

# Global Governance - Strategy Review

January 19, 2016

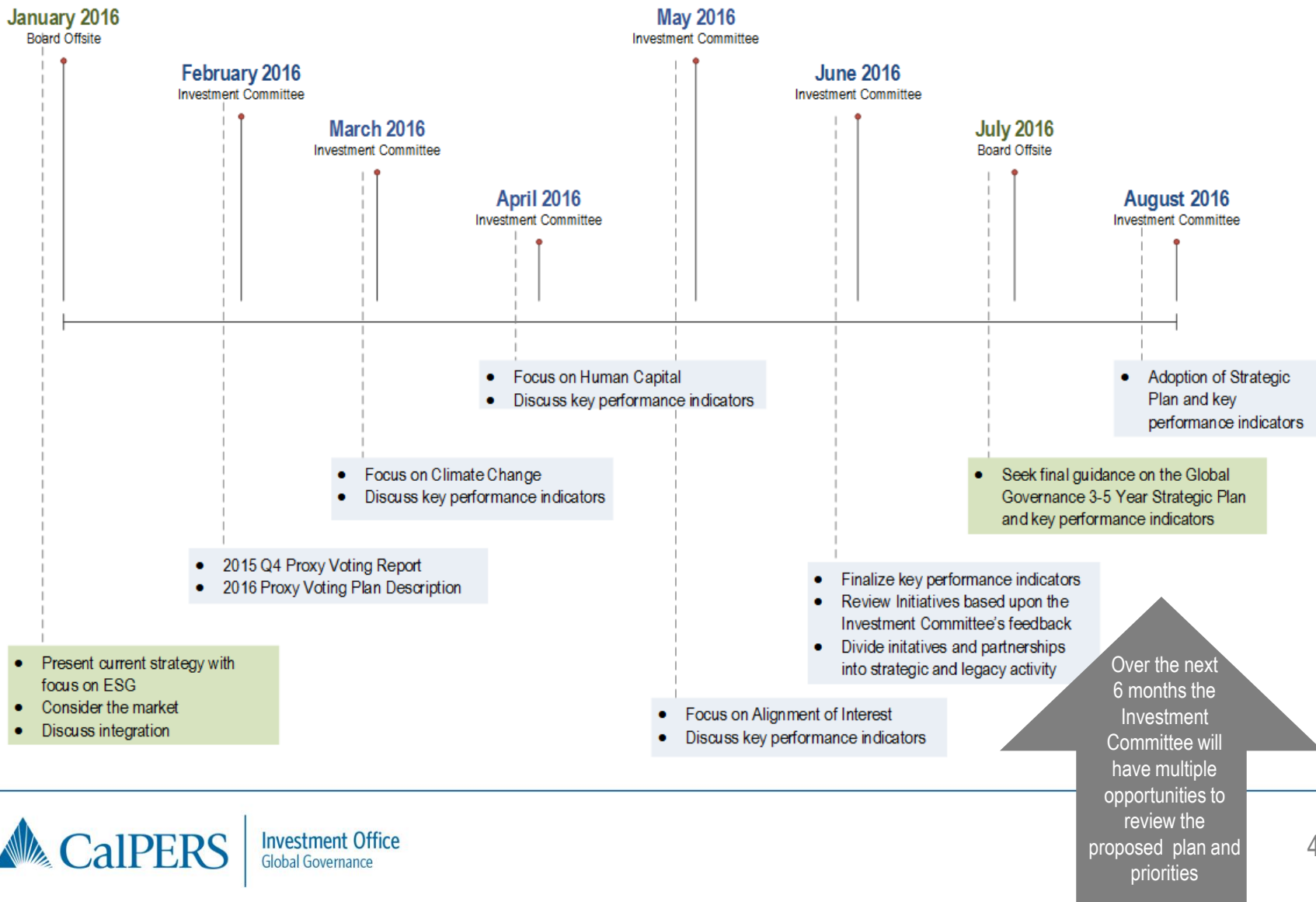
# Workshop Objectives

- Review the Strategic Direction for the Global Governance Program and Environmental, Social, and Governance (ESG) Integration
  - Present 2016 Proxy Voting Plan Overview
- Provide an industry context – looking across the market at what peers and other funds are doing on ESG integration
- Discuss the current ESG Integration strategy and how it is used in the investment process
- Wrap-up

# Introduction to Global Governance Program Review

- Review Timeline, Mission, Goals and Investment Beliefs that underpin the Global Governance Program
- Review the evolution of the Global Governance Program
- Examine the Global Governance Program's current strategy
- Consider 3-5 Year Strategic Initiatives to prepare a focused strategic medium term plan with flexibility to adapt to the developments in the market

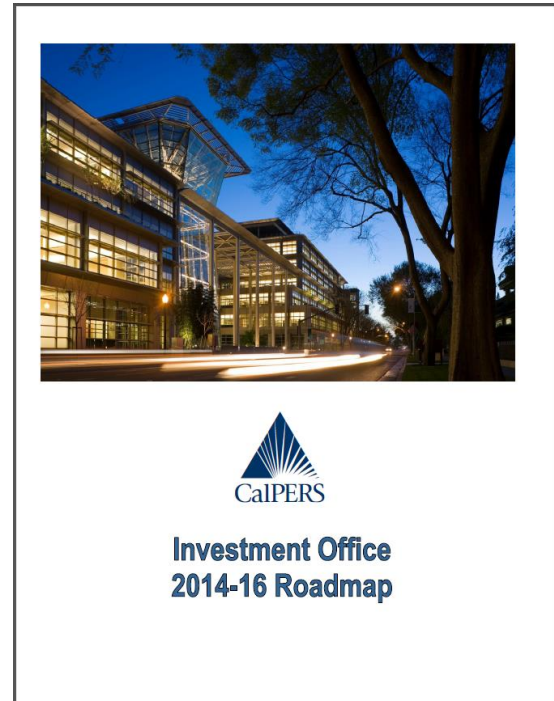
# Proposed Timeline for Developing a 3-5 Year Strategic Plan



# Mission & Goals for the Global Governance Program

The Program's mission and goals are set out in the Investment Office Roadmap:

“Ensure CalPERS acts as a principled and effective investor by advocating corporate governance and financial reform; overseeing the effective management of the three forms of capital: financial, physical and human; and, effectively engaging with portfolio companies and policy makers.”



Our Global Governance Program is focused on improving long-term risk-adjusted returns, guided by Investment Beliefs 2, 3, 4, and 9 in particular

# How do we implement the Investment Beliefs?

The Global Governance Program uses four channels

## Engagement

Effectively exercise ownership rights in a risk-aware manner

## Advocacy

Advocate for financial market law, regulations and policy that sustain the System

## Partnerships

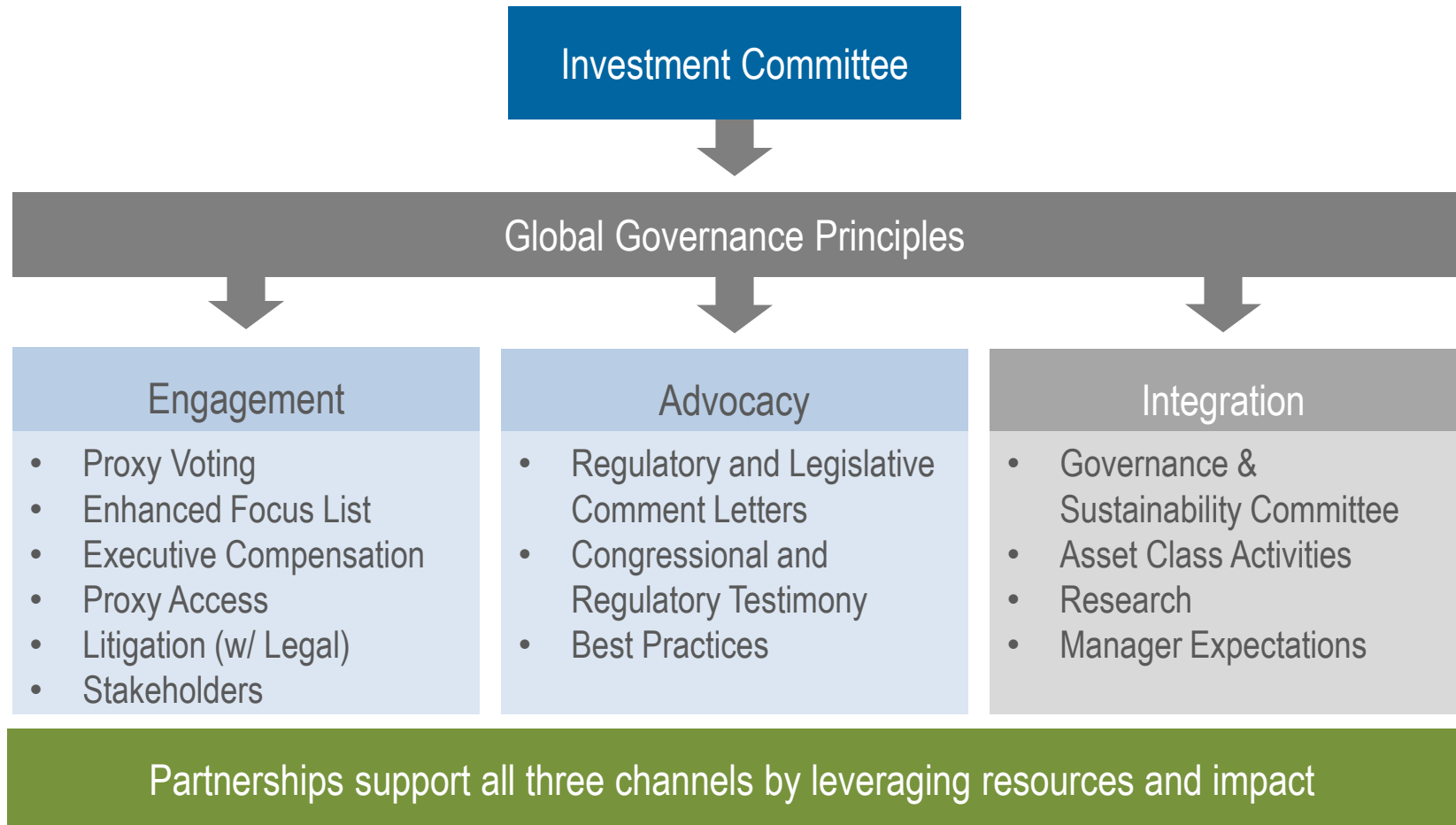
Work with fellow investors to leverage resources and increase impact

## Integration

Integrate ESG risk and opportunity considerations into the investment decision-making process

Work developed in partnership with the Asset Classes

# The Global Governance Principles frame our work



# The Evolution of the Global Governance Program

Past	Present
The Global Governance Program originated in the Legal Office and was later anchored to the Global Equity asset class	Anchored to the Total Fund
Corporate Governance	Global Governance – To capture Financial Markets & ESG (Environmental, Social and Governance)
Principles and Proxy Voting – Core Principles refer to domestic public equity holdings only	Total Fund Principles tailored for global markets
Corporate Engagement – Governance led	Integration of relevant financial, governance, environmental, social factors
Financial market reform priorities focused on U.S. capital markets	Advancing financial market reform priorities in global capital markets based on investment exposure
Mandates driven by Board and State law	Mandates driven by Board and State law
ESG Integration – 111 Scattered initiatives on Environmental, Social and Governance components	Goal is to be evidence based and grounded in economics.



# Reviewing & Exploring the Evidence on ESG

- 5 years ago, CalPERS commissioned a mapping exercise by Mercer of all ESG initiatives across the asset classes and found there were 111.
- This was presented and discussed at an [ESG Board Workshop in 2011](#), where staff proposed a new framework of economics – the three forms of capital: financial, physical and human
  - **Environmental** – Climate Change
  - **Social** – Human Capital
  - **Governance** – Alignment of Interest

“Though theory regarding the relation between risk and valuation is sound, academic research establishing a convincing causal relationship between sustainability factors and risk is sparse.”

“Based on the core economic principles we discuss and the available empirical evidence, we conclude that large institutions should tread carefully on adopting sweeping beliefs related to sustainability factors.”

## Sustainable Investment Research Initiative [Presentation to the Investment Committee](#) on 700 academic studies

June 17, 2013

### **Brad M. Barber**

Gallagher Professor of Finance  
UC Davis Graduate School of Management


### **Robert J. Jackson Jr.**

Associate Professor of Law and Milton Handler Fellow  
Columbia Law School

# Present Framework

Our present framework on ESG is driven by the Investment Beliefs.

- **Environmental**  
Climate Risk
- **Social**  
Human Capital
- **Governance**  
Alignment of Interest



We have four channels to drive these priorities

Engagement

Advocacy

Partnerships

Integration

# Present Workload of Global Governance Program & ESG Integration: Governance Issues

Engagement	Advocacy	Integration
<ul style="list-style-type: none"> <li>• Proxy Voting – Vote at 11,000 company meetings and 105,000 resolutions annually</li> <li>• Proxy Voting Engagements                             <ul style="list-style-type: none"> <li>– Over 1000 company engagements (via conference call, email, letter, and in-person meetings) on corporate governance related matters and proxy voting</li> </ul> </li> <li>• Shareholder Proposals                             <ul style="list-style-type: none"> <li>– Proxy Solicitations</li> <li>– Exempt SEC Filings – Shareowner Letters</li> </ul> </li> <li>• Proxy Access Campaign (98)</li> <li>• Majority Voting for Director Elections Campaign (45)</li> <li>• Advisory Vote on Executive Compensation                             <ul style="list-style-type: none"> <li>– CalPERS letter writing campaign to communicate company “against” votes (488)</li> </ul> </li> <li>• Enhanced Focus List – Japan (8)</li> </ul>	<ul style="list-style-type: none"> <li>• Legislative and Regulatory Guidelines                             <ul style="list-style-type: none"> <li>– Investor Independence; Corporate Accountability; Financial Markets; Diversity</li> </ul> </li> <li>• Commodities and Futures Trading Commission                             <ul style="list-style-type: none"> <li>– Derivatives; CFTC Funding</li> </ul> </li> <li>• Financial Accounting Standards Board                             <ul style="list-style-type: none"> <li>– Materiality</li> </ul> </li> <li>• International Accounting Standards Board                             <ul style="list-style-type: none"> <li>– Conceptual Framework; Agenda</li> </ul> </li> <li>• International Listing Standards (Hong Kong)</li> <li>• Litigation</li> <li>• Public Company Accounting Oversight Board                             <ul style="list-style-type: none"> <li>– Auditing Standards; Audit Partner Disclosure</li> </ul> </li> <li>• Securities and Exchange Commission                             <ul style="list-style-type: none"> <li>– Proxy Access; Universal Proxy Ballots; Shareholder Proposal Rights; Executive Compensation; Derivatives; Political Spending; SEC Funding</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Global Governance Principles</li> <li>• Alignment of Interest</li> </ul>
Partners to Support Work Plan		
<ul style="list-style-type: none"> <li>• Council of Institutional Investors</li> <li>• International Corporate Governance Network</li> <li>• International Finance Reporting Standards Council</li> </ul>	<ul style="list-style-type: none"> <li>• International Limited Partners Association (ILPA)</li> <li>• Pacific Pension Institute</li> <li>• Public Company Accounting Oversight Board (PCAOB)</li> </ul>	<ul style="list-style-type: none"> <li>• Sustainability Accounting Standards Board</li> <li>• The Credit Roundtable</li> </ul>

# Present Workload of Global Governance Program & ESG Integration: Environmental & Social Issues

Engagement	Advocacy	Integration
<ul style="list-style-type: none"> <li>• Board Quality and Diversity</li> <li>• Diverse Director Data Source (3D)</li> <li>• The Conference Board Diversity Events</li> <li>• CERES Carbon Asset Risk (45)</li> <li>• Climate Risk Reporting (Aiming for A - 3)</li> <li>• Human Capital Management Initiative- engagements with (6) companies on supply chain activities</li> <li>• Montreal Pledge engagement with (80) companies</li> <li>• Legislative Mandate                             <ul style="list-style-type: none"> <li>– Thermal Coal Cos (24)</li> <li>– Iran/Sudan (12), Northern Ireland and Holocaust (33)</li> </ul> </li> <li>• Thermal Coal Cos (85)</li> </ul>	<ul style="list-style-type: none"> <li>• Legislative and Regulatory Guidelines                             <ul style="list-style-type: none"> <li>– Sustainability</li> </ul> </li> <li>• Climate Change Policy Advocacy                             <ul style="list-style-type: none"> <li>– Global Investor Statement on Climate Change</li> <li>– “Pocantico Statement” on Climate Resilient Infrastructure</li> <li>– Paris Pledge for Action</li> <li>– Participation in United Nations climate events including: COP 21 (Paris), 2014 &amp; 2015 UN Climate Summits (New York)</li> <li>– Environmental Protection Agency Clean Power Plan review</li> <li>– Carbon Pricing Leadership Panel</li> </ul> </li> <li>• Securities and Exchange Commission                             <ul style="list-style-type: none"> <li>– Petition on diversity</li> </ul> </li> <li>• TIP – California Legislative Policy</li> <li>• United Nations Environmental Programme Finance Initiative                             <ul style="list-style-type: none"> <li>– Inquiry</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• CA Investments</li> <li>• Global Equity Portfolio – HSBC</li> <li>• Global Governance Principles – Principle development:                             <ul style="list-style-type: none"> <li>– Investor Rights; Compensation; Capital Allocation: Environmental and Climate; Total Fund; Human Capital Management</li> </ul> </li> <li>• Private Equity – Clean Tech</li> <li>• Real Assets Sustainability – Core Real Estate 20% Energy Reduction; Urban Land Institute Greenprint Center for Building Performance; Energy Efficiency Retrofits</li> <li>• Real Assets – GRESB Infrastructure; Clean Power Research; Greenprint; Affordable Housing Policy</li> <li>• Responsible Contractor Policy</li> <li>• TIP – Five Year Emerging, Transition, and Diverse Manager Programs; Diversity and Inclusion Steering Committee                             <ul style="list-style-type: none"> <li>– Corporate Boards; External Investment Managers; INVO Talent Management</li> </ul> </li> <li>• Total Fund – Asset Owner Disclosure Project; Carbon Footprinting; Montreal Pledge; Manager Expectations on ESG; Principles for Responsible Investment Reporting; ESG Data and Tools                             <ul style="list-style-type: none"> <li>– MSCI, Sustainalytics, Trucost, Bloomberg, SouthPole, Greenprint</li> </ul> </li> </ul>

## Partners to Support Work Plan

- |   |  |   |
|---|--|---|
| <ul style="list-style-type: none"> <li>• Ceres</li> <li>• Global Peer Exchange</li> </ul> | <ul style="list-style-type: none"> <li>• Principles for Responsible Investment</li> <li>• Sustainability Accounting Standards Board</li> </ul> | <ul style="list-style-type: none"> <li>• United Nations Environmental Programme – Finance Initiative</li> </ul> |
|---|--|---|

# Looking Forward | Focus is essential to being effective

The Global Governance Program has expanded in breadth and depth. Consistent with the Investment Office (INVO) 2020 Vision, we now need to build a strategy for the next 3-5 years.

## Year 1 – 2016 Global Governance Program Work Plan

- 6-month project to reaffirm ESG strategy
- Execute 2016 work plan

## Years 2-5

- Execute agreed upon ESG strategy
- Further integrate ESG into investment decision making
- Optimize organizational structure

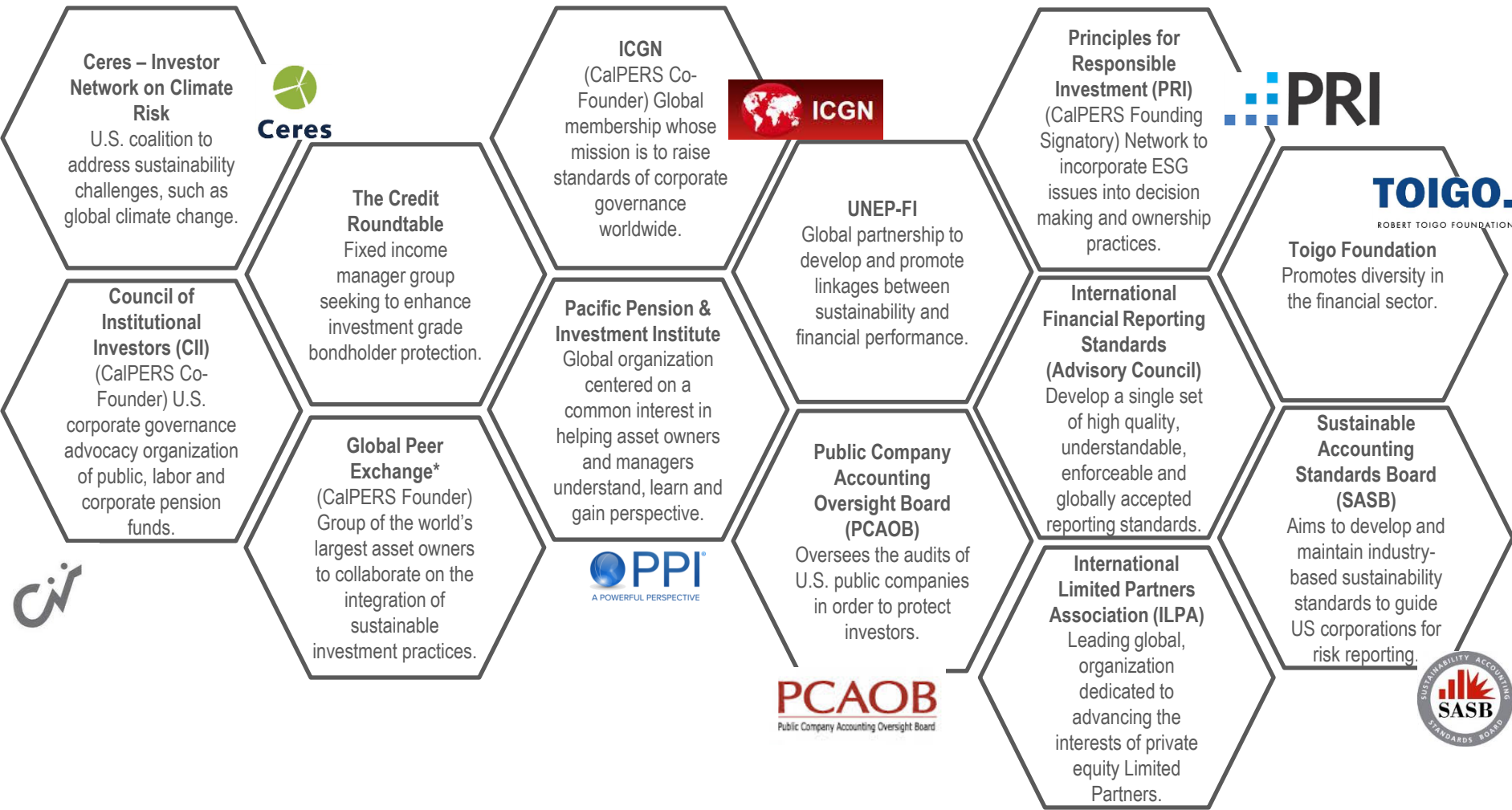
# 2016 Global Governance Program Overview

Engagement	Advocacy	Integration
<ul style="list-style-type: none"> <li>• Proxy Voting (11,000)</li> <li>• Proxy Voting Company Engagements (1,000)</li> <li>• Proxy Access Initiative (98)</li> <li>• Majority Vote Initiative(45)</li> <li>• Climate Risk Reporting Engagement (3)</li> <li>• Advisory Vote on Executive Compensation (Engagements 488)</li> <li>• Board Quality &amp; Diversity Engagements</li> <li>• Enhanced Focus List Strategy – Japan (8)</li> <li>• Carbon Asset Risk (45)</li> <li>• Human Capital Management (6)</li> <li>• Legislative Mandate – Northern Ireland/Holocaust (33)</li> <li>• Legislative Mandate – Thermal Coal (24-85)</li> <li>• Legislative Mandate – Sudan/Iran (12)</li> </ul>	<ul style="list-style-type: none"> <li>• Dodd-Frank Implementation -Credit Rating Agencies, Derivatives, Housing Finance Reform</li> <li>• Legislative and Policy Engagement Guidelines</li> <li>• Sustainability Accounting Standards Board</li> <li>• Financial Stability Board</li> <li>• Financial Accounting Standards Board</li> <li>• Public Company Accounting Oversight Board</li> <li>• International Accounting Standards Board</li> <li>• Securities and Exchange Commission</li> <li>• International Corporate Governance Network</li> </ul>	<ul style="list-style-type: none"> <li>• INVO Governance and Sustainability Subcommittee</li> <li>• Global Governance Principles Review</li> <li>• Carbon Footprint – Montreal Pledge</li> <li>• Exploration of Income Inequality</li> <li>• Pilot Manager Expectations on ESG</li> <li>• Sustainable Investment Research Initiative (SIRI)</li> <li>• UN PRI Reporting</li> <li>• 3<sup>rd</sup> Sustainable Investment and Operations Report</li> <li>• Diverse Director DataSource (3D)</li> </ul>

# 2016 Proxy Voting Plan

<p><b>Proxy Voting</b></p>	<p>Consistent with the CalPERS Global Governance Principles, staff will cast votes “for” or “against” management and shareowner proposals at approximately 11,000 company meetings. Common proposal types during 2016 will include:</p> <ul style="list-style-type: none"> <li>• Management: advisory vote on executive compensation (say on pay), advisory vote on golden parachutes, annual bonus plans, auditor ratification, director elections, employee stock purchase plans, exclusive forum provisions, elimination of cumulative voting, elimination of supermajority voting requirements, issuance of additional shares, long-term incentive plans, mergers &amp; acquisitions, and share recapitalization .</li> <li>• Shareowner: ability to call special meetings, board declassification, climate risk, climate change policy, equity holding requirements, independent board chairman, linking pay to sustainability, majority vote for director elections, political contributions, performance based compensation, proxy access, and sustainability reporting.</li> </ul>
<p><b>CalPERS Shareowner Proposal Activity</b></p>	<p>File and/or co-file shareowner proposals on the following topics:</p> <ul style="list-style-type: none"> <li>• Proxy Access</li> <li>• Majority Vote for Director Elections</li> <li>• Climate Risk Reporting</li> </ul> <p>At companies where staff is unable to successfully negotiate implementation, staff will run a proxy solicitation campaign. This includes engagement of top shareowners, filing shareowner letters with the SEC, and hiring a proxy solicitor.</p>
<p><b>Working with Partners</b></p>	<p>Proxy Access – New York City Funds Board Accountability Project</p> <ul style="list-style-type: none"> <li>• Assist NYC Funds and other investors by engaging companies surrounding the adoption of proxy access.</li> <li>• Efforts to support may include engaging investors and proxy advisory firms, coordinating shareowner solicitation campaigns, and annual general meeting attendance.</li> </ul>

# Partnerships





# 2016 Global Governance Program Work Plan | Partnerships

Annual Meeting	Date	Location
PRI ESG Summit at SuperReturn	February 22-25	Berlin, Germany
PPI Winter Roundtable	February 24-26	Rancho Palos Verdes, CA
ICGN Frankfurt Conference	March 8-9	Frankfurt, Germany
PRI Geneva Summit on Sustainable Finance	March 22	Geneva, Switzerland
CII Spring Conference	March 21-23	Washington, D.C.
The Credit Roundtable Spring Conference	April 12	Washington, D.C.
CERES Conference 2016	May 4-5	Boston, MA
Toigo 15 <sup>th</sup> Annual Gala	June 9	New York, NY
ICGN San Francisco Conference	June 27-29	San Francisco, CA
IFRS Conference	June 30 – July 1	Zurich, Switzerland
PPI Summer Roundtable	July 27-29	Cambridge, MA
PRI InPerson 2016	September 6-8	Singapore
IFRS World Standard-Setters Meeting	September 26-27	London, UK
CII Fall Conference	September 28-30	Chicago, IL
PPI Asia Roundtable	October 26-28	Kowloon, Hong Kong
The Credit Roundtable Fall Meeting	November	Chicago, IL
ILPA General Partner Summit	November	New York City, NY
ICGN London Conference	December 7	London, UK

Attendance,  
Preparation,  
Talking Points for  
Annual Meetings

# Proposed 3-5 Year Strategy

- Identify and optimize legacy and partnership activities
- Examine and execute on strategic core activities  
(e.g. Responsible Contractor Policy, Enhanced Focus List)
- Focus discretionary capacity on Strategic Priorities

# Discretionary Capacity – Recommended Strategic Priorities

➔ Focus is essential to being effective

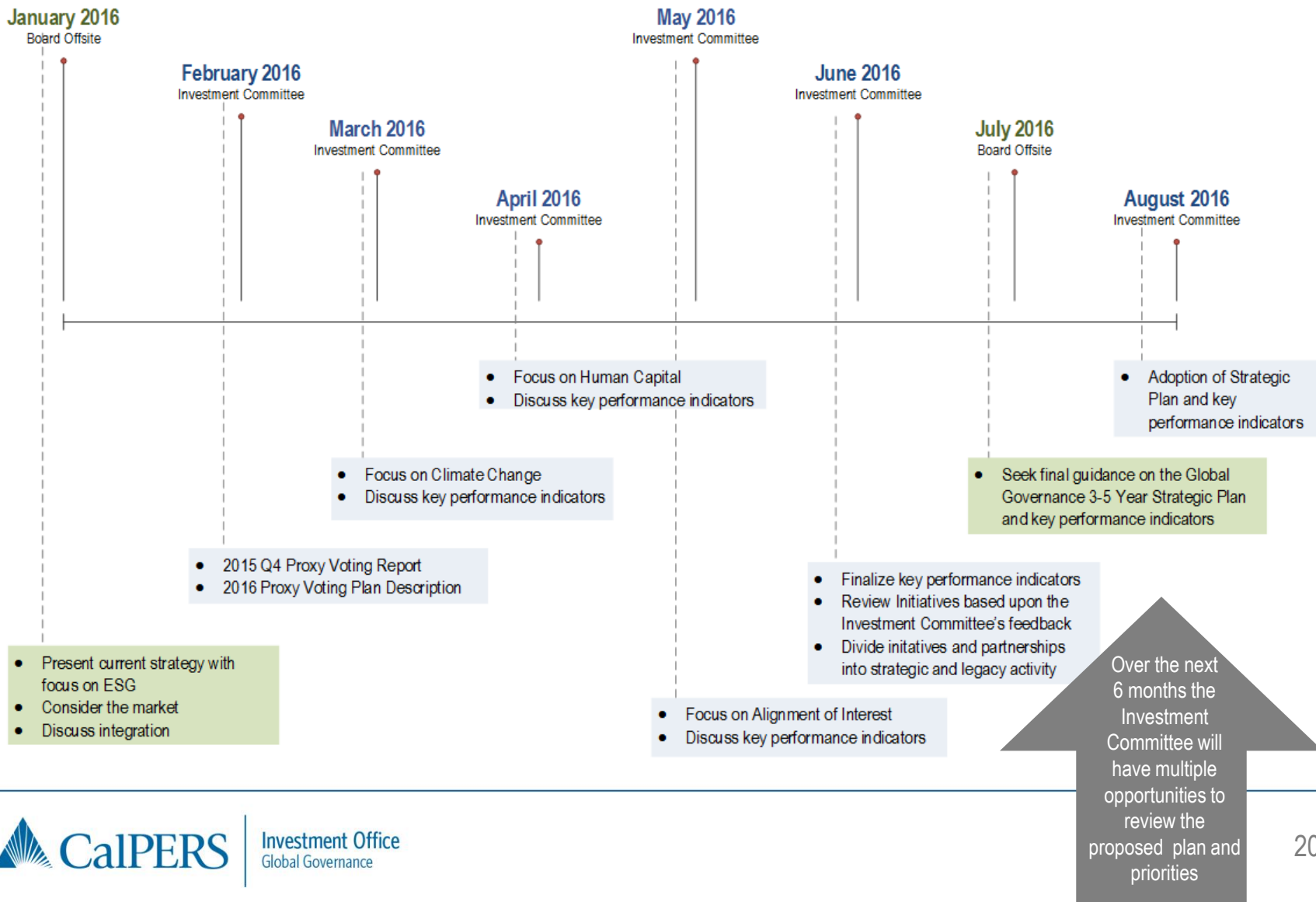
➔ Maintain these three themes

Climate Change	Human Capital	Alignment of Interest
<ul style="list-style-type: none"><li>• Data reporting issues – Climate Change</li><li>• Refresh carbon asset review and climate change engagement strategy around 80 Montreal Pledge companies</li></ul>	<ul style="list-style-type: none"><li>• Board Diversity</li><li>• Supply Chain Activities</li></ul>	<ul style="list-style-type: none"><li>• Board accountability – Proxy Access, Majority Vote for Director Elections</li><li>• Corporate Reporting and Accounting</li><li>• Fee and performance transparency</li><li>• Explore, with Legal Office, potential ESG related actions.</li></ul>

**Review Partnerships and select those which best leverage resources and impact**

The following slide reflects the timeline for discussion of these three themes.

# Proposed Timeline for Developing a 3-5 Year Strategic Plan



## Supplemental Reading

- Towards Sustainable Investment & Operations: Making Progress
  - CalPERS 2014 Report
- Investment Beliefs Implementation Review Findings
  - September 2015 IC Agenda Item 6a
- Consultant Reports
  - The Pursuit of Sustainable Returns, Mercer
  - We Need a Bigger Boat, Towers Watson