CalPERS and Divestment

The call for divestment has become an increasingly popular tool for promoting an important cause or belief. As laudable as the underlying motivations may be, divestment has unintended consequences for the CalPERS fund, our Board and our members. The most acute is a conflict for the CalPERS Board of Administration (Board), which has a fiduciary duty to its members.

Our Obligations as Fiduciaries

As fiduciaries, our duty is to our members and their beneficiaries. This duty derives from the California Constitution requiring the Board to act "solely in the interest of, and for the exclusive purpose of providing benefits to, participants and their beneficiaries, minimizing employer contributions, and defraying reasonable expenses of administering the system." These duties include an explicit obligation to diversify the portfolio to minimize the risk of loss and maximize the rate of return. And, these duties explicitly "take precedence over any other duty." As a mature, cash-flow negative system, CalPERS is obligated to seek out and implement the portfolio construction methods that best serve our mission—the sustainable delivery of promised pension benefits.

Divestment Conflicts With Our Fiduciary Duty

As a government agency, CalPERS is sensitive to public policy issues, but divestment pits social responsibility against our fiduciary obligations. Why?

It Increases Risk. Divestment limits investment opportunities, decreasing diversification, limiting returns, and increasing risk in our investment portfolio.

We Lose our Voice. When we divest, we give up our "seat at the table" as a shareowner, thereby losing our best avenue for influencing a company to act in line with our core values and principles. CalPERS believes engagement is the first call to action, and results show that engagement is the most effective form of communicating concerns with the companies we own. Divestment is not to be confused with a product boycott, or sanctions, which are a direct hit to a company where it counts—the bottom line.

We Lose Money. As of June 30, 2016, CalPERS-related divestment initiatives, including forgone performance and transaction fees, are estimated to have cost the System nearly $8 billion. Given the reliance on investment returns to pay promised benefits, these forgone investment returns and added transaction costs can spell higher contribution rates for CalPERS employers and their employees.

Engagement Works – Our Vote is Our Voice

Corporate engagement is critical to our investment strategy. CalPERS has a long and successful history of engaging portfolio companies on environmental, social, and governance (ESG) topics, including climate change, natural resource availability, and respect for human rights. Engagement yields real results.

CalPERS

As a direct result of keeping our "seat at the table," many of the causes championed by CalPERS are gaining important ground. For example:

Climate Change – In partnership with the "Aiming for A" campaign, a coalition of asset owner investors, British Petroleum and Royal Dutch Shell agreed to support a 2015 shareowner proposal on climate risk reporting. The following year, CalPERS co-filed shareowner proposals addressing climate risk reporting at Rio Tinto, Anglo American, and Glencore. These proposals were supported by management and received over 96% support. Investor engagement was an essential part of the successful campaigns.

Proxy Access – Proxy access provisions in bylaws allow shareowners to more easily nominate directors to public company boards. Partnering with New York City's Board Accountability Project, CalPERS has engaged multiple portfolio companies to win this investor-friendly right, with over 400 companies adopting proxy access provisions since 2015. One success story in particular is our proxy-access campaign with Exxon Mobil, which garnered 49% support in 2015, and successfully passed in 2016 with 61% of the vote. Due to the increased pressure from investors urging Exxon to have a climate-competent board, Exxon announced in early 2017 that an atmospheric scientist, Dr. Susan Avery, had been added to its board of directors.

Worker Safety – Following the Rana Plaza garment factory collapse in Bangladesh in 2013, CalPERS co-founded the investor-led Human Capital Management Coalition. The coalition, representing some $1.2 trillion in assets under management, developed a set of questions that investors can use to engage companies to improve worker safety. Additionally, CalPERS has engaged on supply-chain activities with companies such as Carter's, Children's Place, Walmart, Kohl's, Gap, and McDonald's.

Investor Networks – Through our investor networks, we are also driving real change. For example, CalPERS is on the board of the Council of Institutional Investors, which engages on corporate governance topics with other investors representing an aggregate $20 trillion, as well as on the board of Ceres, whose Investor Network on Climate Risk represents $14 trillion worth of investor capital held by like-minded institutions dedicated to addressing climate change. In the fixed income space, CalPERS participates in the Credit Roundtable and Fixed Income Forum, representing total member assets of roughly $25 trillion.

We are committed – In August 2016, the Board adopted a five-year plan for CalPERS' sustainable investment and governance work. The plan identifies work across six strategic initiatives and serves as the framework by which we execute our proxy voting responsibilities, engage public companies, and work with internal and external investment managers to ensure alignment with our Investment Beliefs, Core Values, and policies.

We Are in This Together

As reflected in CalPERS Investment Belief 3, our investment decisions may reflect wider stakeholder views provided they are consistent with our fiduciary duties to our members and beneficiaries. While our primary stakeholders are the more than 1.8 million members, the more than 3,000 employers, and the millions of California taxpayers who collectively bear the economic consequences of CalPERS' investment decisions, CalPERS has many stakeholders who express opinions on investment strategy or ask CalPERS to engage on a particular issue. We must all weigh the costs, risks, and unintended consequences of divestment against our fiduciary duty to California's public employees.