

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

December 14, 2015

# Today's Objectives

## Today

- From To Statement – Overview of structure and framework
- Recap and discuss individual principle revisions:
  - Introduction and Purpose sections
  - Tenure
- Respond to questions from November 18, 2015 meeting
- Areas for future Review and Development
- Seek Subcommittee approval of the Global Governance Principle revisions

## Next Steps

- Integrate feedback received from today's meeting
- Continue development of principles for future discussion
- Present the Global Governance Principles to the Investment Committee at the February 2016 meeting

# 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 core 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

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
- Briefly captures the evolution of the Global Governance Principles highlighting the transition to a wider scope that includes sustainable investment (ESG, financial markets and regulation) 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.)

# Principle Revision Recap

Section	Principle	Proposed Language	Section/Page Number
Introduction and Purpose		See Attachment #2 with tracked changes. Staff refreshed the Introduction and Purpose to include statement on regulatory environment, financial markets, ESG components, and remove historical focus.	Page 3-9
Board Quality: Diversity, Independence, and Competence (Tenure change from 10 years to 12 years)	Director Tenure (New language underlined)	Boards should consider all relevant facts and circumstances to determine whether a director should be considered independent – these considerations should include the director’s years of service on the board as extended tenure may adversely impact a director’s ability to bring an objective perspective to the boardroom. <u>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 detailed annual explanation why the director can continue to be classified as independent.</u> Additionally there should be routine discussions <u>as part of a rigorous evaluation and succession planning process</u> surrounding director refreshment to ensure boards maintain the necessary mix of skills, <u>diversity</u> , and experience to meet strategic objectives.	Section B-9d Page 20
Regulatory Effectiveness	Properly Funded Regulators	In order to fulfill their vital function regulators need to have funding which is independent, sufficient, and multi-year.	Section E (Intro) Page 37
General edits		The document has been edited to provide for a more consistent tone. See tracked changes throughout the document.	

## Response to Questions at November 18, 2015 meeting:

Board Member Questions:	Staff Response/Edit:
<ul style="list-style-type: none"> <li>Board Turnover/Refreshment</li> </ul>	<ul style="list-style-type: none"> <li>For future review and development. Staff will continue to work on board refreshment concepts.</li> </ul>
<ul style="list-style-type: none"> <li>Minimum standard (SEC requirement) related to proxy access nominee disclosures.</li> </ul>	<ul style="list-style-type: none"> <li>For future review and development.</li> </ul>
<ul style="list-style-type: none"> <li>Question on proxy confidentiality and investors providing disclosure to management on how institutions voted.</li> </ul>	<ul style="list-style-type: none"> <li>For future review and development.</li> </ul>
<ul style="list-style-type: none"> <li>Request to re-word the first sentence of introduction to “The nation’s largest public pension fund”.</li> </ul>	<ul style="list-style-type: none"> <li>Edit made – see tracked changes. <b>(page #1)</b></li> </ul>
<ul style="list-style-type: none"> <li>Employee Compensation (Statement from Global Sullivan Principles)</li> </ul>	<ul style="list-style-type: none"> <li>For future review and development.</li> </ul>
<ul style="list-style-type: none"> <li>Compensation – Stock Options and the short-term</li> </ul>	<ul style="list-style-type: none"> <li>For future review and development.</li> </ul>
<ul style="list-style-type: none"> <li>Request to change “Executive Compensation” to “Compensation” for consistency</li> </ul>	<ul style="list-style-type: none"> <li>Edits made – see tracked changes</li> </ul>

## Areas for future Review and Development

Subject	Issue
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> <li>• Proxy Access – “minimum” standards (beyond SEC) for nominee disclosure</li> <li>• Board Turnover/Refreshment – Explore options and concepts for independent director refreshment</li> <li>• Interlocking Directors</li> </ul>
Compensation	<ul style="list-style-type: none"> <li>• Employee Compensation (Sullivan Principle) – Income Inequality for future develop following CalPERS symposium. Consideration should be given to retirement security and fair wages.</li> <li>• Share buybacks and executive compensation</li> <li>• Review of performance metrics linked to equity awards</li> <li>• Review stock option weakness and short-term focus</li> </ul>
Capital Allocation	<ul style="list-style-type: none"> <li>• Share buybacks and dividends</li> <li>• Request to address what is meant by “excessive debt leverage”.</li> </ul>
Environment and Climate Change	<ul style="list-style-type: none"> <li>• Water related issues</li> <li>• Clean Air</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 (make reference to “investors” where appropriate)</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 principle</li> </ul>
Vote Disclosure Language	<ul style="list-style-type: none"> <li>• Develop post-AGM proxy vote disclosure language</li> </ul>



# Revision Timeline

