



Seattle City Employees' Retirement System

Environmental, Social and Governance (ESG) Update Second Quarter 2017

Purpose

This update is required by the following motion adopted by the Board on February 12, 2015:

*The Retirement Board of Administration directed that the Seattle City Employees' Retirement System (SCERS) pursue corporate engagement on climate change and other environmental issues, as presented by staff in their January 26, 2015 memorandum; and pursue, as appropriate, investments that are expected to produce investment results consistent with SCERS's fiduciary duty to its members and, if possible, also positively address climate change and other environmental issues. The Board recognizes that these types of investments (e.g. renewable energy, cleantech, and green bonds) are relatively new and limited in availability and will need to be considered prudently as SCERS pursues investments in its asset class (e.g. real assets, private equity, fixed income). **SCERS's staff and advisers will provide quarterly updates regarding Environmental, Social and Governance (ESG) investment issues** and incorporate ESG into SCERS's work plan. The Board directs SCERS's staff to engage with trade associations such as Coalition for Environmentally Responsible Economics (Ceres) and other pensions to examine an approach to ESG investments, and also to consider engaging with an independent consultant to assist in this review.*

Staff has primarily focused on the environmental issue of climate change. At the Board's direction, other ESG matters may be considered in future updates.

Activity Directed to SCERS

- **Mayor Murray** sent a letter to the SCERS Board on April 11, 2017, requesting that the Board re-evaluate its position on the role of fossil fuel holdings in SCERS's investment portfolio and divest any holdings in companies whose primary business is the mining or burning of coal (a third request related to the City's Deferred Compensation Plan, which is managed by SDHR rather than SCERS). At the Board meeting on April 13, 2017, the Board passed motions requesting that: (1) the Investment Advisory Committee review prior recommendations on fossil fuel divestment made by NEPC and staff; (2) staff produce a review of the positive action strategy that the Board adopted in February 2015 related to climate change; and, (3) legal counsel provide a full analysis of the Board's fiduciary duty as applied to fossil fuel divestment. These items will be discussed at the Board meeting on July 13, 2017.

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Industry Developments

- President Trump declared his intention to withdraw the United States from the COP21 Paris Climate Agreement.
- The **Montgomery County Council** (Maryland) passed a non-binding resolution that asks the Montgomery County Employees' Retirement System to divest from its fossil fuel holdings. The measure had originally been introduced as a law requiring divestment. It was later modified to a resolution following opposition from county retirees and the retirement system board who found it to interfere with the retirement system's fiduciary duty.¹
- Bills were introduced in the **California legislature** requiring CalPERS and CalSTRS to divest from companies involved in the construction of the border wall between the United States and Mexico (AB 946) and from companies that build or finance the Dakota Access Pipeline (AB 20).

Membership Organization Activity

- Jason Malinowski and Jill Johnson attended the **Ceres Investor Network** meeting in San Francisco. In this meeting California Treasurer, Betty Yee, and representatives from CalPERS introduced the "Global Climate 100 Initiative," which will focus their efforts on corporate engagement to maximize effectiveness. They invited others to join with them in this process, although its relevance to smaller investors like SCERS was unclear.
- Jill Johnson attended the Ceres Conference in San Francisco. The topics broadly covered actions undertaken by states, for example California, towards meeting the goals agreed to at the COP21 in Paris. These initiatives are already underway and will continue despite the change of direction at the federal government level.
- Jill Johnson and Jason Malinowski participated in **Ceres'** monthly conference calls and frequent list serve activity for the INCR Carbon Asset Risk Working Group, INCR Policy Working Group, Shareholder Initiative on Climate and Sustainability (SICS) and Low Carbon, Clean Energy Working Group.

SCERS Proactive Strategy

Corporate and Regulatory Engagement

- SCERS, CalSTRS, the Nathan Cummings Foundation and the UK-based Local Authority Pension Fund Forum, with the support of the 50/50 Climate Project, urged shareholder action at **Southern Company**, a gas and electric utility. SCERS and the other investors requested votes against two directors and the executive compensation plan to hold the board accountable for serious delays in key projects (Kemper coal power plant, Vogtle nuclear project) that have incurred significant losses. While the measure passed, there was significant (39%) opposition to the executive compensation plan, which demonstrated that shareholders were losing confidence in the company.²
- **JP Morgan** updated its proxy voting guidelines to reflect the materiality of company environmental policies and disclosures in response to a shareholder proposal in which SCERS was a co-filer. The proposal has since been withdrawn.
- **BlackRock** made changes to their investment stewardship procedures to prioritize climate change in response to a shareholder proposal in which SCERS was a co-filer. The proposal has since been withdrawn.³
- SCERS joined the Council for Institutional Investors and many of its members in a letter to the **House of Representatives** opposing provisions in the Financial Choice Act bill that would

weaken important shareholder rights, including setting prohibitively high hurdles for filing shareholder resolutions.⁴

- SCERS joined Boston Common Asset Management and other institutional investors in a letter to the **banks financing the Dakota Access Pipeline** asking them to reroute the pipeline to avoid the Standing Rock Sioux Tribe's treaty territory and therefore protect the banks' reputation and consumer base and avoid legal liabilities.⁵
- SCERS joined the AFL-CIO and other institutional investors in a letter to the **Securities and Exchange Commission** in support of a CEO-to-worker pay ratio disclosure rule that is required under the Dodd-Frank Act.⁶

Integrating Climate Change into the Investment Process

- **BlackRock** voted for shareholder resolutions at Occidental Petroleum and ExxonMobil that require the companies to publish annual assessments of the impact of climate change and related policy on their businesses. BlackRock is a material shareholder in both companies and had opposed similar resolutions in prior years. Both resolutions passed despite being opposed by management. SCERS had placed BlackRock on watch in December 2016 due to ESG concerns, including their reticence to oppose management and limited focus on environmental and social issues.^{7,8}
- Jason and Jill had an educational meeting with the **Sustainability Accounting Standards Board (SASB)** in San Francisco. SASB is working towards developing a universal set of sustainability metrics for company financial reporting.
- Jason and Jill had an introductory call with the **UN Principles of Responsible Investing (PRI)** to explore possible membership. Jill subsequently attended the Western North American Network PRI conference in Victoria, BC. The conference touched on all aspects of environmental, social and governance investing issues. Beatrix Dart, a co-founder of the 30% club, which advocates for a minimum of 30% of women on corporate Boards, was a key note speaker. She said that diversity is the best insurance against group-think. A panel of mostly Canadian pension plans discussed the pros and cons of The Climate Related Financial Disclosure (TCFD) project.

Sustainability Investments

Motion: "... *The Board recognizes that these types of investments (e.g. renewable energy, cleantech, and green bonds) are relatively new and limited in availability and will need to be considered prudently as SCERS pursues investments in its asset class (e.g. real assets, private equity, fixed income)*"

- No updates.

¹ https://www.washingtonpost.com/local/md-politics/montgomery-council-urges-pension-funds-to-sell-fossil-fuel-investments/2017/05/16/cf9ef06a-3a5e-11e7-8854-21f359183e8c_story.html?utm_term=.57e431bb353c

² <https://www.bloomberg.com/news/articles/2017-04-25/southern-challenged-over-executive-pay-amid-power-plant-delays>

³ <http://www.reuters.com/article/us-blackrock-climate-exclusive-idUSKBN16K0CR>

⁴ http://www.cii.org/files/issues_and_advocacy/correspondence/2017/05-17-17%20FinChoice%20Letter%20FINAL.pdf

⁵ <http://news.bostoncommonasset.com/wp-content/uploads/2017/02/Investor-Statement-to-Banks-Financing-DAPL-updated-as-of-4-21-2017.pdf>

⁶ <https://drive.google.com/file/d/0B9TKBaOfJhNHYZNQeWFXZV8wSzA/view>

⁷ <https://www.ft.com/content/d8d177a4-4623-11e7-8519-9f94ee97d996>

⁸ <http://www.reuters.com/article/us-blackrock-occidental-climate-idUSKBN1882AA>

Appendix

SCERS Public Equity Allocation to Fossil Fuel Companies

As of March 31, 2017

SCERS Ownership	Account Type	Allocation (\$ million)	% of SCERS Total Portfolio
Direct	Separate Account	\$31.5	1.2%
Indirect	Commingled Fund	\$55.9	2.2%
Total		\$87.4	3.4%

Source: Bloomberg, Fossil Free Indexes, SCERS calculation; excludes overlay program, transition holdings

Note: Fossil Fuel companies as defined by the Carbon Underground 200, a list generated by Fossil Free Indices of the top 100 public coal companies globally and the top 100 public oil and gas companies globally ranked by the potential carbon emissions content of their proven reserves; Carbon Underground 200 constituents as of July 2016