
August 15, 2016**Item Name:** Global Governance Strategic Review: Adoption of 5-Year Plan**Program:** Global Governance**Item Type:** Action**Recommendation**

Staff recommends that the CalPERS Board adopt the Global Governance 5-Year Plan presented in the attachment.

Executive Summary

This agenda item presents the final phase in developing CalPERS' new 5-year sustainable investment strategy on integrating environmental, social, and governance (ESG). The new ESG strategy has been developed through an iterative process the Investment Committee launched January 2016. The attached plan delineates the Strategic and Core areas to focus CalPERS' resources with associated key performance indicators (KPIs). The Strategic work includes a focus on:

- Data and Corporate Reporting Standards
- Engage UN PRI Montreal Pledge Companies
- Diversity and Inclusion
- Manager Expectations
- Research
- Private Equity Fee and Profit Sharing Transparency

Core work represents activity under current CalPERS policy and mandates. Timelines for accomplishing these initiatives, as well as the progress we hope to make during the 5-year plan, are presented in the attachment.

Strategic Plan

This agenda item supports the CalPERS Strategic Plan goals of improving long-term pension benefits sustainability and actively managing business risks with an enterprise-wide view.

Investment Beliefs

This agenda item supports the CalPERS Investment Beliefs:

Investment Belief 2: A long time investment horizon is a responsibility and an advantage

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 5: CalPERS must articulate its investment goals and performance measures and ensure clear accountability for their execution

Investment Belief 7: CalPERS will take risk only where we have a strong belief we will be rewarded for it

Investment Belief 9: Risk to CalPERS is multi-faceted and not fully captured through measures such as volatility or tracking error

Background

In January 2016, the Investment Committee began vetting CalPERS' new 5-year strategy through monthly reports to the Investment Committee. The intent of these sessions was to solicit feedback on CalPERS' climate change, human capital and board quality strategies for engagement, advocacy and integration. Staff additionally grouped the initiatives as Strategic and Core and developed key performance indicators and recommendations for partnerships.

Budget and Fiscal Impacts

Not Applicable.

Benefits/Risks

Benefits – Continuing our focus on understanding and improving alignment of interest factors is consistent with our Investment Beliefs.

Risks – Poor disclosure creates uncertainty around implementation of Investment Beliefs.

Attachments

Attachment 1 – Review of ESG Strategy: Final 5-Year Plan

Anne Simpson

Investment Director
Global Governance

Dan Bienvenue

Managing Investment Director
Global Equity

Theodore Eliopoulos

Chief Investment Officer



Global Governance Strategy Review

Investment Committee, August 2016

Objectives

- Review strategic and core initiatives with key performance indicators
- Seek Investment Committee's approval of 5-year plan

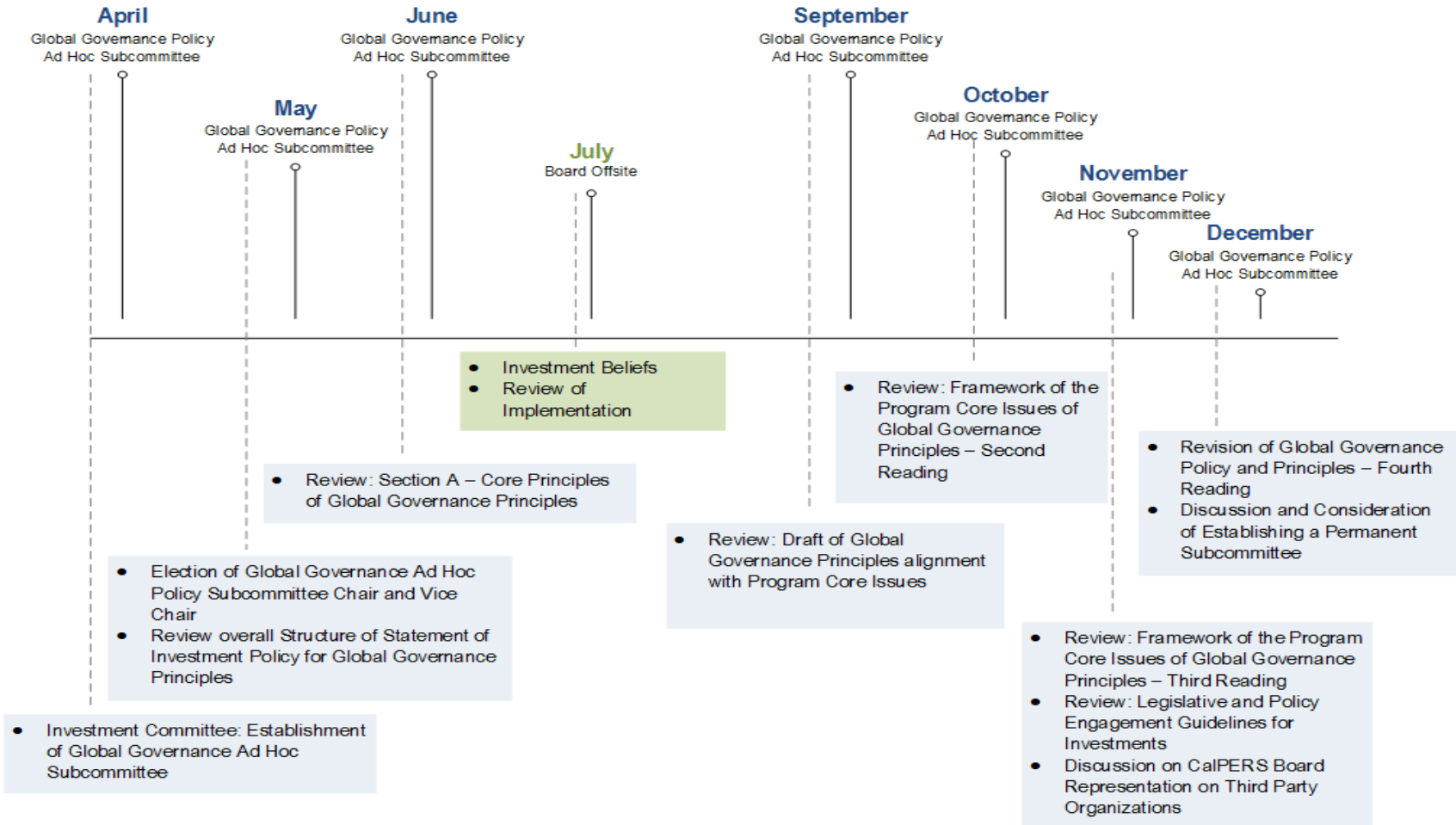
Global Governance Strategy Review

Summary of the 5-year plan for Governance & Sustainability

	Environmental	Social	Governance
S T R A T E G I C	<ul style="list-style-type: none"> Data and corporate reporting standards (includes water risk) Manager Expectations (includes water risk) 	<ul style="list-style-type: none"> Data and corporate reporting standards (includes human capital) Manager Expectations 	<ul style="list-style-type: none"> Data and corporate reporting standards (focusing on the long-term) Manager Expectations
	<ul style="list-style-type: none"> Research <ul style="list-style-type: none"> Sustainable Investment Research Initiative (SIRI) Global Equity Strategies 	<ul style="list-style-type: none"> Research <ul style="list-style-type: none"> SIRI Diversity Income inequality (action plan if warranted) 	<ul style="list-style-type: none"> Research <ul style="list-style-type: none"> Topics from Global Governance Principles Review Supply Chain Activities
	<ul style="list-style-type: none"> Engage 80 PRI Montreal Pledge Companies (identify water risk candidates) 	<ul style="list-style-type: none"> Diversity and Inclusion <ul style="list-style-type: none"> Engagement Voting 3D Advocacy 	<ul style="list-style-type: none"> Private Equity Fee and Profit Sharing Transparency (including AB 2833)
	<ul style="list-style-type: none"> Carbon Footprinting – Total fund Thermal Coal Companies – (SB185) 	<ul style="list-style-type: none"> Responsible Contractor Program 	<ul style="list-style-type: none"> Proxy Voting Shareowner Campaigns (Proxy Access/ Majority Voting) Focus List Divestment: Mandates, Policy & Principles
C O R E	Work through Partnerships to leverage resources and impact		
	<ul style="list-style-type: none"> Corporate Engagements Federal and Legislative Guidelines Sustainability Report Response to Ad Hoc Media and Stakeholder Requests 		

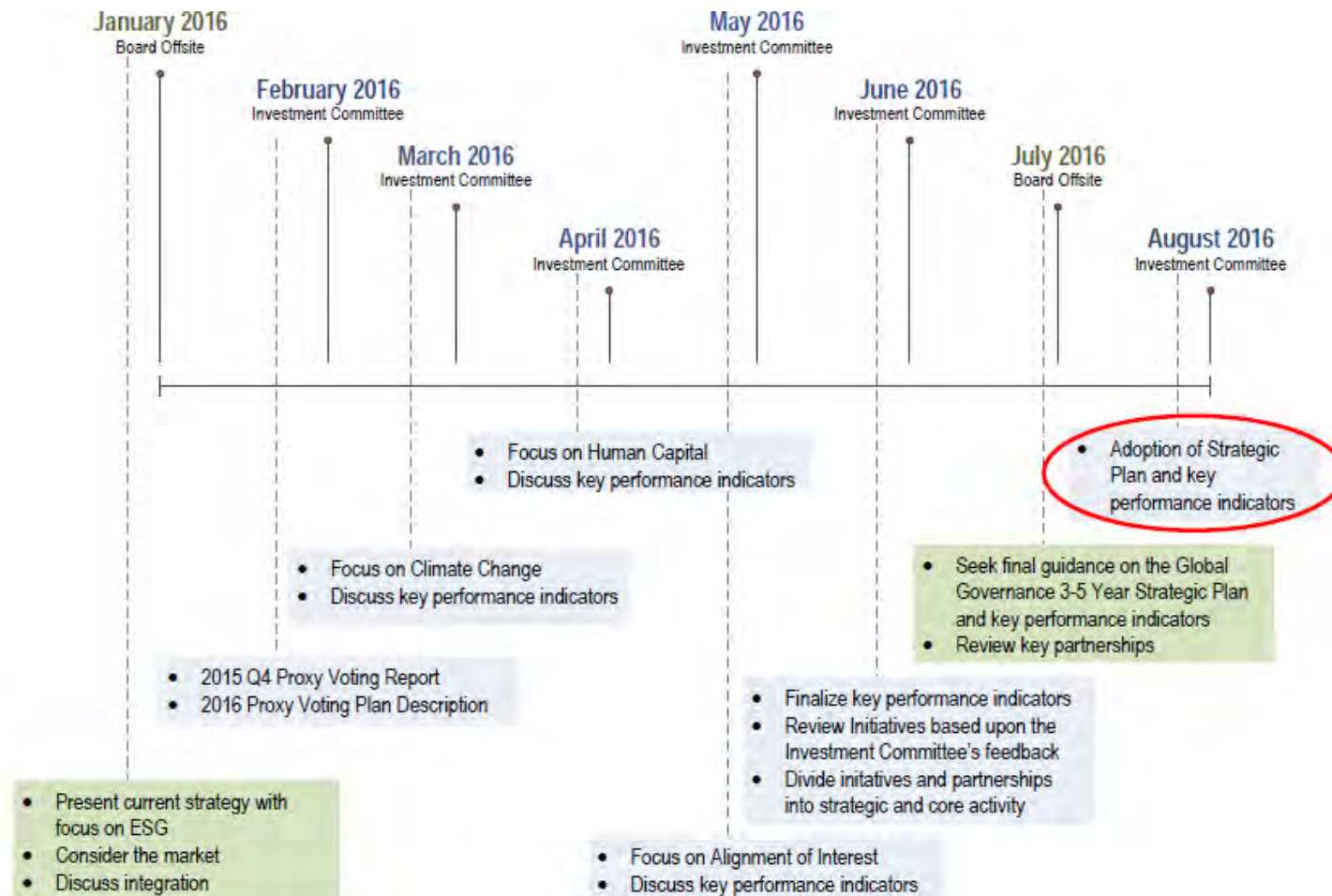
Global Governance Strategy Review

2015 Timeline: Global Governance Principles Review



Global Governance Strategy Review

Proposed Timeline for Developing a 3-5 Year Strategic Plan



Strategy on ESG Integration

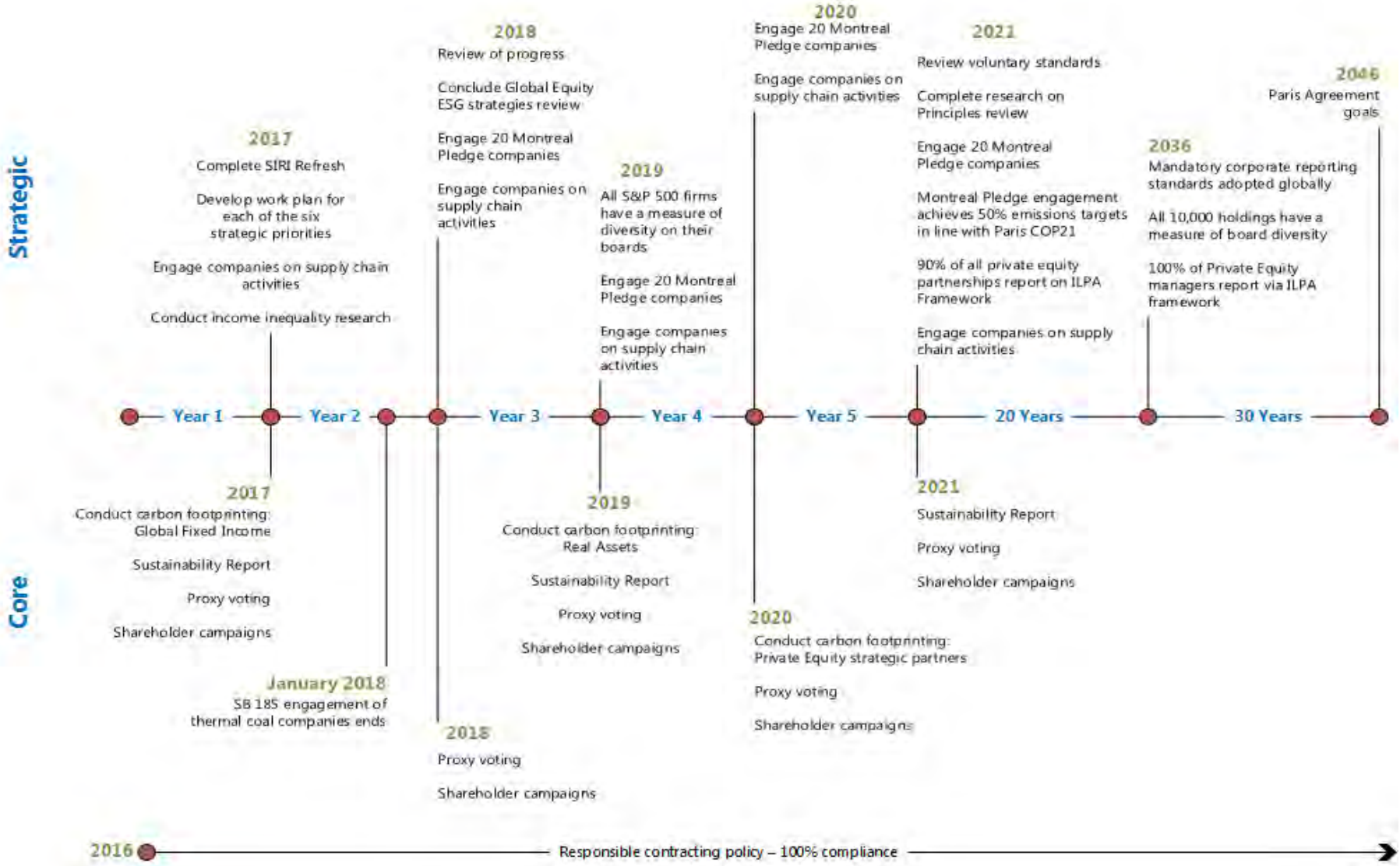
- Environmental
- Social
- Governance

Our approach utilizes three channels supported by partnerships



Global Governance Strategy Review

ESG Strategy Timeline



Strategic Initiatives

1. Data & Corporate Reporting Standards

Objectives

- Initial voluntary corporate reporting including enhanced disclosure of ESG considerations in periodic filings globally
- Adoption of enhanced mandatory reporting of ESG in periodic filings globally

Key Performance Indicators

- Benchmark and track the progress of integrated reporting globally
- Mandatory standards adopted globally

Timeline:

- Review voluntary standards: 5 years
- Mandatory standards to be adopted globally: 20 years

2. Engage UN PRI Montreal Pledge Companies

Objective

- Manage climate risk and opportunity by engaging 80 Montreal Pledge companies

Key Performance Indicators for 80 Montreal Pledge Companies

- All 80 companies establish a carbon reduction target consistent with Paris COP 21
- Measure and report reduction in carbon footprint
- Track financial performance of companies with established reduction targets

Timeline:

- Emissions reduction targets for portfolio companies generating half of the emissions: 30 years
- Engage 20 companies: each of years 2, 3, 4, 5 of the 5-year plan

3. Diversity & Inclusion

Objective

- Enhance Total Fund performance by increasing corporate board diversity

Key Performance Indicators

- All public companies in which CalPERS invests have a dimension of board diversity¹
- Track financial performance of companies with diverse boards

Timeline:

- Board diversity: 3 years for the S&P 500²; 20 years for all 10,000+ holdings in public equity

¹Diversity: Board diversity should be thought of in terms of skill sets, gender, age, nationality, race, sexual orientation, gender identity, and historically under-represented groups. Consideration should go beyond the traditional notion of diversity to include a more broad range of experience, thoughts, perspectives, and competencies to help enable effective board leadership. – Source: Global Governance Principles, Section B.9.

²Reference: 2015 Spencer Stuart Board Index - <https://www.spencerstuart.com/research-and-insight/spencer-stuart-us-board-index-2015>

4. Manager Expectations

Objective

- Manager Expectations that allow CalPERS to better understand and manage ESG investment risk and opportunity across the portfolio

Key Performance Indicators

- All managers have policies and procedures for including ESG information in decision making
- Asset classes establish and implement documented procedures for due diligence, contracting, and monitoring activities

Timeline:

- All managers to have policies and procedures for including ESG information: 5 Years
- Asset classes to establish and implement documented procedures: 2 Years
- Pilot report to IC December 2016

5. Research

Objective

- Strengthen understanding of ESG factors relevant to risk and return specific to CalPERS' investment objectives

Key Performance Indicators

- Complete evidence review
 - SIRI refresh (inclusive of diversity and income inequality)
 - Global Equity strategies
 - Research companies most exposed to water risk to inform engagement
 - Topics from Global Governance Principles review, including supply chain issues
- Integrate relevant research findings into investment decision making

Timeline:

- Complete SIRI refresh: 1 year
- Global Equity strategies: 2 years
- Present findings of income inequality research and action plan if warranted: 2 years
- Principles review topics: 5 years
- Efforts to integrate ESG research: Ongoing

6. Private Equity Fee & Profit Sharing Transparency

Objective

- Industry adoption of the Institutional Limited Partners Association (ILPA) framework for transparency of fees and profit sharing

Key Performance Indicators

- Ensure 100% of CalPERS' strategic private equity partnerships complete the ILPA fee reporting template and provide profit sharing information
- Target 100% of CalPERS private equity strategic partnerships complete the ILPA fee reporting template and provide profit sharing information
- Track and report industry ILPA adoption
 - Partnerships completing the ILPA fee reporting template and providing profit sharing information
 - Limited partners requiring such information from their general partners

Timeline:

- 90% of all partnerships: 5 years
- 100% of all partnerships: 20 years

Core Initiatives

Investment Committee Reporting on Core Activities

Annual Reporting (January – December):

Q1: Report on Work Plan for upcoming year for:

- Proxy Voting
- Shareowner Campaigns
- Corporate Engagements
- Global Governance Principles
- Legislative Guidelines

Q2: Report on:

- Responsible Contractor Policy
- Partnerships

Q3: Report on results for:

- Proxy Voting
- Shareowner Campaigns
- Corporate Engagements
- Focus List

Q4: Report on results of:

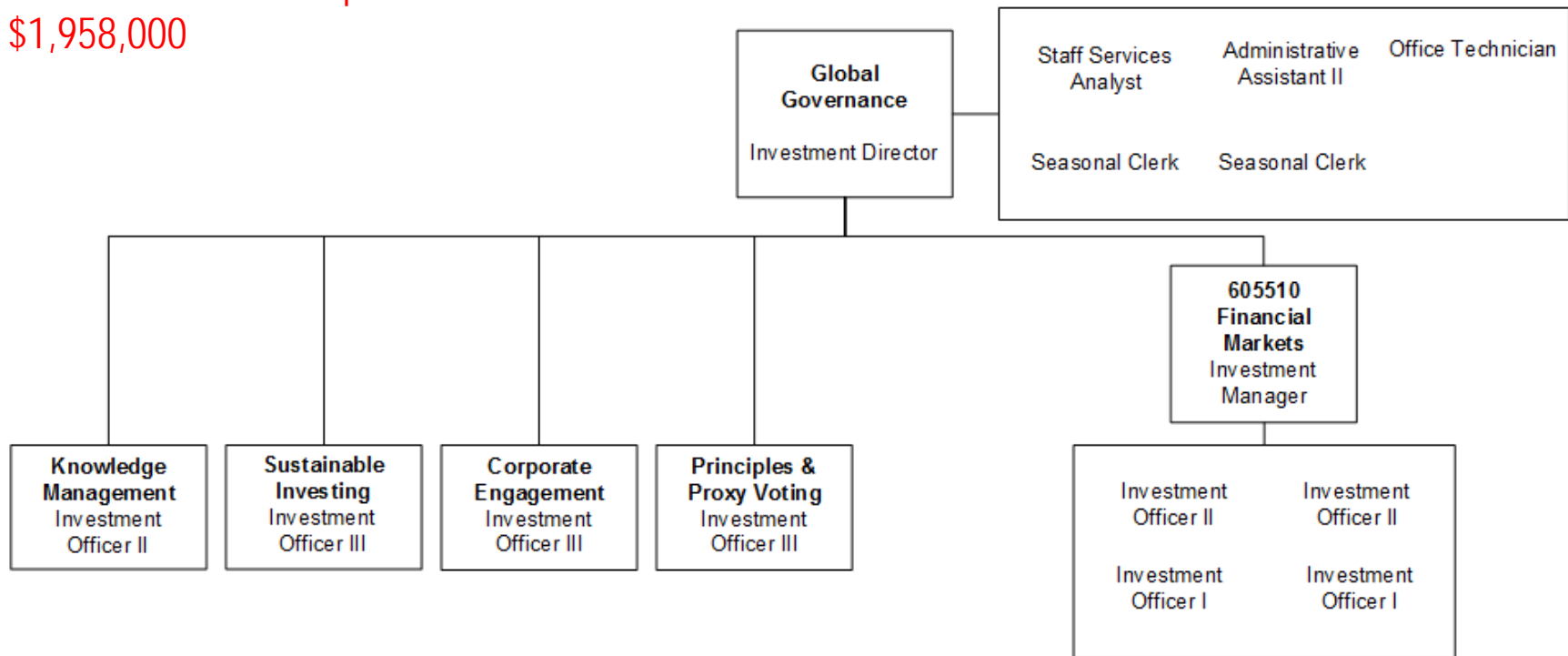
- Carbon Footprinting
- Divestment: Mandates, Policy and Principles, including Thermal coal companies SB 185

Bi-Annual Reporting:

- Sustainability Report

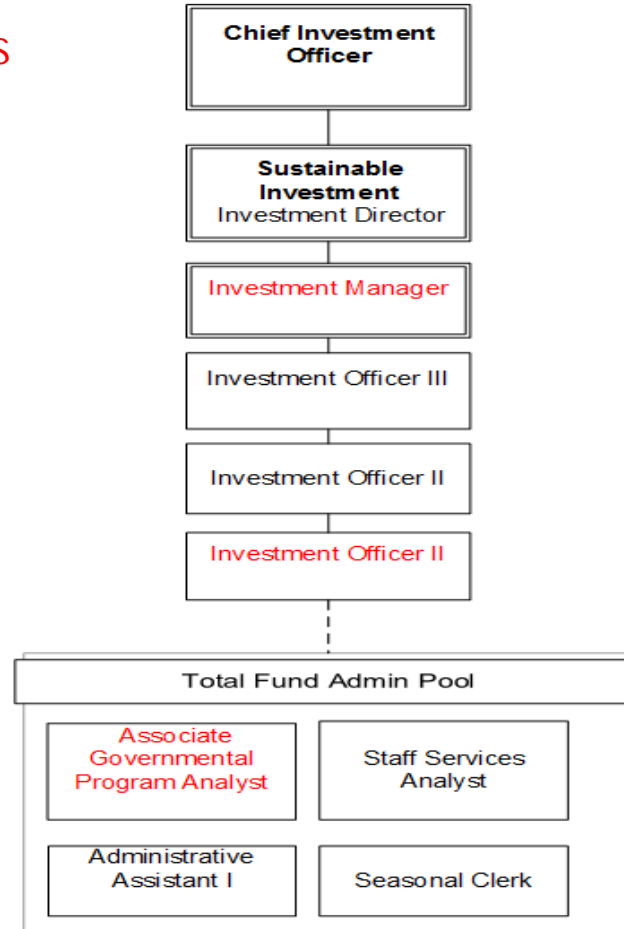
Global Governance Current Org Structure

Total cost for current positions
\$1,958,000



New Organizational Alignment – Sustainable Investment

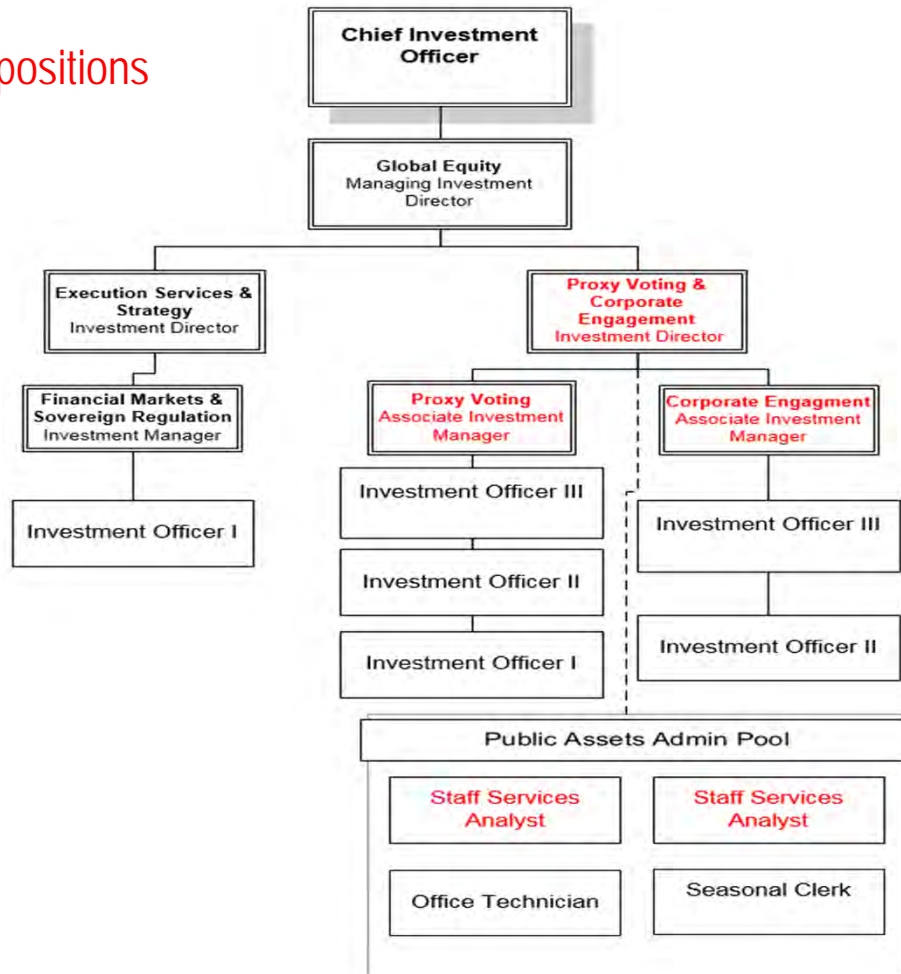
Total cost for added positions
\$660,000



New positions in red

New Organizational Alignment – Global Equity

Total cost for added positions
\$1,204,000



New positions in red

Additional Organizational Alignment

- New Function
- Position to be transferred from other INVO area

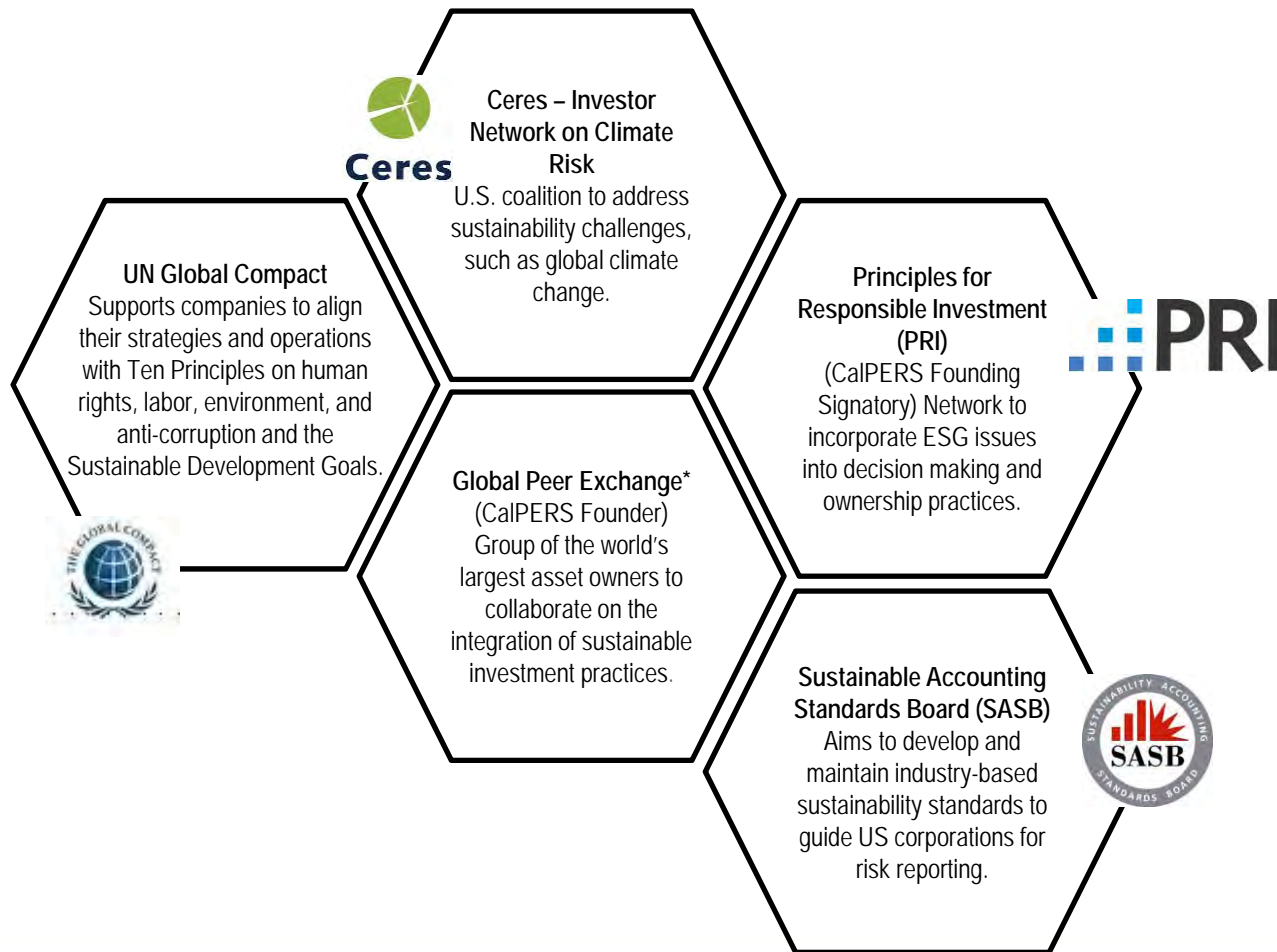


Appendix: Partnerships

Partnerships | Key to Strategy

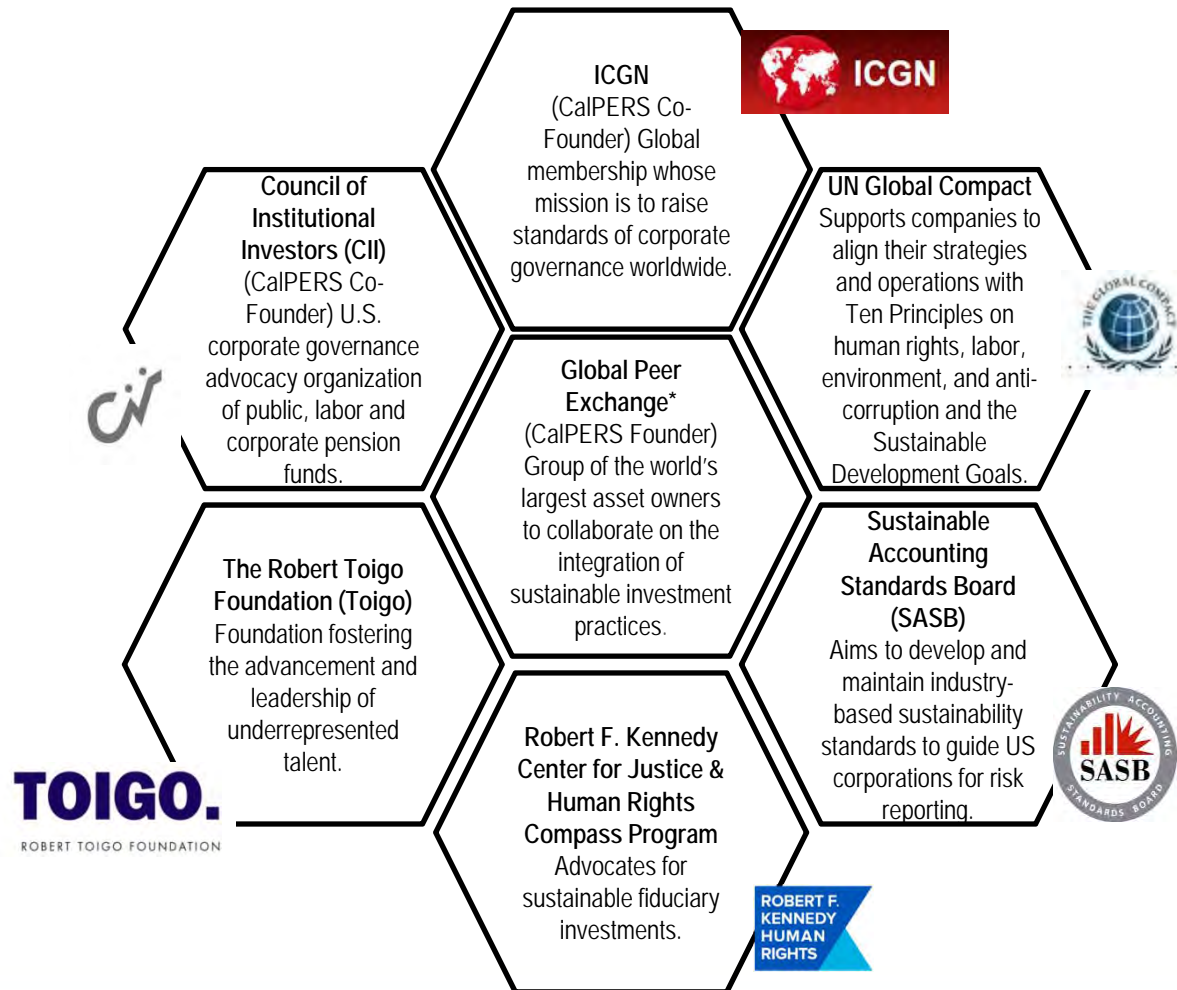
- Many relationships, but certain partnerships are key to implementing ESG strategy
- Share experiences and best practices
- Leverage resources
- Enhance impact
- Estimated annual cost:
 - Membership Fees: \$106,000
 - Related Expenses: \$80,000

Key Partnerships | Environmental



*APG Asset Management, Australian Super, BT Pension Scheme, CalSTRS, Florida State Board of Administration, Government Employee Pension Fund (South Africa), New York City, Norges Bank Investment Management, Ontario Teachers' Retirement System, PGGM, PREVI (Brazil), TIAA-CREF, Universities Superannuation Scheme, and RPMI (UK).

Key Partnerships | Social



*APG Asset Management, Australian Super, BT Pension Scheme, CalSTRS, Florida State Board of Administration, Government Employee Pension Fund (South Africa), New York City, Norges Bank Investment Management, Ontario Teachers' Retirement System, PGGM, PREVI (Brazil), TIAA-CREF, Universities Superannuation Scheme, and RPMI (UK).

Global Governance Strategy Review

Key Partnerships | Governance



*APG Asset Management, Australian Super, BT Pension Scheme, CalSTRS, Florida State Board of Administration, Government Employee Pension Fund (South Africa), New York City, Norges Bank Investment Management, Ontario Teachers' Retirement System, PGGM, PREVI (Brazil), TIAA-CREF, Universities Superannuation Scheme, and RPMI (UK).