



# Seattle City Employees' Retirement System

## Environmental, Social and Governance (ESG) Update Fourth 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

- Representatives and members of **UNITE HERE** gave public comment at the July and October Investment Committee meetings asking that SCERS encourage Brookfield Asset Management (a SCERS-invested real estate manager) to act fairly with workers at its hotel properties that are seeking to unionize or negotiate contracts. SCERS staff subsequently spoke with Brookfield's Head of Hospitality Investments to understand their approach to unionization efforts and inquire on the concerns raised by UNITE HERE. Staff found Brookfield's approach to be accommodative and reasonable.
- Following a discussion on fossil fuel divestment at the July Board meeting that was in response to a letter that **former Mayor Murray** sent to the SCERS Board in April, a motion was passed at the August Board meeting where "the Board of Administration reaffirmed its support for the positive action strategy related to climate change, as presented by staff on July 13, 2017, that includes engaging as shareholders with corporations and other entities, considering sustainability investments, and integrating climate change risk into the investment process. The Board concluded that the positive action strategy is the most effective means for Seattle City Employees' Retirement System (SCERS) to beneficially impact climate change while meeting its paramount fiduciary duties to the members of SCERS."

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## Industry Developments

- **CalSTRS'** Investment Committee approved divesting all non-US thermal coal holdings by July 1, 2017, as required by the Public Divestiture or Thermal Coal Companies Act. This represents approximately \$8.3 million, or 0.003%, of their portfolio and is concentrated in three companies. This follows a February 2016 vote in which the investment committee voted to divest US thermal coal holdings. SCERS does not have any direct investment in these three companies.<sup>1</sup>
- **CalPERS** completed its planned divestment from thermal coal companies that were not responsive to engagement efforts in advance of July 1, 2017, the date specified by the Public Divestiture of Thermal Coal Companies Act. Three companies responded to CalPERS' engagement by indicating plans to adapt their business models in consideration of clean energy generation. They were not divested. While fourteen companies either did not respond to CalPERS' engagements or failed to adjust their business plans and were divested. SCERS does not have any direct investment in these thermal coal companies.<sup>2</sup>
- **San Francisco City and County Employees' Retirement System (SFERS)** delayed a discussion on fossil fuel divestment that had been planned for its August Board meeting given the expectation of poor Board attendance. Fossil fuel divestment is opposed by both staff and its general investment consultant, **NEPC**. In the SFERS staff memo to the Board on the subject, Chief Investment Officer, William Coaker stated that while "...staff is keenly aware and concerned with the negative impact that climate change is having on our environment... We recognize that SFERS' divestment from fossil fuel holdings will not reduce carbon emissions – it simply changes ownership of these securities. With divestment, SFERS will forfeit its standing as a shareholder to engage these fossil fuel companies to transition their business plans to a low carbon economy in line with the Paris Agreement."<sup>3</sup>
- **Walden Asset Management** withdrew its proposal to **Vanguard Funds** that sought a report on its proxy voting policies and practices after Vanguard agreed to be more supportive of climate risk and board diversity in its company engagements and proxy voting.

## ESG Investor Organization and Staff Activity

- SCERS became a signatory of the **UN Principles of Responsible Investing (PRI)** in August 2017. The PRI is a world leader of responsible investment. It works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate. SCERS is one of the first smaller US public pension plans to become a signatory to this global organization.
- 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.
- Jill Johnson participated on a panel at the **US Markets Group PNW Institutional Investor Forum**, in Portland, OR, and shared ways in which a smaller pension plan can have a positive effect on ESG issues.
- Jason Malinowski participated on a panel at the **PRI Western North American Network** event in Seattle on November 6, 2017 on the topic of ESG integration for asset owners.

## **SCERS Positive Action Strategy**

### **Shareholder Advocacy**

- SCERS and approximately 100 other institutional investors signed an investor initiative co-sponsored by Boston Common Asset Management and ShareAction titled: “Banking on a Low Carbon Future, Alignment with the Taskforce on Climate-related Financial Disclosures (TCFD).” The investors, representing a combined total of nearly \$2 trillion in assets under management, wrote to the CEOs of 62 of the world’s largest banks calling for disclosure of the banks’ responses to climate change risks and opportunities.<sup>4</sup>
- SCERS and Mercer reviewed the watch list status of BlackRock following the 2017 proxy season that is discussed in an accompanying memo.

### **Integrating Climate Risk into the Investment Process**

- Staff initiated discussions with NEPC on improving their ESG capabilities to better meet SCERS ongoing needs.

### **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)*”

- Global Infrastructure Partners, a SCERS-invested infrastructure manager, announced that it was acquiring Equis Energy. Equis owns 11 gigawatts of solar, wind and hydroelectric power assets in Australia, Japan, India, Indonesia, the Philippines and Thailand.<sup>5</sup>
- Tax reform may have a negative impact on renewable energy.<sup>6</sup> Reducing corporate taxes would also lower a key source of clean-power financing. Additionally, the large number of solar imports, mostly from China, have hurt US manufacturers. President Trump may respond by imposing trade barriers, which would in turn could solar development.<sup>7</sup>

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<sup>1</sup> <https://www.reuters.com/article/us-california-calstrs-coal/calstrs-agrees-to-divest-non-u-s-thermal-coal-assets-idUSKBN18Z044>

<sup>2</sup> <https://www.calpers.ca.gov/docs/board-agendas/201708/invest/item04f-00.pdf>

<sup>3</sup> <https://mysfers.org/wp-content/uploads/08092017-board-meeting-07-fossil-fuel-A.pdf>

<sup>4</sup> <https://shareaction.org/press-release/investor-letter-bank-low-carbon/>

<sup>5</sup> <https://www.bloomberg.com/news/articles/2017-10-25/global-infrastructure-acquires-equis-energy-in-5-billion-deal>

<sup>6</sup> <https://www.bloomberg.com/news/articles/2017-10-03/u-s-tax-reforms-would-leave-renewable-energy-out-in-the-cold>

<sup>7</sup> <https://www.politico.com/story/2017/09/22/solar-tariff-trump-china-trade-243021>

## Appendix

### **SCERS Public Equity Allocation to Fossil Fuel Companies**

*As of September 30, 2017*

SCERS Ownership	Account Type	Allocation (\$ million)	% of SCERS Total Portfolio
Direct	Separate Account	\$32.3	1.2%
Indirect	Commingled Fund	\$51.7	1.9%
Total		\$84.0	3.0%

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