company, except at the express request of shareowners.
    d. **Cumulative Voting Rights**: Shareowners should have the right to combine votes in a contested election of directors. Such a right gives shareowners the ability to combine their votes for directors and either cast all of those votes for one candidate or distribute those votes for any number of candidates.
    e. **Shareholder Identification**: The board should ensure that the company maintains a record of the registered owners of its shares or those holding voting rights over its shares. Registered shareowners, or their agents, should provide the company (where anonymity rules do not preclude this) with the identity of beneficial owners or holders of voting rights

when requested in a timely manner. Shareowners should be able to review this record of registered owners of shares or those holding voting rights over shares.

f. **Bundled Voting**: Shareowners should be allowed to vote on unrelated issues separately. Individual voting issues (particularly those amending a company's charter), bylaws or anti-takeover provisions should not be bundled.
g. **Broker Votes**: Uninstructed broker votes and abstentions should be counted only for purposes of a quorum, or the minimum number of members necessary to make a decision.
h. **Advance Notice, Holding Requirements and Other Provisions**: Advance notice bylaws, holding requirements, disclosure rules, and any other company imposed regulations on the ability of shareowners to solicit proxies beyond those required by law should not be so onerous as to deny sufficient time, limit the pool of eligible candidates, or otherwise make it impractical for shareowners to submit nominations or proposals and distribute supporting proxy materials**.**

6. **Special Meetings and Written Consent**: Shareowners should be able to call special meetings or act by written consent.

7. **Judicial Forum**: Companies should not attempt to restrict the venue for shareowner claims by adopting charter or bylaw provisions that seek to establish an exclusive forum. Nor should companies attempt to bar shareowners from the courts through the introduction of forced arbitration clauses.

B. Board Quality: Diversity, Independence and Competence

Corporate boards of companies, investment vehicles and external managers must be accountable for overseeing the use of our capital.

1. **Director Accountability**: As a fiduciary, a director owes a duty of loyalty to the corporation and its shareowners and must exercise reasonable care in relation to his or her duties as a director. Directors should be accountable to shareowners, and management accountable to directors.
    a. **Long-term Vision**: Corporate directors and management should have a long-term strategic vision that, at its core, emphasizes sustained shareowner value and effective management of both risk and opportunities in the oversight of financial, physical, and human capital. In turn, despite differing investment strategies and tactics, shareowners should encourage corporate management to resist short-term behavior by supporting and rewarding long-term superior returns.
    b. **Accessibility to Shareowner Inquiry**: To ensure this accountability, directors must be accessible to shareowner inquiry concerning their key decisions affecting the company's strategic direction.
    c. **Annual Director Elections**: Every director should be elected annually. Accountability mechanisms may require directors to stand for election on an annual basis or to stand for election at least once every three years.
    d. **Board Size**: The board periodically reviews its own size and determines the size that is most effective toward future operations.
    e. **Director Attendance**: Without compelling and stated reasons, directors should be expected to attend at least 75 percent of the board and key committee meetings on which they sit.
    f. **Director Time Commitment**: The board adopts and discloses guidelines in the company's proxy statement to address competing time commitments that are faced when directors, especially acting CEOs, serve on multiple boards.

2. **Informed Directors**: Directors should receive training from independent sources on their fiduciary responsibilities and liabilities. Directors have an affirmative obligation to become and remain independently familiar with company operations; they should not rely exclusively on information provided to them by the CEO to do their jobs. Directors should be provided meaningful information in a timely manner prior to board meetings and should be allowed reasonable access to management to discuss board issues.
    a. **Board Access to Management**: The board should have a process in place by which all directors can have access to senior management.
    b. **New Director Induction**: The board should have in place a formal process of induction for all new directors so that they are well-informed about the company as soon as possible after their

appointment. Directors should also be enabled to regularly refresh their skills and knowledge to discharge their responsibilities.

3. **Board Independence**: Independence is the cornerstone of accountability. It is now widely recognized that independent boards are essential to a sound governance structure. Nearly all corporate governance commentators agree that boards should be comprised of at least a majority of "independent directors." But the definitional independence of a majority of the board may not be enough in some instances. The leadership of the board must embrace independence, and it must ultimately change the way in which directors interact with management. Independence also requires a lack of conflict between the director's personal, financial, or professional interests, and the interests of shareowners.
   a. **Majority of Independent Directors**: At a minimum, a majority of the board consists of directors who are independent. Boards should strive to obtain board composition made up of a substantial majority of independent directors.
   b. **Independent Executive Session**: Independent directors should meet periodically (at least once a year) alone in an executive session, without the CEO. The independent board chair or lead (or presiding) independent director should preside over this meeting.
   c. **Board Role of Retiring CEO**: Generally, a company's retiring CEO should not continue to serve as a director on the board and at the very least be prohibited from sitting on any of the board committees.

4. **Board Committee Independence**: The full board is responsible for the oversight function on behalf of shareowners. Should the board decide to have other committees (e.g. an executive committee) in addition to those required by law, the duties and membership of such committees should be fully disclosed. Committees who perform the audit, director nomination and executive compensation functions should consist entirely of independent directors. The board (not the CEO) should appoint the committee chairs and members. Committees should be able to select their own service providers to access independent sources of knowledge and experience. Some regularly scheduled committee meetings should be held with only the committee members (and, if appropriate, the committee's independent consultants) present. The process by which committee members and chairs are selected should be disclosed to shareowners.

5. **Board Chairperson Independence and Leadership**: The board should be chaired by an independent director. The chair is responsible for leadership of the board and ensuring its effectiveness. The chair should ensure a culture of openness and constructive debate that allows a range of views to be expressed. The CEO and chair roles should only be combined in very limited circumstances; in these situations, the board should provide a written statement in the proxy materials discussing why the

combined role is in the best interest of shareowners, and it should name a lead independent director to fulfill the following duties:

a. Coordinate the scheduling of board meetings and preparation of agenda material for board meetings and executive sessions of the board's independent or non-management directors.
b. Lead board meetings in addition to executive sessions of the board's independent or non-management directors.
c. When selecting a new CEO, boards should re-examine the traditional combination of the "chief executive" and "chair" positions.
d. Define the scope, quality, quantity and timeliness of the flow of information between company management and the board that is necessary for the board to effectively and responsibly perform their duties.
e. Oversee the process of hiring, firing, evaluating, and compensating the CEO.
f. Approve the retention of consultants who report directly to the board.
g. Advise the independent board committee chairs in fulfilling their designated roles and responsibilities to the board.
h. Interview, along with the chair of the nominating committee, all board candidates, and make recommendations to the nominating committee and the board.
i. Assist the board and company officers in assuring compliance with and implementation of the company's Governance Principles.
j. Act as principal liaison between the independent directors and the CEO on sensitive issues.
k. Coordinate performance evaluations of the CEO, the board, and individual directors.
l. Recommend to the full board the membership of the various board committees, as well as selection of the committee chairs.
m. Be available for communication with shareowners.

6. **Director Independence**: The board should ensure that policies and procedures on conflicts of interest are established, understood and implemented by directors, management, employees and other relevant parties. If a director has an interest in a matter under consideration by the board, then the director should promptly declare such an interest and be precluded from voting on the subject or exerting influence. Each company should disclose in its annual proxy statement the definition of "independence" relied upon by its board. The board's definition of "independence" should address, at a minimum, a director who:

a. Is not currently, or within the last five years has not been, employed by the Company in an executive capacity.
b. Has not received more than $50,000 in direct compensation from the Company during any 12-month period in the last three years other than:
  i. Director and committee fees including bona fide expense reimbursements.
  ii. Payments arising solely from investments in the company's securities.

c. Is not affiliated with a company that is an adviser or consultant to the Company or a member of the Company's senior management during any 12-month period in the last three years that has received more than $50,000 from the Company.

d. Is not a current employee of a company (customer or supplier) that has made payments to, or received payments from the Company that exceed the greater of $200,000 or 2 percent of such other company's consolidated gross revenues.

e. Is not affiliated with a not-for-profit entity (including charitable organizations) that receives contributions from the Company that exceed the greater of $200,000 or 2 percent of consolidated gross revenues of the recipient for that year.

f. Is not part of an interlocking directorate in which the CEO or other employee of the Company serves on the board of another company employing the director.

g. Has not had any of the relationships described above with any parent or subsidiary of the Company.

h. Is not a member of the immediate family of any person described in 6a-h.

7. Board Responsibilities: The board responsibilities should include the following:

a. CEO Performance: Independent directors establish CEO performance criteria focused on optimizing operating performance, profitability and shareowner value creation; and regularly review the CEO's performance against those criteria.

b. Corporate Strategy: Review, approve and guide corporate strategy, capital discipline and allocation, major plans of action, risk policies, and business plans.

i. **Capital Allocation Discipline**: Boards should provide shareowners with robust oversight and disclosure surrounding capital allocation decisions, including optimizing the capital structure to ensure discipline in prioritizing the most productive use of capital over the long-term. We recommend the following**:**

a) **Policy**: The board should develop and disclose its policy on capital allocation that outlines the application of discretionary cash flows for organic growth projects, investments, strategic mergers and acquisitions, cash and scrip dividends, debt repayment, and share repurchases. The board should also communicate its philosophy on the use of debt leverage.

b) **Board Monitoring and Assessment**: The board should monitor capital allocation decisions and the range of capital allocation alternatives and their corresponding risks.

c) **Disclosure**: The board should disclose the following details in regulatory filings:

1. The board's role in overseeing capital allocation decisions and how each decision aligns with the company's strategic priorities for investment to ensure long-term value creation
2. The controls and metrics in place to monitor capital allocation decisions

3. The impact on performance targets in executive compensation plans
4. The board's measures to address potential conflicts of interest with incentives impacted by capital allocation decisions, such as share buybacks.

c. Corporate Performance: Set performance objectives, monitor implementation and corporate performance, and oversee major capital expenditures, and acquisitions/divestitures.

d. Corporate Culture: Boards should have an active role in setting a high-performance corporate culture, which includes: respectful treatment of employees; efforts to promote diversity, inclusion and innovation; providing a workplace free of sexual harassment and other forms of harassment; fostering trust between employees and management; and promoting ownership and accountability for an ethical corporation.

i. **Policy**: The board should develop and disclose its efforts towards establishing effective corporate culture, including its anti-harassment policy, and the mechanisms through which the board learns about employee complaints, how the claims are addressed, and the actions taken. CalPERS supports voluntary arbitration in company policies.

ii. **Board Oversight**: Boards should have oversight of the following:

a. Review of the company's policies, practices and executive responsibilities related to corporate culture

b. Review of the potential risks related to corporate culture, including all forms of harassment

c. Implementation of effective corporate culture

iii. **Disclosure**: Companies should ensure all settlements are reported to the Board. Financial-reporting standard setters generally require disclosure of material settlements, including those involving sexual harassment. CalPERS supports disclosure of settlements, including those related to sexual harassment, involving an executive or member of the board or at any level within the company when a pattern of behavior is demonstrated.

e. Corporate Annual Report and Accounts: Affirm that the company's annual report and accounts present a true and fair view of the company's position and prospects. As appropriate, taking into account statutory and regulatory obligations in each jurisdiction, the information provided in the annual report and accounts should comply with the following:

i. be relevant to investment decisions, enabling shareowners to evaluate risks, past and present performance, and to draw inferences regarding future performance;

ii. enable shareowners, who put up the risk capital, to fulfill their responsibilities as owners to assess company management and the strategies adopted

iii. be a faithful representation of the events it purports to represent

iv. generally, be neutral and report activity in a fair and unbiased way except where there is uncertainty (prudence should prevail such that assets and income are not overstated and liabilities and expenses are not understated; there should be substance over form; any off-balance sheet items should be appropriately disclosed)

v. be verifiable so that when a systematic approach and methodology is used the same conclusion is reached
vi. be presented in a way that enables comparisons to be drawn of both the entity's performance over time and against other entities
vii. recognize the 'matching principle', which requires that expenses are matched with revenues.
viii. recognize the establishment and maintenance of an effective system of internal control which should be measured against internationally accepted standards of internal audit and tested periodically for its adequacy(where an internal audit function has not been established, full reasons for this should be disclosed in the annual report, as well as an explanation of how adequate assurance of the effectiveness of the system of internal controls has been obtained)

f. Reincorporation: When considering reincorporation, corporations should analyze shareowner protections, company economic, capital market, macro-economic, and corporate governance considerations. Companies should not reincorporate to offshore locations where corporate governance structures are weaker, which reduces management accountability to shareowners.

g. Charitable and Political Contributions: Robust board oversight and disclosure of corporate charitable and political activity is needed to ensure alignment with business strategy and to protect assets on behalf of shareowners. We recommend the following:

i. **Policy**: The board should develop and disclose a policy that outlines the board's role in overseeing corporate charitable and political contributions (including direct or indirect[4] lobbying and grassroots lobbying communications[5]), the terms and conditions under which charitable and political contributions are permissible, and the process for disclosing charitable and political contributions annually.
ii. **Board Monitoring, Assessment and Approval**: The board of directors should monitor charitable and political contributions (including direct or indirect lobbying and grassroots lobbying communications) made at the local, state, and federal levels by the company. The board should ensure that only contributions consistent with and aligned to the interests of the company and its shareowners are approved.
iii. **Disclosure**: The board should disclose on an annual basis the amounts and recipients of monetary and non-monetary contributions made by the company at the local, state, and federal levels during the prior fiscal year. If any expenditure earmarked or used for political or charitable activities were provided to or through a third-party to influence elections of candidates or ballot measures or governmental action, then those expenditures should be included in the report.

[4] "Indirect lobbying" is lobbying activities engaged in by a trade association or other organization of which the company is a member or a financial contributor.
[5] "Grassroots lobbying communication" is a communication directed to the general public that (a) refers to specific legislation or regulation, (b) reflects a view on the legislation or regulation and (c) encourages the recipient of the communication to take action with respect to the legislation or regulation.

8. **Board, Committee, and Director Evaluation**: No board can truly perform its function of overseeing a company's strategic direction and monitoring management's success without a system of evaluating itself. The board should establish preparation, participation and performance expectations for itself (acting as a collective body), for the key committees and each of the individual directors. A process by which these established board, key committee and individual director expectations are evaluated on an annual basis should be disclosed to shareowners. Directors must satisfactorily perform based on the established expectations with re-nomination based on any other basis being neither expected nor guaranteed.

9. **Board Talent Assessment and Diversity**: The board should facilitate a process that ensures a thorough understanding of the diverse characteristics necessary to effectively oversee management's execution of a long-term business strategy. Board diversity should be thought of in terms of skill sets, gender, age, nationality, race, sexual orientation, gender identity, disability, and historically under-represented groups. Consideration should go beyond the traditional notion of diversity to include a more broad range of experience, thoughts, perspectives, and competencies to help enable effective board leadership. A robust process for how diversity is considered when assessing board talent and diversity should be adequately disclosed and include the following:
   a. **Director Talent Evaluation**: To focus on the evolving global capital markets, a board should disclose its process for evaluating the diverse talent and skills needed on the board and its key committees.
   b. **Director Attributes**: Board attributes should include a range of skills and experience which provide a diverse and dynamic team to oversee business strategy, risk mitigation and senior management performance. The board should establish and disclose a diverse mix of director attributes, experiences, perspectives and skill sets that are most appropriate for the company. Collectively, director attributes should include expertise in at least the following areas: accounting or finance, international markets, business, human capital management, industry knowledge, governance, customer-base experience or perspective, crisis response, leadership, strategic planning, and competence managing multifaceted risk – including expertise and experience in climate change and other environmental risk management strategies, where material to business model or operations. Additionally, existing directors should receive continuing education regarding a company's activities and operations to ensure the board maintains the necessary skill sets and knowledge to meet its fiduciary responsibilities.
   c. **Director Nominations**: With each qualified director nomination recommendation, the board should consider the issue of competence, independence, continuing director tenure, as well as board diversity, and take steps as necessary to ensure that the board maintains openness to new ideas, a willingness to re-examine the status quo, and ability to exercise judgment in the best interests of the corporation free of any external influence that may attempt to be or may appear to be exerted upon them.

d. **Director Tenure**: Boards should consider all relevant facts and circumstances to determine whether a director should be considered independent – these considerations include the director's years of service on the board – extended periods of service may adversely impact a director's ability to bring an objective perspective to the boardroom. We believe director independence can be compromised at 12 years of service – in these situations a company should carry out rigorous evaluations to either classify the director as non-independent or provide a detailed annual explanation of why the director can continue to be classified as independent. Additionally, there should be routine discussions as part of a rigorous evaluation and succession planning process surrounding director refreshment to ensure boards maintain the necessary mix of skills, diversity, and experience to meet strategic objectives.

e. **Diversity Disclosure**: Boards should annually disclose their demographic information including race, ethnicity and gender. Ideally, companies should disclose their Employer Information Report, known as the EEO-1 report, or similar workforce demographic data to enable shareowners to assess the board's diversity relative to its workforce and compare companies in similar industries.

10. **Role of the Audit Committee**: At least one member of the Audit Committee should have recent and relevant financial experience. The main role and responsibilities of the Audit Committee should be described in the committee's terms of reference including the following:

a. **Auditor Liability**: To strengthen the auditor's objective and unbiased audit of financial reporting, audit committees should ensure that contracts with the auditor do not contain specific limits to the auditor's liability to the company for consequential damages or require the corporation to use alternative dispute resolution.

b. **Auditor Selection**: Audit committees should promote expanding the pool of auditors considered for the annual audit to help improve market competition and thereby minimize the concentration of only a small number of audit firms from which to engage for audit services. To allow audit committees a robust foundation to determine audit firm independence, auditors should provide three prior years of activities, relationships, and services (including tax services) with the company, affiliates of the company and persons in financial reporting oversight roles that may impact the independence of the audit firm.

c. **Auditor Rotation**: Audit committees should promote rotation of the auditor to ensure a fresh perspective and review of the financial reporting framework.

d. **Audit Committee Communication with Auditor**: The auditor should articulate to the Audit Committee, risks and other matters arising from the audit that are significant to the oversight of the financial reporting process, including situations where the auditor is aware of disputes or concerns raised regarding accounting or auditing matters. The Audit Committee should consider providing to investors a summary document of its discussions with auditors to enhance investor confidence in the audit process.

e. **Monitoring the integrity of the accounts**: And any formal announcements relating to the company's financial performance, and reviewing significant financial reporting judgments contained in them.

f. **Oversight of key accounting policies and accounting judgments**: Which should be in accordance with generally accepted international accounting standards, and disclosing such policies in the notes to the company's accounts.

g. **Audit Scope**: Agreeing to the minimum scope of the audit as prescribed by applicable law and any further assurance that the company needs. Shareowners (who satisfy a reasonable threshold shareholding) should have the opportunity to expand the scope of the forthcoming audit or discuss the results of the completed audit should they wish to.

h. **Auditor Independence**: Assuring itself of the quality of the audit carried out by the external auditors and assessing the effectiveness and independence of the auditor each year. This includes overseeing the appointment, reappointment and, if necessary, the removal of the external auditor and the remuneration of the auditor. There should be transparency in advance when the audit is to be tendered so that shareowners can engage with the company in relation to the process should they so wish.

i. **Auditor Dialogue**: Having appropriate dialogue with the external auditor without management present and overseeing the interaction between management and the external auditor, including reviewing the management letter provided by the external auditors and overseeing management's response; and reporting on its work and conclusions in the annual report.

j. **Assertion of Internal Financial Controls**: The Audit Committee should require the auditor's opinion to include commentary on any management assertion that the system of internal financial controls is operating effectively and efficiently, that assets are safeguarded, and that financial information is reliable as of a specific date, based on a specific integrated framework of internal controls.

k. **Audit Committee Expertise**: Audit Committee financial expertise at a minimum should include skill-sets as outlined by Section 407(d)(5)(i) of Regulation S-K and the Exchange listing requirements. Boards should consider the effectiveness of the Audit Committee and designated financial expert(s) in its annual assessment. Firms may be able to reduce their cost of capital as related to the quality of its financial reporting. The quality of financial reporting can be increased by appropriately structuring the Audit Committee with effective financial expertise.

l. **Annual Reporting**: Disclosures in the annual reporting must include the following:
   i. Assessment of the independence and objectivity of the external auditor to assure the auditors and their staff have no financial, business, employment or family and other personal relationships with the company
   ii. Assessment of the appropriateness of total fees charged by the auditors;
   iii. Assessment of non-audit services and fees charged including limitations or restrictions tied to the provision of non-audit services

iv. Explanation of why non-audit services were provided by the auditor rather than by another party and how the auditor's independence has been safeguarded;
v. Rational for recommending the appointment, reappointment or removal of the external auditor, including information on tendering frequency, tenure, and any contractual obligations that acted to restrict the choice of external auditors
vi. Auditor rotation period
vii. Assessment of issues which resulted in an auditor resignation
viii. Assessment of all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit clients or persons in a financial reporting oversight role that may have a bearing on independence.

11. **Role of the Nomination Committee**: The main role and responsibilities of the nomination committee should be described in the committee's terms of reference including the following:
   a. **Skills Matrix**: Developing a skills matrix, by preparing a description of the desired roles, experience and capabilities required for each appointment, and then evaluating the composition of the board.
   b. **Board Appointments**: Leading the process for board appointments and putting forward recommendations to shareowners on directors to be elected and re-elected.
   c. **Director Conflicts of Interest**: Upholding the principle of director independence by addressing conflicts of interest (and potential conflicts of interest) among committee members and between the committee and its advisors during the nomination process.
   d. **Independent Consultants**: Considering and being responsible for the appointment of independent consultants for recruitment or evaluation including their selection and terms of engagement and publicly disclosing their identity and consulting fees.
   e. **Shareowner Dialogue**: Entering into dialogue with shareowners on the subject of board nominations either directly or via the board
   f. **Board Succession Planning**: The board should implement and disclose a board succession plan that involves preparing for future board retirements, committee assignment rotations, committee chair nominations and overall implementation of the company's long-term business plan. Boards should establish clear procedures to encourage and consider board nomination suggestions from long-term shareowners. The board should respond positively to shareowner requests seeking to discuss incumbent and potential directors.

12. **Role of the Compensation Committee**: The main role and responsibilities of the compensation committee should be described in the committee terms of reference including the following:
   a. **Compensation Philosophy**: Determining and recommending to the board the remuneration philosophy and policy of the company.

b. **Oversight of Plan Design, Implementation, Monitoring and Evaluation**: Short-term and long-term share-based incentives and other benefits schemes including pension arrangements, for all executive officers.
c. **Director Conflicts of Interest**: Ensuring that conflicts of interest among committee members and between the committee and its advisors are avoided.
d. **Independent Consultants**: Appointing any independent remuneration consultant including their selection and terms of engagement and disclosing their identity and consulting fees; and
e. **Shareowner Dialogue**: Maintaining appropriate communication with shareowners on the subject of remuneration, either directly or via the board.

13. **Risk Oversight**: In response to the turmoil in the financial markets and economic uncertainties, CalPERS has elevated the importance of risk oversight and management. The primary goal is to ensure companies adopt policies, operating procedures, internal controls, federal and state law compliance programs, reporting, and decision-making protocols to effectively manage, evaluate, and mitigate risk. The ultimate outcome is to ensure that companies function as “risk intelligent” organizations. We recommend the following:
    a. The board is ultimately responsible for a company’s risk management philosophy, organizational risk framework and oversight. The board should be comprised of skilled directors with a balance of broad business experience and extensive industry expertise to understand and question the breadth of risks faced by the company. Risk management should be considered a priority and sufficient time should be devoted to oversight.
    b. The company should promote a risk-focused culture and a common risk management framework should be used across the entire organization. Frequent and meaningful communication should be considered the “cornerstone” for an effective risk framework. A robust risk framework will facilitate communication across business units, up the command chain and to the board. The company’s culture with regard to risk and the process by which issues are escalated and de-escalated within the company should be evaluated at intervals as appropriate to the situation.
    c. The board should set out specific risk tolerances and implement a dynamic process that continuously evaluates and prioritizes risks. An effective risk oversight process considers both internal company related risks such as operational, financial, credit, solvency, liquidity, corporate governance, cyber-security, environmental, reputational, social, product safety and external risks such as geopolitical, industry related, systemic, and macro-economic.
    d. Compensation practices should be evaluated to ensure alignment with the company’s risk tolerances and that compensation structures do not encourage excessive risk taking.
    e. At least annually, the board should approve a documented risk management plan and disclose sufficient information to enable shareowners to assess whether the board is carrying out its risk oversight responsibilities. Disclosure should also include the role of external parties such as third-party consultants in the risk management process. While ultimate responsibility for a company’s

risk management approach rests with the full board, having a risk committee (be it a stand-alone risk committee, a combined risk committee with nomination and governance, strategy, audit or other) can be an effective mechanism to bring the transparency, focus and independent judgment needed to oversee the company's risk management approach.

f. While the board is ultimately responsible for risk oversight, executive management should be charged with designing, implementing and maintaining an effective risk program. Roles and reporting lines related to risk management should be clearly defined. At a minimum, the roles and reporting lines should be explicitly set out for the board, board risk committees, Chief Executive Officer, Chief Financial Officer, the Chief Risk Officer, and business unit heads. The board and risk related committees should have appropriate transparency and visibility into the organization's risk management practices to carry out their responsibilities.

14. CEO Succession Plan: The board should proactively lead and be accountable for the development, implementation, and continual review of a CEO succession plan. Board members should be required to have a thorough understanding of the characteristics necessary for a CEO to execute on a long-term strategy that optimizes operating performance, profitability and shareowner value creation. At a minimum, the CEO succession planning process should include the following:

a. Become a routine topic of discussion by the board.

b. Extend down throughout the company emphasizing the development of internal CEO candidates and senior managers while remaining open to external recruitment.

c. Require all board members be given exposure to internal candidates.

d. Encompass both a long-term perspective to address expected CEO transition periods and a short-term perspective to address crisis management in the event of death, incapacitation or untimely departure of the CEO.

e. Provide for open and ongoing dialogue between the CEO and board while incorporating an opportunity for the board to discuss CEO succession planning without the CEO present.

f. Be disclosed to shareowners on an annual basis and in a manner that would not jeopardize the implementation of an effective and timely CEO succession plan.

15. Director Succession Plan: The board should proactively lead and be accountable for the development, implementation, and continual review of a director succession plan. Board members should be required to have a thorough understanding of the characteristics necessary to effectively oversee management's execution of a long- term strategy that optimizes operating performance, profitability, and shareowner value creation. At a minimum, the director succession planning process should include the following:

a. Become a routine topic of discussion by the board.

b. Encompass how expected future board retirements or the occurrence of unexpected director turnover as a result of death, incapacitation or untimely departure is addressed in a timely manner.

c. Encompass how director turnover either through transitioning off the board or as a result of rotating committee assignments and leadership is addressed in a timely manner.
d. Provide for a mechanism to solicit shareowner input.
e. Be disclosed to shareowners on an annual basis and in a manner that would not jeopardize the implementation of an effective and timely director succession plan.

16. **Human Capital Management Practices**: Corporations should adopt maximum progressive practices toward the elimination of human rights violations in all countries or environments in which the company operates. Additionally, these practices should emphasize and focus on preventing discrimination, harassment of any kind including sexual harassment, and/or violence based on race, color, religion, national origin, age, disability, sexual orientation, gender identity, marital status, or any other status protected by laws or regulations in areas of a company's operation. Boards should be accountable for companies to develop and implement company policies, procedures, integrated financial reporting, training and internal reporting structures to ensure commitment to the following:
    a. **Universal Human Rights**: Express our support for universal human rights and, particularly, those of our employees, the communities within which we operate, and parties with whom we do business. This includes free, prior, and informed consent as a standard in relation to Indigenous Peoples' rights.
    b. **Equal Employment Opportunity**: Promote equal opportunity for our employees at all levels of the company with respect to issues such as color, race, gender, age, disability, ethnicity or religious beliefs, and operate without unacceptable worker treatment such as the exploitation of children, physical punishment, female abuse, involuntary servitude, or other forms of abuse.
    c. **Freedom of Association**: Respect our employees' voluntary freedom of association.
    d. **Eliminate all Forms of Forced and Compulsory Labor**: Compensate our employees to enable them to meet at least their basic needs and provide the opportunity to improve their skill and capability in order to raise their social and economic opportunities.
    e. **Provide a safe and healthy workplace**: Protect human health and the environment; and promote sustainable development.
    f. **Promote fair competition**: This includes respect for intellectual and other property rights, and not offer, pay or accept bribes.
    g. **Strategic Social Investment**: Work with governments and communities in which we do business to improve the quality of life in those communities – including their educational, cultural, economic and social well-being – and seek to provide training and opportunities for workers from disadvantaged backgrounds.
    h. **Application to Supply Chain**: Promote the application of these principles by those with whom we do business

C. Executive, Director, and Employee Compensation

CalPERS believes well-designed compensation programs can be a powerful and effective tool to reward value-creating executives and employees and appropriately align their interests with those of providers of capital (shareowners) to achieve sustainable, long-term investment returns.

CalPERS recognizes that having a one-size-fits-all compensation program may not be appropriate for companies of different sizes, locations, and industries. Therefore, we believe companies should have flexibility in designing and structuring their compensation programs, given their disparate operating business models.

Our compensation principles are intended to provide a framework for companies to consider in designing and implementing their compensation programs.

The following summarizes our compensation principles:

1. **Compensation Philosophy**: Companies that demonstrate sustainable long-term performance should be able to properly reward their executives and employees for contributing to the success of the business and creating long-term shareowner value. The board, through its Compensation Committee, has the core function to ensure compensation programs are:
    a. **Aligned with Providers of Capital:** Compensation programs should symmetrically align the interests of the companies' executives and employees with the providers of capital, that is, both sides should participate in good and bad times. Incentive pay should be tied to shareowner experience.
    b. **Linked to Performance:** Compensation programs should have an appropriate pay-for-performance alignment where pay is directly linked to company performance. Executives and employees should be rewarded for focusing on and generating sustainable long-term performance.
    c. **Risk Aware:** Compensation programs should incentivize prudent risk taking by executives and employees. The rationale for the appropriateness of the metrics used to promote long-term shareowner value creation should be adequately disclosed and explained in the compensation programs.
    d. **Aligned with Business Strategy:** Compensation programs should provide a clear and well-articulated philosophy that links compensation and performance metrics to the company's long-term business strategy.
    e. **Supportive of Sustainability Objectives:** Compensation programs should be designed to support relevant sustainability performance objectives.
    f. **Cost Effective & Equitable:** Compensation programs should not result in unwarranted transfer of wealth from shareowners to company executives and employees. Compensation should be reasonable and equitable, and the quantum should be determined within the context of the company's workforce as a whole.
    g. **Free from Discrimination & Bias:** Compensation programs should actively incentivize fairness and structurally avoid discrimination and bias that may unfairly affect the compensation of any employee, such as discrimination and bias related to gender, age, nationality, race, sexual orientation, gender identity and disability. Through an active

approach to bias and discrimination elimination, companies should strive to attract and retain the best employees and mitigate risk of legal challenges.

h. **Transparent:** Compensation programs should be transparent and provide clear, comprehensive, and relevant disclosures necessary to allow shareowners to evaluate a company's compensation practices.

2. **Compensation Elements:** Compensation programs should have an appropriate mix of fixed and variable pay elements, and a significant portion of the plans should be performance-based.
   a. **Salary:** Salary is one of the few components of compensation not "at risk," therefore it should be set at a reasonable level and appropriately reflect the responsibilities at the company.
   b. **Incentive Compensation:** Incentive compensation, whether short-term or long-term, should be demonstrably linked to company performance and enhance long-term shareowner value. We believe incentive compensation should be primarily long-term and performance-based. Companies should disclose and discuss the relevance and appropriateness of the award structures, such as performance metrics, peer groups, performance periods, and/or any other performance conditions, in the context of how they relate to company's specific strategy, business or industry. Rationale should be provided for performance metrics chosen and why the performance targets are relevant and challenging. We believe performance targets should be challenging, and except in rare and extraordinary situation, the Compensation Committee should not "lower the bar" by changing the performance targets. The Compensation Committee should fully disclose revised performance targets and provide sufficient justification if significant changes are made to initial or prior year ones. Additionally, compensation programs should disclose equity ownership and retention guidelines. It is important for the executive's financial interests to be aligned with those of shareowners and the company's long-term success, so we believe executives should attain and continuously hold a significant equity investment in the company they are managing. Furthermore, all equity awards, whether subject to equity ownership requirements or not, should not be hedged, pledged, or otherwise encumbered.
   c. **Other Forms of Compensation:** We believe that additional compensation awards granted outside of the company's incentive plans may potentially undermine the integrity of its regular incentive plans or the link between pay and performance, or both. While we are wary of such awards, we recognize that additional compensation awards, such as supplemental or one-off awards, may be appropriate if companies provide a thorough description as well as an explanation of how they align with long-term company performance and shareowner value creation.
   d. **Retirement Plans and Other Post-Employment Benefits:** We believe post-employment benefits, including retirement plans, can be an important part of overall compensation. Companies should clearly articulate and disclose post-employment benefits, which may include defined contribution/benefit plans, supplemental executive retirement plans (SERPs), health care benefits, pensions or other retirement benefits, and provide an explanation demonstrating how these align with long-term shareowners' interests.

3. **Compensation Structure:** We believe it is in the best interests of companies to have well-structured compensation programs that properly incentivize executives and employees, appropriately align the interests of executives and shareowners, and create long-term shareowner value. Compensation plan structures, including the quantitative and qualitative components, should be thoroughly disclosed in the compensation programs for shareowners to evaluate the compensation practices.
    a. **Shareowner Advisory Vote on Executive Compensation:** Companies should submit executive compensation policies to shareowners for approval on an annual basis.
    b. **CEO Pay Ratio:** Companies should disclose the ratio of CEO compensation to the median annual total compensation of all other employees, and the methodology used to determine the ratio. CEO pay should be consistent with internal wage structures (CEO to median employee, and CEO to named executive officers) rather than be driven by external benchmarking. Internal pay equity is important for recognizing and incentivizing the contribution of the general employee base to the company's success as well as attracting and retaining employees.
    c. **Peer Benchmarking:** Companies should disclose the companies in peer groups used for benchmarking and/or other comparisons. We believe companies should not use peer groups to ratchet up pay that is seemingly unrelated to company performance. Where peer benchmarking is used, target pay percentile levels should be set after considering the company's historic financial performance relative to its chosen peers. Companies should provide a rationale if the peer group used for compensation purposes differs from that used to compare overall company performance. We believe companies should provide sufficient justification for any award of compensation for below median performance.
    d. **Vesting Period/Post-Vesting Holding Requirements:** Companies should disclose and clearly articulate the rationale for vesting periods and any mandatory holding periods on vested awards. The post-vesting holding requirements should ensure the executive's interests are properly aligned with those of long-term shareowners. To achieve this alignment, we believe equity compensation should be subject to a minimum vesting and/or holding period of 5 years from grant date, with the provision that no more than 20% of the equity can be sold annually starting in the sixth year from grant date.
    e. **Post-Separation Holding Period:** Companies should disclose any holding period requirements for executives after retirement or separation of service. We believe the equity compensation earned by executives should be held for a minimum of 2 years after they retire or separate from the company.
    f. **Excise Tax Gross-Ups:** We believe excise tax gross-ups should not be permitted in compensation programs. If tax gross-up provisions are used, companies should disclose them and provide justifications for having such arrangements in the compensation programs.
    g. **Clawback Policy:** Companies should develop and disclose policies to recoup compensation made to executives during periods of fraudulent activity, inadequate oversight, misconduct including harassment of any kind such as sexual harassment, or gross negligence, which impacted or is reasonably expected to impact financial results or cause reputational harm.

h. **Change in Control Payments:** Any provisions providing for compensation following change-in-control events should be "double-triggered," that is, such provisions should stipulate that compensation is payable only: (a) after a control change takes place, and (b) if a covered executive's job is terminated or downgraded because of the control change.
i. **Severance Agreements:** In cases where the company will consider severance agreements, the policy should contain the overall parameters of how such agreements will be used including the specific detail regarding the positions within the company that may receive severance agreements; the maximum periods covered by the agreements; provisions by which the agreements will be reviewed and renewed; any hurdles or triggers that will affect the agreements; a clear description of what would and would not constitute termination for cause; and disclosure of where investors can view the entire text of severance agreements. Severance payments that provide benefits with a total present value exceeding market standard should be ratified by shareowners.
j. **Hedging:** Companies should disclose hedging policies that prohibit the use of derivatives or other structures to hedge director or executive stock ownership. We believe hedging undermines the alignment of interests of the executives with shareowners and should be prohibited.

4. **Equity Plan:** CalPERS believes equity-based compensation plans are a useful way for companies to reward all levels of management and staff to further align the action of employees with shareowners. When seeking shareowner approval, the Compensation Committee should fully disclose its equity-based compensation plan philosophy, longer-term vesting schedule, and how it plans to implement the program. Disclosure related to plan costs; frequency of requests for shares; annual and absolute dilution; option repricing, backdating, and spring-loading/bullet-dodging policy; distribution of shares at all levels of the firm; burn-rate; and change-in-control provision and evergreen provisions will be assessed for alignment with shareowners.

5. **Director Compensation**: Independent directors should be reasonably compensated for serving on the company's board. To ensure directors maintain their independence, objectivity, and alignment with shareowners' interests, director compensation (a) should be in the form of cash and/or equity-based awards that should be fully vested on grant date, and (b) should not include any change-in-control or severance arrangements. Company insiders serving on a board should not receive additional compensation. We believe the compensation programs should not provide directors with performance-based awards under any circumstances, as such awards may create a potential conflict with the directors' primary role as an independent representative of shareowners. Companies should fully disclose director equity ownership and holding requirements and guidelines. To demonstrate alignment with shareowners, directors should attain and continuously maintain an equity ownership in the company that is meaningful given their particular financial context. Also, directors should repay compensation to the company in the event of malfeasance or a breach of fiduciary duty involving the director.

D. Corporate Reporting

CalPERS expects fair, accurate and timely reporting on how companies employ and identify risks related to financial, human and physical capital, in order to generate sustainable economic returns.

1. **Integrated Financial Reporting**: Financial reporting plays an integral role in the capital markets by providing transparent and relevant information about the economic performance and condition of businesses. Effective financial reporting depends on high quality accounting standards, as well as consistent application, rigorous independent audit and enforcement of those standards. Companies should provide for the integrated representation of operational, financial, human capital management practices, environmental, social, and governance performance in terms of both financial and non-financial results in order to offer investors better information for assessing risk. The board should provide an integrated report that puts historical performance into context, and portrays the risks, opportunities and prospects for the company in the future, helping shareowners understand a company's strategic objectives and its progress towards meeting them. Such disclosures should:
   - **a.** be linked to the company's business model
   - **b.** be genuinely informative and include forward-looking elements where this will enhance understanding
   - **c.** describe the company's strategy, and associated risks and opportunities, and explain the board's role in assessing and overseeing strategy and the management of risks and opportunities
   - **d.** be accessible and appropriately integrated with other information that enables shareowners to obtain a picture of the whole company
   - **e.** use key performance indicators (KPIs) that are linked to strategy and facilitate comparisons, including human capital KPIs such as:
     - total workforce cost
     - stability of the workforce, including voluntary and involuntary turnover and internal hire rates
     - average hours of training per employee per year
     - safety of workforce, including frequency, severity and lost-time due to injuries, illness and fatalities
     - diversity data including race, ethnicity and gender by level such as an Employer Information Report, known as the EEO-1 report, or similar demographic data
     - standardized measures of employee satisfaction use objective metrics where they apply and evidence-based estimates where they do not
     - be strengthened where possible by independent assurance that is carried out annually and with regard to established disclosure standards
   - **f.** use objective metrics where they apply and evidence-based estimates where they do not

   g. be strengthened where possible by independent assurance that is carried out annually and with regard to established disclosure standards

2. **Transparency**: Operational, financial, and governance information about companies must be readily transparent to permit accurate market comparisons; this includes disclosure and transparency of objective globally accepted minimum accounting standards, such as the International Financial Reporting Standards (IFRS).
   - **a. Comprehensive Disclosure**: The board should present a balanced and understandable assessment of the company's position and prospects in the annual report and accounts in order for shareowners to be able to assess the company's performance, business model and strategy (including human capital management, and climate change strategy) and long-term prospects. Additionally, to provide for efficient analysis and comparison of corporations by shareowners, corporations should adopt well-known reporting standards[6] and tools to disclose industry-relevant environmental, social, and governance risks and opportunities that can affect the performance of the company.
   - **b. Materiality**: The board should disclose relevant and material information on a timely basis so as to allow shareowners to take into account information which assists in identifying risks and sources of wealth creation. Issues material to shareowners should be set out succinctly in the annual report, or equivalent disclosures, and approved by the board itself.
   - **c. Board Governance Principles**: The board should adopt and disclose a written statement of its own governance principles, and re-evaluate them on at least an annual basis.

3. **Proxy Materials**: Proxy materials should be written in a manner designed to provide shareowners with the information necessary to make informed voting decisions. Similarly, proxy materials should be distributed in a manner designed to encourage shareowner participation. All shareowner votes, whether cast in person or by proxy, should be formally counted with vote outcomes formally announced.

4. **Auditor's Enhanced Reporting to Investors**: Auditors should provide independent assurance and attestation to the quality of financial statements to instill confidence in the providers of capital. Auditors should bring integrity, independence, objectivity, and professional competence to the financial reporting process. The audit opinion should state whether the financial statements and disclosures are complete, materially accurate, and free of material misstatement, whether caused by error or fraud. Auditors should provide a reasonable and balanced assurance on financial reporting

[6] The Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), Global Reporting Initiative Standards (GRI), International Integrated Reporting Council (IIRC) and Carbon Disclosure Project (CDP) offer useful investor endorsed disclosure guidance.

matters to investors in narrative reports such as an Auditor's Discussion and Analysis (AD&A) or a Letter to the Shareowners. Enhanced reporting should include:

- **a.** Business, operational and other risks believed to exist and considered.
- **b.** Assumptions used in judgments that materially affect the financial statements, and whether those assumptions are at the low or high end of the range of possible outcomes.
- **c.** Appropriateness of the accounting policies adopted by the company.
- **d.** Changes to accounting policies that have a significant impact on the financial statements.
- **e.** Methods and judgments made in valuing assets and liabilities.
- **f.** Unusual transactions.
- **g.** Accounting applications and practices that are uncommon to the industry.
- **h.** Identification of any matters in the Annual Report that the auditors believe are incorrect or inconsistent with the information contained in the financial statements or obtained in the course of their audit.
- **i.** Audit issues and their resolutions, which the audit partner documents in a final audit memo to the Audit Committee.
- **j.** Quality and effectiveness of the governance structure and risk management.
- **k.** Completeness and reasonableness of the Audit Committee report.

5. **Stakeholder Relations**: CalPERS believes that corporations should strive for active cooperation with stakeholders. This cooperation will be most likely to create wealth, employment and sustainable economies. With adequate, accurate and timely data disclosure of environmental, social, and governance practices, shareowners are able to more effectively make investment decisions by taking into account those practices of the companies in which the System invests.

6. **Environmental Management Practices**: CalPERS' believes companies' long-term value creation requires effective management of environmental risks and opportunities. Companies should identify, manage, and disclose material environmental risks and opportunities that are relevant to their short and long-term success. Environmental issues may include the following:
   - i. **Environmental effects on company**: change, volatility or deterioration in the environment that may impact business operations, such as:
     - climate change, extreme weather
     - loss or degradation of ecosystem services (e.g., pollination), decline of biodiversity
     - change in access to clean, affordable and adequate sources of water and other critical natural resources (e.g., natural food supplies)
   - ii. **Company impact on the environment**: Potential regulatory change, liability, license to operate, reputational or market access risks posed by the company's environmental impacts, including:

- emissions, pollution, waste, loss of biodiversity, degradation of natural ecosystems (e.g., deforestation)

iii. **Transition**: Transition of company's industry and/or customers toward more sustainable products, services or practices, such as:
- low carbon economy, technologies improving environmental outcomes
- sustainability certifications, restoration, adaptation and risk mitigation business models

With regard to material environmental risk and opportunities, good practices include:

a. Board Oversight:

i. The board identifies and oversees management of material environmental risks and opportunities and sets robust and relevant environmental strategy, time-bound goals and/or targets[7].

ii. Board member(s), board committee(s), or full board have pertinent environmental knowledge and experience, or have a designated committee or other such body with the ability to access independent sources of such knowledge and experience.

iii. Alignment of lobbying (including direct or indirect lobbying and grassroots lobbying communications) activities and company expenditures with environmental strategy.

b. Management Execution

i. Senior executives manage the development and execution of science-based and time-bound environmental strategies, goals, and/or targets.

ii. Risk and opportunity management throughout the value chain, strategic planning and general business activities integrate environmental considerations.

iii. Executive officers' compensation is linked to attainment of environmental goals and targets.

iv. The company calculates environmental metrics relevant to its business operations annually, including, but not limited to, greenhouse gas emissions.

c. Disclosure on Environmental Risks and Opportunities[8]:

i. Governance: Company's governance around environmental risks and opportunities.

ii. Strategy: Actual and potential impacts on the company's businesses, strategy and financial planning.

   i. Risks and opportunities the company has identified over the short, medium, and long-term.

   ii. Environmental commitments the company has made including timelines, targets, and impact on financial statements, and business strategy.

[7] The global climate change agreement reached at the 21st Conference of the Parties (COP21), "The Paris Agreement", provides globally agreed, and CalPERS endorsed, targets related to climate change.

[8] The Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), GRESB and CDP offer useful investor endorsed disclosure guidance pertaining to climate impacts, deforestation, water and other potentially material environmental factors.

iii. Engagement with policy makers regarding environmental risks and opportunities material to the company (including related expenditures).

iii. Risk Management: How the company identifies, assesses, and manages environmental risks and opportunities including the following:

i. How company works to ensure its business models and supply chain are robust, responsive, and/or resilient.

ii. If and how company uses internal pricing for carbon, water, or other natural resources.

iii. How company manages traceability issues in its supply chain.

iv. How company identifies and manages impacts, or potential impacts, on local environments and communities including company's approach to material human capital issues (e.g., public health, land rights, and just transition in relation to workers).

iv. Metrics and Targets: Environmental metrics[4] used to assess and manage relevant environmental risks and opportunities, noting where third-party verification has been used. These metrics should be decision-useful, for both the company and investors. Performance relative to targets and commitments should also be disclosed.

7. **Codes of Conduct/Ethics**: The board should adopt high standards of business ethics through codes of conduct/ethics (or similar instrument) and oversee a culture of integrity, notwithstanding differing ethical norms and legal standards in various countries. This should permeate all aspects of the company's operations, ensuring that its vision, mission and objectives are ethically sound and demonstrative of its values. Codes should be effectively communicated and integrated into the company's strategy and operations, including risk management systems and compensation structures.

   a. **Behavior and Conduct**: The board should foster a corporate culture which ensures that employees understand their responsibilities for appropriate behavior. There should be appropriate board level and staff training in all aspects relating to corporate culture and ethics. Due diligence and monitoring programs should be in place to enable staff to understand relevant codes of conduct and apply them effectively to avoid company involvement in inappropriate behavior.

   b. **Bribery and Corruption**: The board should ensure that management has implemented appropriately stringent policies and procedures to mitigate the risk of bribery and corruption or other malfeasance. Such policies and procedures should be communicated to shareowners and other interested parties.

   c. **Whistleblowing**: The board should ensure that the company has in place an independent, confidential mechanism whereby an employee, supplier or other stakeholder can (without fear of retribution) raise issues of particular concern with regard to potential or suspected breaches of a company's code of ethics or local law.

   d. **Prohibit Greenmail**: Every company should prohibit greenmail.

8. **Company General Meetings**: The general meeting agenda should be posted on the company's website at least one month prior to the meeting taking place. The agenda should be clear and properly itemized and include the date and location of the meeting as well as information regarding the issues to be decided at the meeting.
    a. **Vote Deadline**: The board should clearly publicize a date by which shareowners should cast their voting instructions.
    b. **Share Blocking**: The practice of share blocking or requirements for lengthy shareholdings should be discontinued.
    c. **Selection and Notification of Meeting Time and Location**: Corporations should make shareowners' expense and convenience primary criteria when selecting the time and location of shareowner meetings. Appropriate notice of shareowner meetings, including notices concerning any change in meeting date, time, place or shareowner action, should be given to shareowners in a manner and within time frames that will ensure that shareowners have a reasonable opportunity to exercise their franchise.
    d. **Record Date and Ballot Item Disclosure**: To promote the ability of shareowners to make informed decisions regarding whether to recall loaned shares: (1) shareowner meeting record dates should be disclosed as far in advance of the record date as possible, and (2) proxy statements should be disclosed before the record date passes whenever possible.
    e. **Timely Disclosure of Voting Results**: A company should broadly and publicly disclose in a timely manner the final results of votes cast at annual and special meetings of shareowners. Whenever possible, preliminary results should be announced at the annual or special meeting of shareowners. If a board-endorsed resolution has been opposed by a significant proportion of votes, the company should explain subsequently what actions were taken to understand and respond to the concerns that led shareowners to vote against the board's recommendation.
    f. **Election Polls**: Polls should remain open at shareowner meetings until all agenda items have been discussed and shareowners have had an opportunity to ask and receive answers to questions concerning them.
    g. **Meeting Adjournment and Extension**: Companies should not adjourn a meeting for the purpose of soliciting more votes to enable management to prevail on a voting item. A meeting should only be extended for compelling reasons such as vote fraud, problems with the voting process or lack of a quorum.
    h. **Electronic Meetings**: Companies should hold shareowner meetings by remote communication (so-called "virtual" meetings) only as a supplement to traditional in-person shareowner meetings, not as a substitute. Companies incorporating virtual technology into their shareowner meeting should use it as a tool for broadening, not limiting, shareowner meeting participation. With this objective in mind, a virtual option, if used, should facilitate

the opportunity for remote attendees to participate in the meeting to the same degree as in-person attendees.

i. **Director Attendance**: All directors should attend the annual shareowners' meeting and be available, when requested by the chair, to respond directly to oral or written questions from shareowners.

j. **Broker Non-Votes**: Broker non-votes should be counted for quorum purposes only.

E. Regulatory Effectiveness

It is important to have effective regulation as it protects CalPERS as an investor from externalities, maintains fair, orderly and efficient financial markets, and facilitates capital formation. In order to fulfill their vital functions, regulators need to have funding which is independent, sufficient, and multi-year.

1. **Code of Best Practices**: Each capital market in which shares are issued and traded should adopt its own Code of Best Practices to promote transparency of information, prevention of harmful labor practices, investor protection, and corporate social responsibility. Where such a code is adopted, companies should disclose to their shareowners whether they are in compliance.

2. **Financial Markets**: Policy makers and standards setters who impact investment portfolio risk and return should promote fair, orderly, and effectively regulated financial markets through addressing the following**:**
   a. **Transparency**: To promote full disclosure so that the financial markets provide incentives that price risk and opportunity.
   b. **Governance**: To foster alignment of interest, protect investor rights and independence of regulators.
   c. **Systemic Risks**: To identify issues that give rise to risks that threaten global markets and work to foster action that mitigates those risks.

3. **Global Accounting Standards**: It is critical to maintain high-quality accounting standards in jurisdictions where we invest.

4. **Political Stability**: Progress toward the development of basic democratic institutions and principles, including such things as: a strong and impartial legal system and respect and enforcement of property and shareowner rights. Political stability encompasses the following:
   a. **Political risk**: Internal and external conflict, corruption, the military and religion in politics, law and order, ethnic tensions, democratic accountability, and bureaucratic quality.
   b. **Civil liberties**: Freedom of expression, association and organization rights; rule of law and human rights; free trade unions and effective collective bargaining; personal autonomy and economic rights**.**
   c. **Independent judiciary and legal protection**: An absence of irregular payments made to the judiciary, the extent to which there is a trusted legal framework that honors contracts, clearly delineates ownership and protects financial assets.

5. **Transparency**: Financial transparency, including elements of a free press, is necessary for investors to have truthful, accurate and relevant information. Transparency encompasses the following:

   a. **Freedom of the press**: Structure of the news delivery system in a country, laws and their promulgation with respect to the influence of the news, the degree of political influence and control, economic influences on the news, and the degree to which there are violations against the media with respect to physical violations and censorship.
   b. **Monetary and fiscal transparency**: The extent to which governmental monetary and fiscal policies and implementation are publicly available in a clear and timely manner, in accordance with international standards.
   c. **Stock exchange listing requirements**: Stringency of stock exchange listing requirements with respect to frequency of financial reporting, the requirement of annual independent audits, and minimal financial viability.
   d. **Accounting standards**: The extent to which U.S. Generally Accepted Accounting Principles, or International Accounting Standards are used in financial reporting and whether the country is a member of the International Accounting Standards Council.

6. **Sustainable Policy Framework**: Sound regulation should be based on scientific and transparent analysis of social and environmental issues. Regulation should be long-term focused and stable, providing the certainty for innovation, smart investment, and global competitiveness.
   a. **Productive Labor Practices**: No harmful labor practices or use of child labor. In compliance, or moving toward compliance, with the International Labor Organization (ILO) Declaration on the Fundamental Principles and Rights at Work. Productive Labor Practices encompasses:
      i. **ILO ratification**: Whether the convention is ratified, not ratified, pending ratification or denounced.
      ii. **Quality of enabling legislation**: The extent to which the rights described in the ILO convention are protected by law.
      iii. **Institutional capacity**: The extent to which governmental administrative bodies with labor law enforcement responsibility exist at the national, regional and local levels.
      iv. **Effectiveness of implementation**: Evidence that enforcement procedures exist and are working effectively and evidence of a clear grievance process that is utilized and provides penalties that have deterrence value.
   b. **Environmental Risk Factors**:
      i. **Carbon Pricing Policy**: Policymakers should establish stable and clear carbon pricing policy that appropriately prices the externalized cost to the economy and society from greenhouse gas emissions. Specifically, carbon pricing should be set at a level, and with the regulatory certainty, that incentivizes the business practices, consumer behavior, and related investment decisions needed to drive the transition to a thriving, low-carbon global economy. Effective carbon pricing policies should decrease emissions and therefore the physical risk to investors' portfolios from

climate change. Additionally, policies should be designed to avoid exacerbating economic inequality and its related geopolitical risks, and policies should be designed to provide incentives for carbon sequestration, including through natural methods, such as ecosystem protection and restoration.

7. **Market Regulation and Liquidity**: Regulators should address reputational risk and ensure potential market and currency volatility is adequately rewarded. Market regulation and liquidity encompasses: market capitalization, change in market capitalization, average monthly trading volume, growth in listed securities, market volatility as measured by standard deviation, and return/risk ratio.

8. **Capital Market Openness**: Regulators should ensure free market policies, openness to foreign investors, and legal protection for foreign investors. Capital market openness encompasses the following:
   a. **Foreign investment**: Degree to which there are restrictions on foreign ownership of local assets, repatriation restrictions or un-equal treatment of foreigners and locals under the law.
   b. **Trade policy**: Degree to which there are deterrents to free trade such as trade barriers and punitive tariffs.
   c. **Banking and finance**: Degree of government ownership of banks and allocation of credit, freedom financial institutions have to offer all types of financial services and protectionist banking regulations against foreigners.

9. **Settlement Proficiency/Transaction Costs**: Regulators should ensure reasonable trading and settlement proficiency and reasonable transaction costs. Settlement proficiency/transaction costs encompass the following:
   a. **Trading and settlement proficiency**: Degree to which a country's trading and settlement is automated, and success of the market in settling transactions in a timely, efficient manner.
   b. **Transaction costs**: The costs associated with trading in a particular market, including stamp taxes and duties, amount of dividends and income taxes and capital gains taxes.

APPENDIX A – CALPERS' LABOR PRINCIPLES

- **Freedom of association and the effective recognition of the right to collective bargaining**
  - Seek to support and improve the well-being of employees as part of human capital management strategy and in compliance with applicable laws

- **The elimination of all forms of forced or compulsory labor**
  - Respect the human rights of those affected by their investment activities and seek to confirm that their investments do not flow to companies that utilize forced labor

- **The effective abolition of child labor**
  - Respect the human rights of those affected by their investment activities and seek to confirm that their investments do not flow to companies that utilize child labor

- **The elimination of discrimination in respect of employment and occupation**
  - Respect the human rights of those affected by their investment activities and seek to confirm that their investments do not flow to companies that maintain discriminatory policies. Seek to improve diversity, equity, and inclusion in portfolio investments to address recruitment, retention, and compensation

- **A safe and healthy working environment**
  - Seek to support and improve the well-being of employees as part of human capital management strategy that includes providing a safe and healthy workplace

APPENDIX ~~A~~B

United Nations Supported Principles for Responsible Investment

Launched in April 2006, The Principles for Responsible Investment (PRI) provides the framework for investors to give appropriate consideration to environment, social and corporate governance (ESG) issues. The PRI was created as an initiative of the UN Secretary-General and coordinated by the UNEP Finance Initiative and the UN Global Compact. An international working group of 20 institutional investors was supported by a 70-person multi-stakeholder group of experts from the investment industry, intergovernmental and governmental organizations, civil society and academia.

CalPERS is one of the original signatories.

The Principles

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.

In signing the Principles, we as investors publicly commit to adopt and implement them, where consistent with our fiduciary responsibilities. We also commit to evaluate the effectiveness and improve the content of the Principles over time. We believe this will improve our ability to meet commitments to beneficiaries as well as better align our investment activities with the broader interests of society.

We encourage other investors to adopt the Principles. Additional information can be found at http://www.unpri.org.

APPENDIX ~~B~~C

LIST OF MEMBERSHIPS AND ENDORSEMENTS SUPPORTED BY CALPERS

1. The Global Sullivan Principles
   https://www.sullivanprinciples.html
2. UN Global Compact Principles
   https://www.unglobalcompact.org
3. Council of Institutional Investors (CII)
   http://www.cii.org
4. International Corporate Governance Network Principles (ICGN)
   https://www.icgn.org
5. Ceres
   http://www.ceres.org
6. Sustainability Accounting Standards Board (SASB)
   https://www.sasb.org
7. Taskforce for Climate-related Financial Disclosures (TCFD)
   https://www.fsb-tcfd.org

Governance & Sustainability Principles

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CalPERS