CalPERS

Investment Committee
Agenda Item 6b

March 19, 2018

Item Name: ESG Strategic Plan Update

Program: Sustainable Investments

Item Type: Information

Executive Summary

This agenda item provides an update on the CalPERS Environmental, Social and Governance (ESG) 5-Year Strategic Plan (Plan), including progress on underlying strategic priorities, core workload initiatives and associated key performance indicators.

Strategic Plan

This agenda item supports the CalPERS 2017-22 Strategic Plan goal of Fund Sustainability, and the 2017-18 Business Plan goals of Investment Beliefs and ESG Risk Integration. Specifically, the Plan seeks to integrate ESG risk and opportunity considerations into investment processes and decisions, thereby improving the long-term sustainability of the fund.

Investment Beliefs

This item supports the following CalPERS' Investment Beliefs:

- Investment Belief 2: regarding the responsibility and advantage of a long-term investment horizon and the sub-beliefs which require that CalPERS encourage companies and external managers to consider the long-term impact of their actions.
- Investment Belief 3: CalPERS' investment decisions may reflect wider stakeholder views, provided they are consistent with its fiduciary duty to members and beneficiaries
- Investment Belief 4: Long-term value creation requires effective management of three forms of capital: financial, physical and human.
- Investment Belief 9: Risk to CalPERS is multi-faceted and not fully captured through measures such as volatility or tracking error.

Background

In 2016, the Investment Committee (Committee) and Investment Office Staff (Staff) engaged in a series of discussions and monthly reports on CalPERS' climate change, human capital and board quality strategies for engagement, advocacy and integration. The iterative process resulted in development of the Plan, which is the first of its kind amongst institutional investors like CalPERS. The Plan, guided by CalPERS' Investment Beliefs and the CalPERS Governance and Sustainability Principles (Principles), identifies six strategic priorities, and core workload initiatives focused on ESG issues which cross the Total Fund and impact risk and return. Each initiative has a clearly defined objective, key performance indicators to serve as measures of success, milestones and a timeline.

In August 2017, the Committee approved the Plan and associated ESG Strategy Timeline which reflected long-term ESG integration effort, as outlined in Attachment A. With more than half of the six strategic initiatives having 20 or 30 year targets, CalPERS models Investment Belief 2 which states a “long time investment horizon is a responsibility and an advantage” which requires consideration of “the impact of [our] actions on future generations of members and taxpayers.”

To complete the priorities within the Plan, Staff utilize the three channels of advocacy, engagement, and integration, all of which are supported by foundational relationships with strategic partners.

Analysis
Since the 2017 Plan approval, Staff focused efforts on creating detailed work plans, meeting the stated 2017-18 deliverables identified on the ESG Strategy Timeline, and driving progress on long-term key performance indicators. Accomplishments within each strategic priority are detailed below.

Data and Corporate Reporting Standards
CalPERS participates in domestic and international policy development to advance the interests of long-term investors and encourage policymakers to take actions that instill trust and confidence in global financial markets. Advocating for public policies and enhanced disclosures with increased transparency of ESG risk and considerations help promote fair, orderly, and effectively regulated capital markets. With this in mind, CalPERS is committed to the development of comparable and reliable disclosure standards for corporate reporting of ESG considerations.

CalPERS, as representative of the Council of Institutional Investors (CII), actively participates on the International Financial Reporting Standards (IFRS) Council, an advisory body to the International Accounting Standards Board (IASB). IFRS global accounting standards “bring transparency by enhancing the international comparability and quality of financial information, enabling investors and other market participants to make informed decisions.”[1] Currently, 166 jurisdictions have chosen application of these standards[2].

The IFRS Council includes “investors, financial analysts and other users of financial statements, as well as preparers, academics, auditors, regulators, professional accounting bodies and standard-setters”.[3] Staff attend semi-annual meetings to participate in setting priorities and develop strategy related to: working with National Standard-setters; understanding and addressing effects of technology on financial reporting and standard-setting; and engagements with academics. In 2017, Staff recommended and the Council moved to endorse the findings of “wider reporting” on their work plan. The review of wider reporting provides a comprehensive assessment of ESG reporting and the trend towards integrating this into financial reporting. Staff also met with representatives from IASB to share our view of the materiality of ESG disclosure.

Domestically, Staff has been actively engaged on improving data and corporate reporting standards by weighing in on the Financial Accounting Standards Board’s conceptual framework to advocate for integrated reporting, to align discussion with CalPERS’ view and through participation on the Financial Accounting Standards Advisory Council. Staff also participates on the Securities and Exchange Commission (SEC) Investor Advisory Group, which has provided

[1] Source: International Financial Reporting Standards website
[2] Source: International Financial Reporting Standards use by jurisdiction
[3] Source: International Financial Reporting Standards Advisory Council

opportunity to discuss the Human Capital Management (HCM) Coalition petition for rulemaking pursuant to Rule 192(a) of the Commission's Rules of Practice. The HCM petition was submitted by the HCM Coalition, of which CalPERS is a founding member. Together, with other institutional investors with $2.8 trillion in assets, the Coalition requested the Commission adopt new rules, or amend existing rules, to require companies to disclose information about their human capital management policies, practices and performance.

In July 2017, the Financial Stability Board issued final recommendations of its Task Force on Climate-Related Financial Disclosures (TCFD). The TCFD framework defines voluntary climate-related financial disclosures for use by a broad range of audiences such as companies, asset managers and asset owners. Through webinars, written testimony and working group participation, CalPERS supported the development of TCFD, expansion of the Principles for Responsible Investment's (PRI) annual reporting requirements to incorporate the TCFD framework recommendations for asset classes.

CalPERS will be requesting the Climate Action 100+ companies to provide disclosures in alignment with TCFD recommendations. Internally, we have committed as an asset owner to report in line with the same recommendations, which include core elements of:

- Governance: Organization's governance around climate-related risks and opportunities
- Strategy: Actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning
- Risk Management: The processes used by the organization to identify, assess, and manage climate-related risks
- Metrics and Targets: The metrics and targets used to assess and manage relevant climate-related risks and opportunities

As a member of the Sustainability Accounting Standards Board (SASB) Investor Advisory Group, CalPERS is committed to the development of comparable and reliable disclosure standards for corporate reporting of ESG considerations with the previously mentioned TCFD standards. Through this strategic partnership, staff engaged in conversations and provided comments encouraging SASB on further alignment with TCFD recommendations. As a prominent potential standard-setter, SASB received comments intended to raise HCM and corporate governance reporting standards in line with our Principles. In a similar vein, we recommend revisions to our Principles to address company disclosures on Environmental Risks and Opportunities utilizing the TCFD framework of Governance, Strategy, Risk Management, and Metrics and Targets. Please see Committee agenda item 7a for recommended revisions.

The Global Real Estate Sustainability Benchmark (GRESB) is an investor-driven organization that is transforming the way we assess environmental, social and governance performance of real assets globally including real estate portfolios, real estate debt providers and infrastructure assets. Staff participate on the GRESB Advisory Boards for infrastructure and real estate and CalPERS began reporting into GRESB in 2016. Using this tool allows CalPERS Investment Office to review ESG data, along with related performance metrics, for assets managed by external managers. The benchmark is being used to understand how CalPERS' managers and assets compare to the industry and to emerging ESG related performance metrics across global real estate and infrastructure portfolios.

Engage UN PRI Montreal Pledge Companies (to be renamed Climate Action 100+)
As a global investor, CalPERS' portfolio and assets are exposed to the risks of climate change, such as extreme weather events (hurricanes and storms), drought and the wildfires which can result, and sea level rise. Mitigation strategies for this investment risk include reduction of greenhouse gas emissions to limit the rise in the global warming. In order to drive progress on this strategy, Staff has set the objective of engaging 80 Montreal Pledge companies to establish a carbon reduction target consistent with the Paris COP 21, an international environmental agreement on climate change.

The Montreal Pledge was launched by the UN Principles for Responsible Investment (UN PRI) in 2014, with CalPERS as the first U.S. signatory. By signing the Pledge, investors committed to measure and publicly disclose the carbon footprint of their investment portfolios annually. Staff analysis of our global equity portfolio's carbon footprint found that of the 10,000+ companies within the portfolio, only 80 companies are responsible for 50% of the greenhouse gas emissions which contribute to global warming.

In 2017, Staff were the first US public pension plan to disclose the fixed income carbon footprint, with a presentation to the Committee on the corporate credit portfolio's carbon intensity relative to the benchmark index. Staff's efforts will focus next on mapping the carbon footprint of the Real Assets portfolio.

The analysis of our global equity carbon footprint has been shared with other investors, initially at a meeting hosted by the French mission to the United Nations. Asset owners, fund managers, researchers, and experts were invited to review Staff analysis, and consider collaboration on engagement on a global focus list of companies. Staff then convened regional investor networks from North America, Europe, Asia and Australia through the Global Investor Coalition on Climate Change and UN PRI, which spent a year reviewing methodology, data sources, and developing a global engagement agenda. The agenda was to be constructive, confidential, and focused on business strategy that ensured companies received support of their long-term owners in developing new strategies which are financially viable and meet the goals of limiting global warming. The result was the creation of the Climate Action 100+ (CA100+), a coalition currently with 230 investors representing $28+ Trillion in assets.

CA100+ is a five-year initiative which seeks to engage with 100 of the world's largest corporate greenhouse gas emitters to curb emissions, strengthen related financial disclosures, and improve governance on climate change. The emission trajectory of these top 100 emitters – or Systemically Important Carbon Emitters – is critical to whether the global economy meets the 2 degrees target set out in the Paris Agreement. The "+" in CA100+ represents an additional list of companies which will be added to the list next year. These are firms which investors consider important to partner with as they bear climate-related financial risks.

In line with the Paris COP 21, the goal of CA100+ is to partner with companies to bring their business strategies in line with the goal of keeping global warming to less than 2 degrees Celsius. Companies selected for engagement were identified by taking into consideration CDP data of their combined direct and indirect Scope 1, 2, and 3 emissions, as explained below.

- Scope 1: All direct greenhouse gas emissions
- Scope 2: Indirect greenhouse gas emissions related to electricity purchased heat or steam from another company

- Scope 3: Other indirect emissions, such as the extraction and production of purchased materials and fuels, transport-related activities in vehicles not owned or controlled by the firm, outsourced activities, waste disposal, emissions not covered in Scope 2, etc.

In September 2017, the initiative was presented at PRI In Person in Berlin to call for investor support. In December 2017, CA100+ was publicly launched at the One Planet Summit in Paris, with CalPERS selected to represent the coalition. This initiative expands the UN PRI Montreal Pledge engagement as it will enable CalPERS to not only engage top carbon emitters in our portfolio, but increase our efficacy by leveraging partnerships with peer funds and investors networks engaged in CA100+ efforts. Staff has volunteered to serve as lead investor on engagement of both US and International markets' CA100+ companies and sits on the steering group which coordinates the initiative globally. Staff will maintain focus on partnering with 20 per year, as the key performance indicator states, through collaboration with our peers and progress will be reported annually.

Internally, Staff initiated a project to identify and understand potential risk areas relative to physical climate risk, specifically sea-level risk, extreme temperature change and extreme precipitation variability for real assets and global equity. Details will be reported at a future meeting.

Diversity and Inclusion
When boards lack diverse views, they may face many challenges and limitations which can impact performance. As fiduciaries to CalPERS, corporate boards are accountable for overseeing the use of CalPERS' capital. For this reason, it is important the boards represent a diverse mix of characteristics, experiences and competencies to ensure effective board leadership.

With the objective of ensuring all companies in which CalPERS invests have a dimension of diversity on the board, Staff engaged over 500 US companies in the Russell 3000 Index regarding lack of diversity on their boards. These companies were selected based on available data from Institutional Shareholder Services, which highlighted the lack of women in board seats. Staff drafted and sent letters to 504 companies requesting they develop and disclose corporate board diversity policies and implementation plans to address lack of diversity. Staff also developed a framework for addressing a company's lack of response to these engagement activities. The framework was presented for approval to the GSS in December 2017.

In efforts to continually promote and improve board diversity, Staff continue to seek connection of qualified candidates with diverse backgrounds with companies in need of their skills, perspective, and talents. This is fostered through the promotion and use of the Diverse Director DataSource (3D), which was created following a series of roundtables, co-hosted by CalPERS and CalSTRS, with over 150 individuals representing companies, investors, search firms, diversity networks and academics. These roundtables served to identify needs, review existing resources and generate ideas around the potential for 3D.

In 2017, ownership of 3D was transferred to Equilar's Diversity Network with a suite of other resources allowing candidates to connect from a range of other diversity organizations accessible to companies looking for candidates. To date, 3D houses over 400 candidates across a range of industries and backgrounds. A quarter of these candidates have board certification training and international experience. Since the launch of the Equilar Diversity Network, over 150 public companies have signed up to search for diverse candidates. Eleven candidates within 3D were appointed to boards of leading companies such as Shell, Orion, Teletech and AeroCentury.

Over the last quarter Staff have attended Equilar's Diversity Network events to expand the range of candidates who bring racial and ethnic diversity to 3D. Staff also are developing search tools with Equilar and identifying other enhancements to 3D which will help companies search on important new dimensions to board quality, such as climate change competence, human capital management and cyber security expertise. CalPERS' advocacy on diversity has included speaking at conferences, webinars, and giving testimony to State legislative hearings.

Internally, recent organizational changes included the movement of the resources and responsibilities related to the Responsible Contractor Policy Program and Diversity and Inclusion (D&I) into the Sustainable Investments program. For D&I, this consolidation of responsibilities integrates management and reporting of the three work streams focused on diversity of: Corporate Boards, External Managers, and INVO Talent Management, as outlined in the Investment Office D&I 2020 Plan. The Investment Office provides an annual update to its D&I efforts in the "CalPERS Commitment to Diversity" report and an item to the Finance and Administration Subcommittee both of which were most recently provided to the CalPERS Board February 2017. Over the next year, Staff will be planning important Diversity and Inclusion events, such as the Emerging, Transition, and Diverse Manager Day and the CalPERS and CalSTRS Diversity Forum.

<u>*Manager Expectations*</u>
Acknowledging sustainability impacts all areas of the portfolio, CalPERS seeks to ensure sustainable investment considerations are appropriately included throughout the life cycle of investments by internal and external managers. The Plan specifically seeks to integrate ESG factors into investment processes and decisions by internal and external managers. These processes include selection, contracting, monitoring and management.

In 2016, each asset class developed and piloted a set of Sustainable Investment Practice Guidelines (SIPG) which reflect their particular requirements. The SIPGs are intended to evolve and adapt as industry best practices emerge, and as such were updated in 2017. They are now available and posted to CalPERS' website to ensure timely availability for interested parties.

Staff integrated ESG factors into their Annual Program Review, with each asset class delivering such material to the Committee throughout 2017. Highlights include:

- Global Fixed Income: Completed Carbon Footprint of Internal Corporate Fixed Income portfolios; including Governance factors across credit portfolio
- Global Equity: Completed the review of ESG strategies
- Real Assets: Launched the Energy Optimization Initiative to research strategies to optimize energy consumption of the real estate portfolio
- Private Equity: Staff focused on broader adoption of the ILPA Fee and Profit Sharing template

Staff continue to research industry best practices, perform outreach to external managers to understand how the SIPGs are being utilized, refine internal processes, and develop a framework to measure and report on the percentage of internal and external managers with policies and procedures integrating ESG into investment processes and decisions. This measure has been approved as a Strategic Measure within the CalPERS 2017-2022 Strategic Plan specific to Fund Sustainability.

Research
CalPERS believes it is important to understand how sustainability factors impact investment risk and return while grounding our approach in economic data. For this reason, CalPERS created Sustainable Investments Research Initiative (SIRI), which is designed to promote innovative thought leadership that would advance and inform our understanding of sustainability factors and the impact they may have on companies, markets, and investment. The first review led by UC Davis and Columbia University was presented to the Committee in 2014 with 800 academic papers assembled in a searchable database.

In 2017, Staff again partnered with UC Davis to conduct a refresh of the SIRI library. UC Davis was asked to pay particular attention to papers relevant to the following issues:

- Environmental: Climate Change – including issues related to resource scarcity, water stress, carbon emissions, energy efficiency, clean technology, and renewable energy
- Social: Human Capital – including issues related to income inequality, exploitative labor practices, health and safety, responsible contracting and diversity
- Governance: Alignment of interest through corporate governance – including issues such as shareowner rights, executive compensation, fund manager terms and conditions and investor protection

The refreshed database identified over 1,000 new papers which have been uploaded into the SIRI database on CalPERS' website. The SIRI database now includes the following number of studies per topic area:

- Environmental: 591 studies
- Social: 559 studies
- Governance: 1290 studies

In December 2017, Staff participated in the UC Davis Graduate School of Management Finance Symposium "Capitol / Labor Markets in the Age of Inequality" where six academic papers on income inequality were presented and reviewed. These papers were among those identified in the SIRI refresh and are now accessible and searchable on the CalPERS' website.

As a key performance indicator for the Research strategic priority, in 2017 Staff embarked on a deep dive into equity strategies that integrate ESG themes and research while in accordance with CalPERS' investment objectives. A cross-asset class team focused on broad-based, systematic portfolios that thoughtfully integrate ESG analysis and investment considerations, which can be implemented internally. The team analyzed and prioritized the strategy submissions, and presented a summary of the analysis and an investment recommendation. The recommendation was vetted by the Global Equity governance bodies, and approved for implementation, which is currently in progress.

Private Equity Fee and Profit Sharing Transparency
Alignment of interest is vital across the CalPERS portfolio and is an important governance issue for fiduciaries. In collaboration with Institutional Limited Partners Association (ILPA), CalPERS developed the ILPA Fee Reporting Template that has detailed information on fees charged to portfolio companies. This template allows CalPERS to continue to be as transparent as possible when it comes to reporting the fees that are paid to external managers.

Data collection began in 2016 and since that time, the General Partners submit data on a timely basis. The Strategic Fund Template submission rate is stabilized at approximately 80 percent, and overall submission rate is approximately 70 percent. Staff continue to engage Limited Partners and General Partners to understand hindrances to full adoption of the ILPA Fee Template, encourage feedback to be provided to ILPA in order to make the template as relevant as possible, and develop metrics for reporting.

Ad Hoc Stakeholder Requests
Over the last year, Staff received and prioritized a wide range of stakeholder requests according to the framework outlined in Investment Belief 3. Staff's response to such requests has included: collection and analysis of relevant materials; convening multi stakeholder dialogue to further understand the issues; and, facilitation of responses in alignment with our Investment Beliefs and Principles.

These responses may include crafting and responding to investor statements, proxy voting and shareowner proposals, working through partnerships with fellow investors and networks, and proposing revisions to the Principles to provide clarification or ensure relevant issues are included. Please refer to Committee agenda item 6c for proposed Principles' edits, some of which are in response to a number of this year's stakeholder requests.

This past year, some of the topics Staff have initiated research on or responses to include:

- Dakota Access Pipeline ("DAPL") Indigenous Peoples' Rights
- Use of antibiotics in livestock feed
- Opioid Epidemic
- Deforestation
- Chemicals
- Supply chain

At the February 2017 Committee meeting, over 50 individuals requested to make a public comment regarding their concerns with CalPERS' investment in companies involved in DAPL. Following Board direction, Staff engaged with Energy Transfers Partners (ETP) as the DAPL operator and owner, investors, banks providing project finance, the Equator Principles Association which provides a risk framework for use by financial institutions when considering approval of project finance, and other stakeholders including the Standing Rock Sioux Tribe and Labor. CalPERS has requested ETP respond to the Foley Hoag report and also engaged the Environmental Protection Agency (EPA) to request a review. The Foley Hoag report[4] was commissioned by the lead banks and utilized DAPL as a case study to consider international industry good practices (IIPG) for community engagement in the development of pipelines, specifically focused on indigenous peoples' rights. The final report included general industry good practice to:

- Assist companies building future pipelines in the US in incorporating the IIPG
- Potentially help banks in evaluating financing of those projects

In addition, Staff proposed revisions to CalPERS' Principles including language specific to Indigenous Peoples' Rights and free, prior and informed consent. Assembly Bill 20 requires CalPERS to report to the Legislature regarding its engagement activities and outcomes surrounding the DAPL situation. Please refer to Committee agenda item 4e for a more comprehensive overview of CalPERS efforts related to DAPL.

[4] Foley Hoag Summary Report

The use of antibiotics in livestock feed, the opioid epidemic, and chemical use such as pesticides are all topics which Staff have engaged with stakeholders, considered when proxy voting, and addressed through the product safety language enhancement within the Principles.

In further regard to the opioid epidemic, Staff is engaging firms with revenue impacted by the crisis and is reviewing upcoming shareowner proposals to identify opportunities to improve corporate governance.

Partnerships

Partnerships are critical to CalPERS' ESG strategy as they allow us to share experience, pool resources and scale influence. As a member of global investment networks, such as the Ceres Investor Network on Climate Risk and Sustainability, and PRI, CalPERS has engaged and collaborated with companies on understanding carbon, water, and supply chain risks and opportunities. Through such participations and alignment of interests, we are helping to drive the overall success of CalPERS.

Partnerships with notable recent successes include the regional partner organizations, along with PRI, collaborated as the Global Investor Coalition on Climate Change to design and develop CA100+. Organizations, of which CalPERS is a member, include:

- Asia, Investor Group on Climate Change
- North America, Ceres
- Australia/New Zealand, Investor Group on Climate Change
- Europe, Institutional Investors Group on Climate Change
- Principles for Responsible Investors, Global

The Council for Institutional Investors has been a critical resource in the analysis of one-share one-vote structure, providing research and advice on recent Initial Public Offerings (IPOs) in the United States. This led to a highly effective engagement with index providers to offer products reflecting the one-share one-vote principle.

Staff are developing a framework to assess these strategic partnerships to ensure continued alignment of interests, value-add to the portfolio and adequate Staff across the Investment Office is dedicated to these relationships. Staff will report on the progress of this framework at a future Committee meeting.

Sustainability Report

In 2015, Staff presented the second report on CalPERS' sustainability work, highlighting the progress towards, among other items, the launch of the Sustainable Investment Research Initiative (SIRI) and the development of a Cross Asset Class Team on Sustainable Investments. In support of our core beliefs of Openness, Transparency, and Accountability, and integrated sustainability reporting, Staff are collaborating with the Public Affairs and Operational Support Services Divisions to build a more comprehensive Sustainability Report which addresses efforts on integrating ESG into CalPERS' investments and operations.

Staff intend to provide our stakeholders with information on the Plan and associated work streams, the formation of a strengthened governance architecture of Investment Beliefs, CalPERS Total Fund Investment Policy which includes Governance and Sustainability Principles, and the newly-formed Governance and Sustainability Subcommittee (GSS) and related working groups, along with the internal operational improvements throughout the Enterprise. The report is anticipated to be available online by fiscal year-end.

Treasurer's Request- Assault Weapons

Following recent tragic events involving assault weapons such as the Las Vegas massacre, in October 2017 the Committee Chair received a letter from the California State Treasurer John Chiang, requesting CalPERS to consider the following:

- Its investments in companies that retail or wholesale assault weapons banned for sale to the public in California.
- Its investments in companies that manufacture or sell accessories that can accelerate a semi-automatic rifle's rate of fire.

CalPERS' Total Fund Policy, Section 7, sets forth CalPERS' policy on divestment stating the following:

- CalPERS' policy for responding to external or internal initiatives to cause CalPERS to sell investments or refrain from making additional investments (divesting) for the purpose of achieving certain goals that do not appear to be primarily investment-related, such as promoting social justice (divestment initiatives). Typically, divestment initiatives focus on companies that do business in a specific practices deemed undesirable by federal and state law.
- CalPERS' investment in a company does not necessarily signify that it approves of the company's policies, products, or actions. CalPERS, nevertheless, wants companies in which it invests to meet high corporate governance, ethical, and social standards of conduct. The Investment Committee believes that this generally will promote superior long-term investment performance.
- CalPERS' Board and its staff have fiduciary duties of loyalty and prudence, pursuant to the California Constitution, Article XVI, Section 17, and Governance Code Section 20151. These fiduciary obligations preclude CalPERS from sacrificing investment performance for the purpose of achieving goals that do not directly relate to CalPERS operations or benefits. Divesting appears to almost invariably harm investment performance, such as by causing transaction costs (e.g. the cost of selling assets and reinvesting the proceeds) and compromising investment strategies.
- There appears to be considerable evidence that divesting is an ineffective strategy for achieving social or political goals, since the usual consequence is often a mere transfer of ownership of divested assets from one investor to another. Investor that divest lost their ability as shareowners to influence the company to act responsibly.
- CalPERS divestment policy, therefore, generally prohibits divesting in response to divestment initiatives, but permits CalPERS to use constructive engagement, where consistent with fiduciary duties, to help divestment initiatives achieve their goals.
- As reflected by CalPERS Investment Belief 3, CalPERS will use its prioritization framework in considering whether to engage on issues raised by stakeholders.

Under this policy, staff responded to the Treasurer's request with the following:

1. Identified portfolio companies potentially applicable to the Treasurer's request.
2. Sent written correspondence in November 2017, to five portfolio companies requesting:

   "If assault weapons and accessories are indeed available for sale in your stores, we ask that the Board review the reputational and associated risks which this poses to your company in the wake of recent tragedies. We ask that you review the revenues which are earned from the sale of these weapons and accessories, and consider removing them from being sold to the public in your stores. We appreciate there are various federal and state requirements attendant upon purchase of firearms. However, our concern is around the Board's responsibilities to address risks to its reputation and brand."

Engagement results to date are the following:

1. Big 5 Sporting Goods confirmed on March 2, 2018, via conference call, the company has completed the following:
    - In 2016, the company decided to discontinue the sale of assault weapons and ensured there is no current inventory across the retail chain.
    - The company has never carried accessories that can increase the rate of fire or high capacity magazines.
    - The company does not sell hand guns to the public.
    - The company's revenue derived from firearms is approximately 1.5% of sales.
2. Dick's Sporting Goods contacted CalPERS on February 28, 2018, to highlight their announcement that they are committed to the following:
    - No longer selling assault-style rifles from all stores
    - No longer sell firearms to anyone under 21 years of age
    - No longer sell high capacity magazines
    - Has never and will never sell bump stocks that allow semi-automatic weapons to fire more rapidly
    - Calling on policy makers to issue regulations to ban assault-style firearms, high capacity magazines, and so-called "bump stocks". Including a comprehensive database of those banned from buying firearms and for universal background checks which include mental health, among other relevant considerations. Specifically requesting policy makers to "close the private sales and gun show loophole" that waives the need for such background checks.
3. Kroger Company confirmed on March 1, 2018, via conference call, the company has completed the following:
    - Management decided to review the company's policy on the sale of assault weapons to the public and announced on March 1, 2018, it will no longer sell assault weapons in any of its stores nor to accept any special orders of these weapons, for example via online channels.
    - The company does not sell high capacity magazines for ammunition or accessories.
    - The company will be raising the minimum age for purchasing any firearm or ammunition across all stores to 21 years of age.
4. Walmart confirmed in writing the following:
    - The company does not sell any assault weapons following a decision made in 2015.
    - The company's firearm inventory is catered towards the hunter and sporting clay enthusiasts.
    - The company does not sell any handguns in continental United States, expect in Alaska.
    - The company does not sell any assault weapon accessories, such as bump stocks or trigger cranks, which are designed to modify firearms to make them more like an assault weapon.
    - On February 28, 2018, the company announced they reviewed their firearm policy and decided to raise the age restriction for purchasing firearms and ammunition to 21 years of age.
5. Sportsman's Warehouse has agreed to engage with CalPERS. Staff has scheduled a conference call with the Chairman and CEO for March 6, 2018.

CalPERS will continue to monitor the situation for other potential engagement options.

Budget and Fiscal Impacts

Funding for ESG Strategic Plan activities is included in the approved and existing INVO budget.

Benefits and Risks

The progress and completion of the Plan strategic priorities are an integral part of achieving long-term fund sustainability. As objectives are achieved, the following benefits are expected:

- Strengthened understanding of ESG factors relevant to risk and return specific to CalPERS' investment objectives
- Reduced exposure to ESG risk through enhanced disclosures of ESG considerations in periodic filings globally
- Enhanced Total Fund performance by increased corporate board diversity

Conversely, risks of not completing the strategic priorities may include a lessened understanding and management of ESG investment risk and opportunity across the portfolio.

Attachments

Attachment 1 – ESG Strategic Plan Update

____

Anne Simpson
Investment Director

____

Theodore Eliopoulos
Chief Investment Officer