

# Review Draft of Global Governance Principles alignment with Program Core Issues – Second Reading

October 20, 2015

# Today's Objectives

## Today

- Recap new structure and framework
- Respond to questions from September 17, 2015 meeting
- Highlight and seek feedback related to any new principles or gaps requiring further development
- Permission to re-draft to ensure consistency of tone and approach

## Next Meeting – November 18, 2015

- Incorporate any new feedback received from today's meeting
- Continue development of new principles to fill gaps in coverage
- Provide draft of “refreshed” Principles

# Background

- In March 2015, the Global Governance Principles (Principles) were adopted as a Total Fund Policy
- They provide the framework for CalPERS' work through 1) integration into investment decision making 2) engagement and 3) advocacy in support of sustainable investment to reflect our Investment Beliefs
- The Principles are intended to serve as a comprehensive best practice document and speak to our issues of: Investor Rights, Board Quality & diversity, Compensation, Corporate Reporting and Regulatory Effectiveness
- The Principles guide CalPERS engagement, advocacy, and proxy voting decisions, which span more than 10,000 companies in 47 markets
- Each year, the Principles are revised and submitted for approval by the Investment Committee
- On April 13, 2013, the Investment Committee agreed to form an Ad Hoc Global Governance Sub-Committee to oversee review of the Statement of Investment Policy for Global Governance, which includes the Principles, and related issues.

## From To Statement – Recap

From	To
<p><b>Lengthy and complex:</b> duplicative language and organized by capital market – 96 pages assembled over time</p>	<p><b>Clarity</b> of Global Principles framed by the Investment Beliefs and organized by CalPERS' 5 core issues</p> <ul style="list-style-type: none"> <li>• Investor Rights</li> <li>• Board Quality and Diversity</li> <li>• Corporate Reporting</li> <li>• Compensation</li> <li>• Regulatory Effectiveness</li> </ul>
<p><b>Variety of origin:</b> mosaic of principles described through adoption of CalPERS specific and third party references and others in Appendices</p>	<p><b>Simplified:</b> revised format which maintains content while communicating integration with CalPERS Investment Beliefs and application to managers of CalPERS capital across the Total Fund</p>

# New Global Governance Principles Structure

## I. Introduction

- Sets out CalPERS' mission, Investment Beliefs and values
- Captures the history and evolution of the Global Governance Principles highlighting the transition to a wider scope that includes sustainable investment (environmental, social and governance) issues
- Value for investors and the intended audience
- Explains our approach
- Looks forward

## II. Purpose

- Provides an overview of how the Principles are applied to integration, engagement and advocacy across the total fund
- Introduces the CalPERS' Core Issues framework

## III. Global Governance Principles

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

## IV. Appendices

- Principles for Responsible Investment (PRI)
- Includes a list of CalPERS' memberships and supported groups (CII, ICGN, Ceres, etc.)

## Questions to Staff from September 17<sup>th</sup>:

Board Member Questions:	Staff Response/Edit:	Edit is reflected on Page: (Attachment 2)
<ul style="list-style-type: none"> <li>Question on Board Diversity and Tenure (caps).</li> </ul>	<ul style="list-style-type: none"> <li>Under staff review and development.</li> </ul>	
<ul style="list-style-type: none"> <li>Date needs to be updated in first paragraph.</li> </ul>	<ul style="list-style-type: none"> <li>Edit made. Date updated to June 30, 2015 fiscal year end.</li> </ul>	Pg. 3
<ul style="list-style-type: none"> <li>Need to emphasize the whole system is guided by the Board's investment beliefs.</li> </ul>	<ul style="list-style-type: none"> <li>Edit made. Statement now reflects the entire CalPERS system "Boards" Investment Beliefs.</li> </ul>	Pg. 3
<ul style="list-style-type: none"> <li>Question if section 5 on Risk Oversight was removed.</li> </ul>	<ul style="list-style-type: none"> <li>No edit required. The entire section on Risk Oversight had migrated from the "old" principles document to the "new" principles.</li> </ul>	Pg. 17-18
<ul style="list-style-type: none"> <li>Need to talk about an active ownership role rather than the term we use, which is corporate activist role.</li> </ul>	<ul style="list-style-type: none"> <li>Under staff review. Staff will review this element as part of the "Introduction" and "Purpose" re-write.</li> </ul>	
<ul style="list-style-type: none"> <li>Proxy Access question on two year ownership requirement (CII principle).</li> </ul>	<ul style="list-style-type: none"> <li>Edit made. Staff made edit to reflect CalPERS' current position on proxy access reflecting 3% ownership for 3 years with the ability to nominate up to 25% of the board. (vacated SEC rule)</li> </ul>	Pg. 7
<ul style="list-style-type: none"> <li>Revise poison pill section to reflect a full sentence.</li> </ul>	<ul style="list-style-type: none"> <li>Edit made to introduce a full sentence.</li> </ul>	Pg. 8
<ul style="list-style-type: none"> <li>Question on related party transaction and request to review SEC definition.</li> </ul>	<ul style="list-style-type: none"> <li>Under staff review and development.</li> </ul>	

Continued – Questions to Staff from September 17<sup>th</sup>:

Board Member Questions (transcript review):	Staff Response/Edit:	Edit is reflected on page # (Attachment 3)
Universal Proxy	CalPERS position is set out in SEC testimony that all nominees are listed equally on one ballot.	
Judicial Forum – Loser Pays	Under staff review and development.	
Question on principles having equity asset holder bias.	Under staff review and development.	
Question on auditor rotation frequency.	Auditor rotation is best practice.	
Question on the appropriateness of using the term “Human Capital” Management.	Term reflects the Investment Beliefs.	
Question on equity compensation and linking awards to stock price.	Under staff review for development. CalPERS currently recommends the use of <u>multiple</u> performance metrics when linking pay with performance which may include but not limited to TSR, ROC, ROE, and ROA. We also recommend the use of sustainability metrics and linking pay to environmental, health, and safety standards.	

Continued – Questions to Staff from September 17<sup>th</sup>:

Board Member Questions (transcript review):	Staff Response/Edit:	Edit is reflected on page # (Attachment 3)
Question on GHG (greenhouse gas emission) acronym.	Edit made. Staff spelled out Greenhouse Gas Emissions throughout the Principles document.	Pg. 29
Question on regulatory effectiveness and properly funding regulators.	Under staff review and development.	
Question on the location of section related to Corporate Social Responsibility.	Edit made. Staff insert the “Corporate Social Responsibility” language in to Section 16 – Human Capital Management Practices.	Pg. 19
Question on Global Sullivan Principles specific to income inequality and employee compensation.	Change made. Staff restored the Global Sullivan Principle reference surrounding “Employee Compensation”.	Pg. 22
Question on environmental issues specific to water.	Under staff review and development.	
Question over supply chain issues.	Under staff review and development.	
Need to incorporate why the Principles matter to investors within Introduction and Purpose.	Under staff review. To be part of the Introduction and Purpose.	



# Areas Under Review and Development

Subject	Issue
Introduction and Purpose	<ul style="list-style-type: none"> <li>• Incorporate narrative on why principles are meaningful to investors</li> <li>• Introduce Investment Beliefs as framework</li> <li>• Make comments forward looking</li> </ul>
Board Quality and Diversity	<ul style="list-style-type: none"> <li>• Director Tenure to explore term limits</li> </ul>
Investor Rights	<ul style="list-style-type: none"> <li>• Related Party Transactions</li> <li>• Judicial Forum – Loser Pays (fee shifting)</li> <li>• Further consider joint ventures</li> </ul>
Compensation	<ul style="list-style-type: none"> <li>• Income Inequality – develop following CalPERS symposium</li> <li>• Share buybacks and executive compensation</li> <li>• Review of performance metrics linked to equity awards</li> </ul>
Regulatory Effectiveness	<ul style="list-style-type: none"> <li>• Properly funding regulators</li> </ul>
Capital Allocation	<ul style="list-style-type: none"> <li>• Share buybacks and dividends</li> </ul>
Environment and Climate Change	<ul style="list-style-type: none"> <li>• Water related issues</li> <li>• Review best practices following COP 21</li> </ul>
Total Fund Emphasis	<ul style="list-style-type: none"> <li>• Principles in the current form have a bias to equity</li> <li>• Explore how to incorporate other asset classes</li> </ul>
Human Capital Management	<ul style="list-style-type: none"> <li>• Review and develop supply chain</li> </ul>

# Revision Timeline

