



City of Seattle

Seattle City Employees' Retirement System

ESG Quarterly Update: Third Quarter 2020



Introduction

SCERS believes that it can have a beneficial impact on certain Environmental, Social and Governance (ESG) matters consistent with its mission, investment beliefs and fiduciary duties

SCERS has pursued an ESG positive action strategy since 2015 with staff providing quarterly updates to the Board on its progress

The Board has identified *climate change* as an ESG priority for SCERS because of its criticality to the long-term risk and return of the capital markets

Positive Action Strategy

Shareholder
Advocacy


Sustainability
Investments

Integrating Climate
Risk into the
Investment Process



Investor Organizations and Initiatives

SCERS is an active member of three ESG investor organizations that provide shared resources and collaboration opportunities on ESG matters

| |  Ceres Network on Climate Risk and Sustainability |  Council of Institutional Investors® The voice of corporate governance |  PRI Principles for Responsible Investment |
|---------------|---|---|---|
| Primary Focus | Environmental | Governance | Environmental, Social, Governance |
| Mission | Advance leading investment practices, corporate engagement strategies and policy solutions to build an equitable, sustainable global economy and planet | Be the leading voice for effective corporate governance practices for US companies and strong shareholder rights and practices | Understand the investment implications of ESG factors and support its signatories in incorporating these factors into their decisions |
| Membership | North American institutional investors | US pensions and other benefit funds | Global institutional investors |

SCERS also participates in investor initiatives such as the Climate Action 100+ and Climate Majority Project related specifically to climate change



Shareholder Advocacy

Description

SCERS is an active shareholder employing its available rights to encourage companies to take actions that help mitigate climate change, which include increased disclosure, conducting climate risk assessments and ensuring robust government regulation

Current Focus

Interact with SCERS-invested managers so that they fully understand the financial impact of climate change and support actions that help mitigate climate change through their proxy voting and corporate engagement efforts

Engage, alongside other institutional investors, with a limited set of the highest fossil fuel-emitting companies so that they take necessary action on climate change

Advocate, alongside other institutional investors, for preserving and strengthening shareholder rights with regulators, policymakers and other relevant bodies



Shareholder Advocacy

Quarterly Activity



SCERS signed on to letters to the **Federal Reserve and other financial regulators** from Ceres that urged them to incorporate climate change into their regulatory mandate. The letters referenced a recent Ceres report entitled “Addressing climate as a systematic risk: A call to action for U.S. financial regulators”².



The **Securities and Exchange Commission (SEC)** finalized a rule related to proxy advisory firms³, which SCERS and other institutional investors had vigorously opposed during the public comment period. The SEC removed some of the more onerous requirements in the proposal, but it still has the potential to increase the power of corporate management at the expense of shareholders. ISS, SCERS’s proxy voting advisor, resumed its lawsuit against the SEC to prevent the rule from going into effect.

¹ <https://www.ceres.org/sites/default/files/Federal%20Regulators%20Letter.pdf>

² <https://www.ceres.org/resources/reports/addressing-climate-systemic-risk>

³ <https://www.sec.gov/rules/final/2020/34-89372.pdf>



Shareholder Advocacy

Quarterly Activity



Staff provided feedback to **ISS**, SCERS's proxy voting advisor, during its annual policy consultation. Amongst other suggestions, Staff suggested that the ISS Public Funds policy be more supportive of Board diversity through its voting recommendations.



Dimensional, a SCERS-invested manager, released its first Annual Stewardship Report that provides information on its corporate engagements, proxy voting and public policy advocacy¹. Dimensional also amended its proxy voting guidelines to allow for greater support of shareholder resolutions related to better environmental and social disclosures. Staff has been in a multi-year engagement with Dimensional that has sought ESG improvements.

¹<https://us.dimensional.com/-/media/Dimensional/Documents/Shared/2019-annual-stewardship-report.pdf>



Sustainability Investments

Description

Proactively evaluate investments that are expected to help address climate change, such as renewable energy infrastructure, and selectively make such investments if economically equivalent or superior to other available investments in the same category

Current Focus

Commit additional capital to the Infrastructure asset class to achieve its target weight (4%) by investing in diversified managers who preferably have experience and capabilities in the renewable energy sector

Monitor investments in green bonds by SCERS-invested managers and continue evaluating other sustainability investments, such as clean tech



Sustainability Investments

Quarterly Activity

Brookfield

Brookfield, a SCERS-invested manager, announced an agreement to develop and construct a 1,200-megawatt solar project in Brazil, which is targeted for completion in 2023¹.

¹<https://bep.brookfield.com/press-releases/2020/07-20-2020-230853598>



Integrating Climate Risk into the Investment Process

Description

Consider climate change as a risk alongside macroeconomic, geopolitical and other risks when making investment decisions, while also acknowledging that SCERS must take risk in order to generate the high return that it seeks

Current Focus

Expand the integration of ESG considerations to all asset classes (from Public Equity and Infrastructure currently) where it is material

Continue working with NEPC to enhance the climate change scenario analysis methodology that was incorporated into the 2019 asset-liability study



Integrating Climate Risk into the Investment Process

Quarterly Activity



SCERS requested and evaluated PRI assessment reports from each of its investment managers who are PRI signatories. These assessments were compared to NEPC's ESG ratings to understand where the managers may have opportunities to improve integration of material ESG factors into their investment process.

SCERS also received its 2020 PRI assessment report based on staff-provided information and a comparison to other institutions. The assessment continued to highlight Strategy & Governance and Public Equity as areas of strength.



Staff Activity



Jill Johnson participated in planning meetings as a member of the Council of Institutional Investors U.S. Asset Owners Advisory Council and the PRI Western North America Advisory Committee.

Jill also collaborated with an informal group of ESG leads at other public plans on areas of common concern, such as the recent proposed rules from the Securities and Exchange Commission and Department of Labor.



Investor and Industry Developments



The **Department of Labor (DOL)** announced proposed new regulations on June 23rd, named “Financial Factors in Selecting Plan Investment¹.” This proposed regulation would make it more difficult for ERISA plans to invest in strategies that consider ESG. While government plans are not regulated by ERISA, these regulations can have a spillover effect.

The DOL was first flooded with letters² asking for the typical 180-day comment period, instead of the shortened 30 days, then inundated with letters from institutional investors and asset managers opposing the regulation.

The DOL introduced another proposed regulation on August 31st that would curtail ERISA plans ability to vote all proxies³. Corporate pension plans have not greeted this proposed rule positively.

¹ <https://www.federalregister.gov/documents/2020/06/30/2020-13705/financial-factors-in-selecting-plan-investments>

² <https://www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95>

³ <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/fiduciary-duties-regarding-proxy-voting-and-shareholder-rights>



Informational Items



Several local chapters of the **International Union of Operating Engineers** sent letters to SCERS and other investors in Brookfield's Infrastructure funds. The union expressed contract-related concerns with Brookfield and the property management firm (BGIS) that was recently hired for its data center business. SCERS shared these concerns with Brookfield.



Members of **350 Seattle** requested that SCERS take various actions to oppose the renomination of Lee Raymond, former CEO of ExxonMobil, to the Board of JP Morgan Chase. SCERS informed 350 Seattle that it had opposed Mr. Raymond's nomination in 2019 and would continue to do so in 2020. While Mr. Raymond was ultimately renominated by shareholders, JP Morgan Chase announced that he would no longer serve as the Board's lead independent director.



Appendix



Divestment note

SCERS has occasionally been asked by stakeholders to divest from (or invest in) a targeted sector or other set of investments for ESG reasons

- Such requests had been extensively investigated by SCERS, including by legal counsel, staff, the investment consultant and the Investment Advisory Committee
- Each evaluation concluded that divestment conflicted with the Board's fiduciary duties because it was not in the best interests of SCERS members and should not be pursued

The Board has consistently stated that the positive action strategy is the most effective, permissible means for SCERS to beneficially impact its ESG priorities

SCERS's ESG Policy was updated in 2019 to address divestment directly

- "The Board will not divest or invest from a targeted company, sector or set of investment to further an ESG priority because doing so would be inconsistent with SCERS's mission..., fiduciary duties... and investment beliefs."



Fossil fuel company exposure

SCERS Public Equity Exposure to Fossil Fuel Companies

As of December 31, 2019

| SCERS Ownership | Account Type | Exposure (\$ million) | % of SCERS Total Portfolio |
|-----------------|------------------|-----------------------|----------------------------|
| Direct | Separate Account | \$33.2 | 1.1% |
| Indirect | Commingled Fund | \$42.0 | 1.3% |
| Total | | \$75.3 | 2.4% |

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