

AGENDA

A REGULAR MEETING OF THE CORPORATE GOVERNANCE

COMMITTEE AND THE BOARD OF INVESTMENTS*

LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION

300 N. LAKE AVENUE, SUITE 810, PASADENA, CALIFORNIA 91101

8:00 A.M., WEDNESDAY, APRIL 11, 2018**

*The Committee may take action on any item on the agenda,
and agenda items may be taken out of order.*

- I. CALL TO ORDER
- II. APPROVAL OF MINUTES
 - A. Approval of the Revised Minutes of the Regular Committee Meeting of October 11, 2017.
 - B. Approval of the Minutes of the Regular Committee Meeting of January 10, 2018.
- III. PUBLIC COMMENT
- IV. REPORTS
 - A. Developing Engagement Priorities
Scott Zdrazil, Senior Investment Officer
(Report dated March 16, 2018)
 - B. Procedures for Evaluating Prospective ESG-Related Divestments
Scott Zdrazil, Senior Investment Officer
(Report dated March 27, 2018)
- V. REPORT ON STAFF ACTION ITEMS

April 11, 2018

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VI. GOOD OF THE ORDER
(For Information Purposes Only)

VII. ADJOURNMENT

*The Board of Investments has adopted a policy permitting any member of the Board to attend a standing committee meeting open to the public. Members of the Board of Investments who are not members of the Committee may attend and participate in a meeting of a Committee but may not vote, make a motion, or second on any matter discussed at the meeting. The only action the Committee may take at the meeting is approval of a recommendation to take further action at a subsequent meeting of the Board.

**Although the meeting is scheduled for 8:00 a.m., it can start anytime thereafter, depending on the length of the Board of Investment meeting preceding it. Please be on call.

Documents subject to public disclosure that relate to an agenda item for an open session of the Board of Investments that are distributed to members of the Board of Investments less than 72 hours prior to the meeting will be available for public inspection at the time they are distributed to a majority of the Board of Investments Members at LACERA's offices at 300 N. Lake Avenue, Suite 820, Pasadena, CA 91101, during normal business hours of 9:00 a.m. to 5:00 p.m. Monday through Friday.

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REVISED AS OF MARCH 12, 2018

MINUTES OF THE SPECIAL MEETING OF THE CORPORATE GOVERNANCE

COMMITTEE OF THE BOARD OF INVESTMENTS*

LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION

300 N. LAKE AVENUE, SUITE 810, PASADENA, CA 91101

~~MONDAY~~WEDNESDAY, OCTOBER 11, 2017

PRESENT: Shawn Kehoe, Chair

Joseph Kelly

Herman Santos

David Green, Alternate

ABSENT: Valerie Villarreal, Vice Chair

MEMBERS AT LARGE: Michael Schneider

Wayne Moore

Michael Schneider

Ronald Okum

STAFF, ADVISORS, PARTICIPANTS

Jonathan Grabel, Chief Investment Officer

Scott Zdrazil, Senior Investment Officer

Meketa Investment Group

Leandro Festino, Managing Principal

Tim Filla, Vice President

I. CALL TO ORDER

The Meeting was called to order by Chair Kehoe at 8:00 a.m., in the Board Room of Gateway Plaza.

II. APPROVAL OF MINUTES

- A. Approval of the Minutes of the Special Meeting of the Corporate Governance Committee of the Board of Investments of September 11, 2017.

Mr. Santos made a motion, seconded by Mr. Kelly, to approve the minutes of the special meeting of September 11, 2017. The motion carried by unanimous vote.

III. PUBLIC COMMENT

There were no requests from the public to speak.

IV. CONSENT ITEMS

There were no Items.

V. NON-CONSENT AGENDA

A. None.

VI. REPORT

- A. Harmonizing *Corporate Governance Principles*: Select Topics for Committee Review and Clarification
Scott Zdrazil, Senior Investment Officer
(Memo dated September 25, 2017)

Mr. Zdrazil provided a presentation and answered questions from the Committee.

VII. REPORT OF STAFF ACTION ITEMS

VIII. GOOD OF THE ORDER
(For information purposes only)

There were no comments.

IX. ADJOURNMENT

There being no further business to come before the Board, the meeting was adjourned at 8:55 a.m.

~~*The Board of Investments has adopted a policy permitting any member of the Board to attend a standing committee meeting open to the public. In the event five (5) or more members of the Board of Investments (including members appointed to the Committee) are in attendance, the meeting shall constitute a joint meeting of the Committee and the Board of Investments.~~

MINUTES OF THE REGULAR MEETING OF THE CORPORATE GOVERNANCE
COMMITTEE AND THE BOARD OF INVESTMENTS

LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION

300 N. LAKE AVENUE, SUITE 810, PASADENA, CA 91101

WEDNESDAY, JANUARY 10, 2018

PRESENT: Shawn Kehoe, Chair

 Joseph Kelly

 Herman Santos

 David Green, Alternate

MEMBERS AT LARGE: Michael Schneider

 Wayne Moore

 Ronald Okum

 David Muir

 Gina Sanchez

STAFF, ADVISORS, PARTICIPANTS

Jonathan Grabel, Chief Investment Officer

Scott Zdrazil, Senior Investment Officer

Meketa Investment Group

Leandro Festino, Managing Principal

Tim Filla, Vice President

I. CALL TO ORDER

The Meeting was called to order by Chair Kehoe at 8:00 a.m., in the Board Room of Gateway Plaza.

II. APPROVAL OF MINUTES

A. Approval of the Minutes of the Regular Meeting of the Governance October 11, 2017.

Mr. Kehoe made a motion, seconded by Mr. Santos, to approve the minutes of the special meeting of October 11, 2017. The motion carried by unanimous vote.

III. PUBLIC COMMENT

There were no requests from the public to speak.

IV. NON-CONSENT ITEMS

A. Recommendation as submitted by Scott Zdrazil, Senior Investment Officer: That the Committee approve the Adoption of Consolidated *Corporate Governance Principles*. (Memo dated December 15, 2017)

Mr. Santos made a motion, seconded by Mr. Kelly, to approve the Adoption of Consolidated *Corporate Governance Principles*, with revisions to Item V.A. to incorporate reference to actuarial analysis and further review for clarity in wording. The motion carried by unanimous vote.

V. REPORT

A. LACERA's Public Market Managers' ESG Integration: Preliminary Analysis and Takeaways.

Scott Zdrazil, Senior Investment Officer
(Memo dated December 15, 2017)

Mr. Zdrazil provided a presentation and answered questions from the Committee.

January 10, 2018

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VI. REPORT ON STAFF ACTION ITEMS

There were no items to report.

VII. GOOD OF THE ORDER
(For information purposes only)

There were no comments.

VIII. ADJOURNMENT

There being no further business to come before the Committee, the meeting was adjourned at 8:30 a.m.

March 16, 2018

TO: Each Member
Corporate Governance Committee

FROM: Scott Zdrazil 
Senior Investment Officer

FOR: April 11, 2018 Corporate Governance Committee Meeting

SUBJECT: **DEVELOPING ENGAGEMENT PRIORITIES**

Please find attached a brief presentation that provides background information for Committee review and feedback regarding steps that LACERA might pursue to further develop capacity and priorities for active engagement of external parties, such as policy makers and portfolio companies, to promote practices aligned with LACERA's *Corporate Governance Principles*. These initiatives would further enhance LACERA's alignment with the UN Principles for Responsible Investment.

BACKGROUND

In 2016, LACERA adopted an *Investment Belief* stating that, "LACERA considers the risks of ESG factors as relevant to its investment process." The Corporate Governance Committee (Committee) of the Board of Investments (Board), over the past 15 months, has built from the Investment Belief related to environmental, social, and governance (ESG) factors to define principles and procedures to position LACERA to further operationalize and act on LACERA's *Investment Belief*:

- The Board approved refreshed and consolidated *Corporate Governance Principles* in February 2018.
- The Board approved the *Corporate Governance Policy*, August 2017, which consolidated and revised procedural guidance for corporate governance initiatives.

The Committee has also developed and provided feedback on several strategies to "put principles into practice" and act on its ESG *Investment Belief*, *Corporate Governance Principles*, and *Corporate Governance Policy*.

- The Board approved a consolidation and restructuring of global equities investment strategies in January 2018, which will enable LACERA to assume beneficial ownership rights for the targeted strategies, significantly expanding LACERA's proxy voting authority and application of its *Corporate Governance Principles* from approximately 20% of the global equities portfolio value to nearly 85%.

Each Member, Corporate Governance Committee

March 16, 2018

Page 2 of 2

- The Committee reviewed in January 2018 preliminary findings and strategies to assess external managers' approach to integrate ESG into their investment processes, starting with public markets (refinement remains ongoing).

The April Committee meeting will review the attached presentation which references LACERA's existing policy guidance defining engagement activities, provides context for LACERA's prospective actions, and presents several prospective actions for review and feedback.

Following Committee discussion, staff may formulate specific recommendations for Committee approval at an upcoming meeting.

Attachment

Noted and Reviewed:



Jonathan Grabel
Chief Investment Officer

Developing Engagement Priorities

Corporate Governance Committee

April 11, 2018

Scott Zdrazil

Senior Investment Officer – Corporate Governance

Discussion Outline

Policy guidance *defining engagement and guiding core program components*

Context *for developing engagement priorities*

Framework *defining prospective key focus areas*

- Sound public policy
- ESG data availability and quality
- Best practices advocacy
- Thought leadership

Policy Guidance: Defining Engagement

LACERA's approach to engagement defined and guided by LACERA policy

LACERA seeks to responsibly steward its investments in a manner that promotes and safeguards the economic interests of LACERA and its members, consistent with LACERA's mission to "produce, protect, and provide the promised benefits."

Through its corporate governance program, **LACERA prudently exercises its rights as an investor to support policies and practices at portfolio companies, as well as public policies governing financial markets, that are consistent with LACERA's economic interests in order to promote sustainable, long-term value** on behalf of LACERA's members and enhance LACERA's ability to fulfill its mission.

Corporate Governance Policy, Page 1
[emphasis added]



Policy Guidance: Core Program Components

LACERA's *Corporate Governance Policy* defines **four strategies** to collectively promote LACERA's *Corporate Governance Principles*:

Proxy Voting

"Proxy votes are plan assets, have value, and should be managed in a manner consistent with fiduciary duty and LACERA's interest in long-term value. LACERA exercises its voting rights for the exclusive benefit of LACERA's members. LACERA votes proxies of companies held in its U.S. and non-U.S. equity separate accounts, unless otherwise designated in the Investment Management Agreement, and in accordance with LACERA's *Corporate Governance Principles*."

Corporate Engagement

"LACERA advocates its *Investment Beliefs, Corporate Governance Principles*, and mission through dialogue and engagement strategies with portfolio companies, which may include exercising legal rights associated with LACERA's investments, such as sponsoring shareowner resolutions."

Public Policy

"LACERA represents its interests to policymakers, such as legislators, regulatory agencies, and standards-setting agencies, in line with its *Corporate Governance Principles*."*

Investor Collaboration

"LACERA collaborates with other public pension funds, asset owners and asset managers, both informally and formally through investor associations such as the Council of Institutional Investors, in order to enhance LACERA's ability to achieve its objectives and advance its *Corporate Governance Principles*."*

*Source: *Corporate Governance Policy*, Page 2



Context: Considerations for LACERA

The nature of LACERA's **public markets portfolio** and economic exposures should inform and shape LACERA's approach to engagement.

~10,000
global public market
portfolio companies

60
global markets

66.7%
passive equities exposure

0.02%
average ownership stake in each
company

“Universal Owner”

LACERA has a broad and diversified ownership across the marketplace, making LACERA exposed to and heavily reliant upon market “beta” (overall market performance).

Passive Mandates Mean Can't Easily Avoid Exposures

LACERA maintains prominent passive market exposure.

Long-Term Investment Horizon

LACERA has a vested interest in mitigating long-term risks and promoting sustainable economic performance.

Fractional Ownership

LACERA owns only a fraction of each company.

Finite Resources

Limited resources necessitate prioritizing key focus areas.

Context: Effective Partnerships and Approaches



- Collaboration** | Partnerships (both *formal* and *informal*) may enable individual investors to address collective challenges; may enhance LACERA's ability to achieve its objectives
- Credibility** | Maintaining credibility among companies and investors is key to having an impact
- Diplomacy** | Constructive, “quiet diplomacy” – based on LACERA's viewpoint as an investor and *owner* – may promote mutual understanding with companies and policymakers; improves prospects for success
- Focused Priorities** | Intentional and deliberate focus on key priorities with compelling prospects for success enhance LACERA's efficient use of resources and avoid diluting LACERA's impact; manageable workload

Framework to Define Engagement Focus

Pursue **partnerships** with other institutional investors to effectively promote market-wide practices in line with LACERA's *Corporate Governance Principles* focused on four key areas:





Public Policy: Recent Work

Policy Guidance

LACERA supports core rights and protections at portfolio companies and within financial market policies in order to safeguard its investments and foster a stable investment climate within the broader financial markets in which it invests. Financial rules and regulations should promote fair, orderly, and competitive markets and provide for investor protections.

Corporate Governance Principles, §II, Page 9

Numerous policymakers define governance standards

- Regulatory agencies
- Legislators
- Standards-setting agencies such as stock exchange listings standards, Public Company Accounting Standards Board (PCAOB), index providers, etc.

Procedures for initiatives

Corporate Governance Policy provides process for initiatives that are aligned with *Corporate Governance Principles* (Policy, §IV(C)v, Page 4)

Recent work (2017 to present) focused on joint letters

Includes joint investor letters through CII on policy-related topics, implemented under the *Corporate Governance Policy*:

- CII joint letter regarding SNAP IPO granting investors no voting rights
- Implementation of Dodd Frank provision requiring companies to disclose the ratio of CEO-to-median employee pay
- Joint letter to U.S. House of Representatives regarding proposed legislation relating to proxy advisory firms
- Joint letter to U.S. Senate regarding proposed legislation relating to proxy advisory firms and institutional investors

- References:
1. https://www.cii.org/files/issues_and_advocacy/correspondence/2017/02_03_17_SNAP_IPO.pdf
 2. https://www.cii.org/files/issues_and_advocacy/correspondence/2017/Attachment%20to%20December%2012.%202017%20Letter.pdf
 3. https://www.cii.org/files/issues_and_advocacy/correspondence/2018/Feb%2027-18%20Final%20Letter%20CII%20on%20proxy%20advisor%20legislation.pdf





Public Policy: In Development

Current policy work on governance issues, in conjunction with LACERA's partners, includes:

- Proxy advisor regulation
- Weighted voting rights/
Multi-class shares
- Mandatory arbitration
- Regulation of shareholder resolutions
- Corporate disclosures

Each topic is addressed in LACERA's *Corporate Governance Principles*.

Ensure clarity among LACERA “public policy” policies

- LACERA currently has three policies that address public policy initiatives:
 - *Corporate Governance Policy*
 - *Legislative Policy*
 - *BOR Engagement Policy*
- Staff developing forthcoming recommendations (in conjunction with Legal Office):
 - Ensure clarity by defining subject matter jurisdiction of each policy
 - Assess merit and value of BOI federal advocate
 - Ensure policies facilitate achieving objectives



Quality ESG Data: Integrate ESG Analytics

Policy Guidance

Financial markets work most efficiently when investors have timely, reliable, and comparable information about material aspects of a firm's performance. Transparency of a firm's key financial and operating performance is critical for investors to assess the firm's financial viability and prospects... LACERA supports clear and comprehensive disclosure of relevant financial and operating performance indicators (including environmental, social, and governance matters) that may provide valuable information for investors to assess a firm's prospects for delivering sustainable value.

Corporate Governance Principles, §IV, Page 19

Integrate ESG data analytics into LACERA's own Total Fund portfolio analytics:

- Build internal capacity to assess and monitor ESG factors and exposures.
- Both performance versus peers and benchmarks.
- Prospective attribution analyses as ESG data availability and quality improve.
- Consistent with previous Board presentations
 - Corporate Governance Committee January 2017 and October 2017.
 - Risk Committee March 2018 .

Sample Company Analysis



Sample Attribution Analysis

TVA Rating	Portfolio Weight Avg	Portfolio Return Base (%)	Benchmark Weight Avg (%)	Benchmark Return Base (%)	Active Weight Avg (%)	Attribution Allocation (%)	Attribution Selection (%)	Attribution Total (%)
TOTAL	100.00	-3.02	100.00	-2.76	0.00	0.02	-0.28	-0.26
A	17.94	-1.12	18.25	-0.91	-0.31	-0.01	-0.04	-0.04
AA	9.85	-6.26	10.20	-6.31	-0.35	0.01	0.00	0.02
AAA	5.03	-4.37	5.12	-4.46	-0.08	0.00	0.00	0.01
B	12.14	-4.98	11.25	-4.44	0.89	-0.02	-0.06	-0.08
BB	19.40	-1.03	19.30	-0.54	0.10	0.00	-0.09	-0.09
BBB	25.03	-2.78	25.06	-2.55	-0.03	0.00	-0.06	-0.05
CCC	9.80	-4.73	9.64	-4.93	0.16	0.00	0.02	0.02
Others	0.82	-8.93	1.19	-4.61	-0.37	0.02	-0.05	-0.03

Results show the portfolio underperformed the benchmark by 26 bps

Sample reports are for illustrative purposes only



Quality ESG Data: Partnerships to Improve

Policy Guidance

Financial markets work most efficiently when investors have timely, reliable, and comparable information about material aspects of a firm's performance. Transparency of a firm's key financial and operating performance is critical for investors to assess the firm's financial viability and prospects... LACERA supports clear and comprehensive disclosure of relevant financial and operating performance indicators **(including environmental, social, and governance matters)** that may provide valuable information for investors to assess a firm's prospects for delivering sustainable value.

Corporate Governance Principles, §IV, Page 19

The quality, comparability, and investor-relevance of corporate disclosures of environmental and social performance lag financial and governance disclosures.

Support Market Initiatives to Enhance ESG Data Quality and Availability

- **Sustainability Accounting Standards Board (SASB):** Staff assessing recommended affiliation, following May 2017 Committee presentation
- **Climate Risk:** Staff assessing investor initiatives to improve corporate disclosures of climate-related risks to enable investors to better assess and price climate risk, such as the Financial Stability Board's Task force on Climate-related Financial Disclosures (TCFD) and the related Climate Action 100+ initiative.





Best Practices: Board Diversity

Policy Guidance

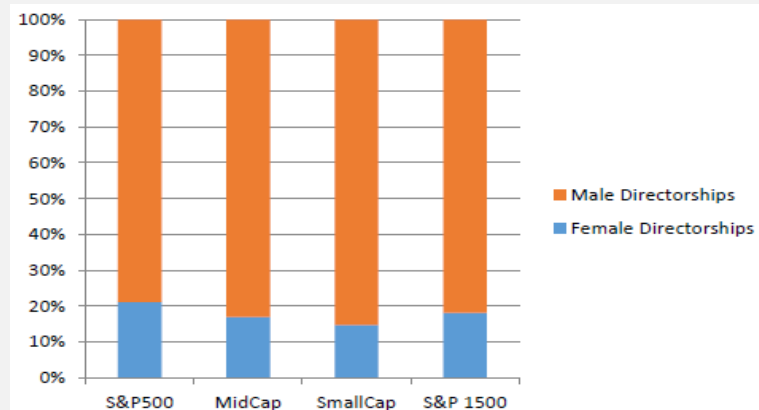
Diversity: The board should establish and disclose policies and processes for ensuring that it identifies and nominates suitable directors from a wide pool of candidates relevant to its business strategy, including, but not limited to, diverse gender, racial, and ethnic backgrounds. A diverse and inclusive board is better positioned to effectively deliberate and oversee business strategy in investors' interests.

Corporate Governance Principles, §I(B)2, Page 5

Partner with Select Public Funds to Engage Focused and Select Number of Portfolio Companies on Board Diversity:

- Growth in empirical research present correlations between gender diversity and firm performance.
- Recent focused investor attention to diversity, but progress remains slow.
- Staff developing steps to partner with select public funds to pursue targeted dialogues with portfolio companies that have few or no women on the board.

U.S. Directorships by Gender, 2016



Source: ISS 2017 Board Study: United States

References: Credit Suisse. *Gender Diversity and Corporate Performance*. August 2012. (<https://www.morganstanley.com/ideas/gender-diversity-investment-framework.html>); ISS. *2017 Board Study: United States*. (No link available.); MSCI. *The Tipping Point: Women on Boards and Financial Performance*. 2016 (<https://www.msci.com/www/research-paper/the-tipping-point-women-on/0538947986>); MSCI. *Women on Boards*. November 2015. (<https://www.msci.com/www/research-paper/research-insight-women-on/0263428390>); Spencer Stuart. *U.S Board Index 2017*. (https://www.spencerstuart.com/-/media/ssbi2017/ssbi_2017_final.pdf?la=en).



Next Steps and Resources

Ensure resources are aligned with objectives and “fit for purpose”

Summary of Forthcoming Steps and Recommendations in Development:

1. Clarify LACERA’s three policies addressing public policy matters to ensure delineated subject matter jurisdiction (with Legal Office).
2. Source ESG data analytics to integrate ESG into Total Fund portfolio analytics.
3. Develop recommendations on specific initiatives to enhance the quality and availability of investment-relevant ESG data.
4. Develop focused engagement to promote board diversity, in line with available resources.
5. Assess adequacy of staffing and other resources.

Appendix

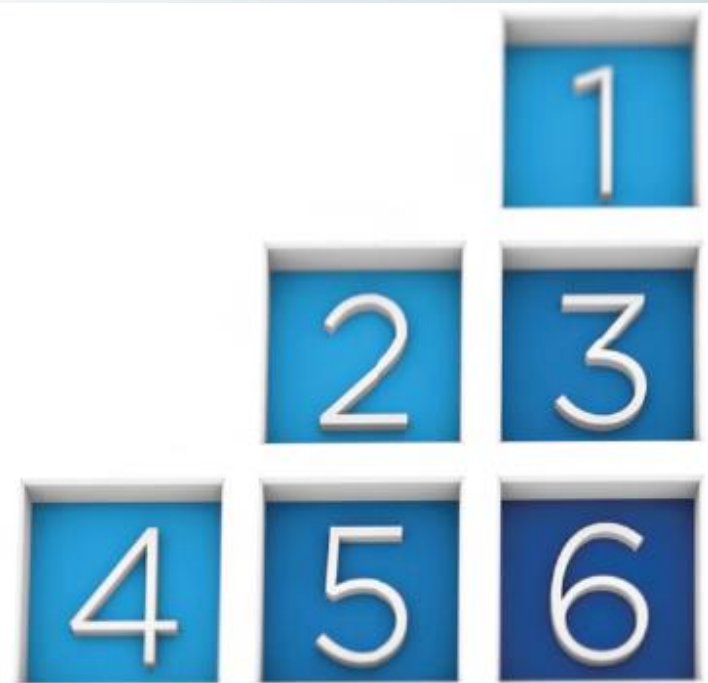


Prospective Steps Further Align LACERA to PRI

Outlined Steps
Would Further
LACERA's Alignment
with Principles 2, 3, and 5
of the PRI

Principles for Responsible Investment

- 1 We will incorporate ESG issues into investment analysis and decision-making processes.
- 2 We will be active owners and incorporate ESG issues into our ownership policies and practices
- 3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- 4 We will promote acceptance and implementation of the Principles within the investment industry.
- 5 We will work together to enhance our effectiveness in implementing the Principles.
- 6 We will each report on our activities and progress towards implementing the Principles.




LACERA is a signatory to the UN-affiliated Principles for Responsible Investment (www.unpri.org).



March 27, 2018

TO: Each Member
Corporate Governance Committee

FROM: Jonathan Grabel 
Chief Executive Officer

Scott Zdrazil 
Senior Investment Officer

FOR: April 11, 2018 Corporate Governance Committee Meeting

SUBJECT: **PROCEDURES FOR EVALUATING PROSPECTIVE ESG-RELATED
DIVESTMENTS**

The following memo presents an informational overview of LACERA's existing policies and procedures to assess requests for divestment and status of current policies on economic substitution. Please find attached LACERA's *Corporate Governance Policy*, Appendix A entitled "Procedures for Evaluating Prospective ESG-Related Divestments." The Corporate Governance Committee requested a review of the current process for evaluating divestment requests.

BACKGROUND

LACERA's current process for evaluating prospective ESG-related divestment requests is outlined in LACERA's *Corporate Governance Policy*, with the Appendix A: Procedures for Evaluating Prospective ESG-Related Divestments" (the "Policy Procedures") outlined on pages 6-7 (**Attachment**).

The Policy Procedures prescribes a formal, 15-step process by which the Board reviews its public market exposures to certain issues of concern for prospective investment restrictions, such as economic substitution. Prior to this policy and process, LACERA evaluated divestment requests on an ad-hoc basis which resulted in the current policies relating to public markets separate account mandates and the economic substitution practice for tobacco, Iran- and Sudan-related exposures.

The Policy Procedures were first developed by the Corporate Governance Committee in August 2013 and adopted by the Board of Investments in November 2014. The formal 15-step process was most recently re-approved by the Board in August 2017, when the broader Corporate Governance Policy and the Appendix's introductory language were modified, while the defined 15-step process described therein was unaltered.

Attachment

CORPORATE GOVERNANCE POLICY

I. Purpose

The Corporate Governance Policy (Policy) outlines the objectives, legal authority, and procedures guiding LACERA's corporate governance program.

II. Strategic Objective

LACERA seeks to responsibly steward its investments in a manner that promotes and safeguards the economic interests of LACERA and its members, consistent with LACERA's mission to "produce, protect, and provide the promised benefits."

Through its corporate governance program, LACERA prudently exercises its rights as an investor to support policies and practices at portfolio companies, as well as public policies governing financial markets, that are consistent with LACERA's economic interests in order to promote sustainable, long-term value on behalf of LACERA's members and enhance LACERA's ability to fulfill its mission.

III. Legal Authority

The LACERA Board of Investments has "the sole and exclusive fiduciary responsibility over the assets of" the system, as provided by the California Constitution (Article XVI, Section 17(a)). LACERA exercises its legal rights on corporate governance matters in furtherance of its fiduciary duty under Article XVI, Section 17 of the California Constitution, the County Employees Retirement Law of 1937 (CERL), and other governing laws, regulations, and case authority. The Board's fiduciary duty has two components:

- A. **Duty of Loyalty.** Under the duty of loyalty, Board members have the sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. (Article XVI, Section 17(a).) Board members shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. (CERL Section 31595(a).) The Board's duty to participants and their beneficiaries shall take precedence over any other duty. (Article XVI, Section 17(b).)
- B. **Duty of Prudence.** Under the duty of prudence, Board members shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims. (Article XVI, Section 17(c); CERL Section 31595(b).) "[T]he Board may, in its discretion, invest or delegate the authority to invest, the assets of the fund through the purchase, holding, or sale of any form or type of investment, financial instrument, or financial transaction when prudent in the informed opinion of the Board." (CERL Section

31595.) Further, the Board "[s]hall diversify the investments of the system so as to minimize risk of loss and to maximize the rate of return, unless under the circumstances it is clearly prudent not to do so." (CERL Section 31595(c).)

The fiduciary obligations of prudence and loyalty to plan participants and beneficiaries compel and guide LACERA's corporate governance activities. LACERA's fiduciary duties extend to, but are not limited to, prudently managing its proxy votes, vigilantly monitoring and diligently mitigating risks to the value of its investments, and judiciously determining action in order to assist in the effective administration of the fund and promote the interest of members and their beneficiaries.

IV. Program Components

LACERA's corporate governance program may include the following components and responsibilities:

A. Proxy Voting

Proxy votes are plan assets, have value, and should be managed in a manner consistent with fiduciary duty and LACERA's interest in long-term value. LACERA exercises its voting rights for the exclusive benefit of LACERA's members. LACERA votes proxies of companies held in its U.S. and non-U.S. equity separate accounts, unless otherwise designated in the Investment Management Agreement, and in accordance with LACERA's *Corporate Governance Principles*.

LACERA participates in securities lending to earn incremental income, per LACERA's "Securities Lending Program Policy." In securities lending, the legal rights accorded those shares, including proxy voting, are transferred to the borrower of the securities during the period the securities are on loan. As a result, LACERA forfeits its right to vote proxies on loaned securities unless those shares have been recalled from the borrower no later than the share's record date.

B. Corporate Engagement

LACERA advocates its *Investment Beliefs, Corporate Governance Principles*, and mission through dialogue and engagement strategies with portfolio companies, which may include exercising legal rights associated with LACERA's investments, such as sponsoring shareowner resolutions.

C. Public Policy

LACERA represents its interests to policymakers, such as legislators, regulatory agencies, and standards-setting agencies, in line with its *Corporate Governance Principles*.

D. Investor Collaboration

LACERA collaborates with other public pension funds, asset owners and asset managers, both informally and formally through investor associations such as the Council of Institutional Investors, in order to enhance LACERA's ability to achieve its objectives and advance its *Corporate Governance Principles*.

V. Responsibilities and Delegations

A. The Board of Investments:

- (i.) Approves and promulgates policies addressing environmental, social, and governance issues, such as corporate governance and proxy voting matters and including but not limited to *Corporate Governance Principles* and this *Corporate Governance Policy*, as recommended by the Corporate Governance Committee of the Board.
- (ii.) Receives periodic reports concerning the program's progress and priorities from the Corporate Governance Committee.
- (iii.) Approves LACERA representatives for nomination to governing bodies of the corporate governance associations to which LACERA is affiliated, as recommended by the Corporate Governance Committee.
- (iv.) Approves procedures to comply with legislated or other mandated divestment or investment exclusions, such as LACERA's *Procedures for Evaluating ESG-Related Divestments* (Appendix A), as developed and recommended by the Corporate Governance Committee.

B. The Corporate Governance Committee of the Board of Investments:

- (i.) Recommends the *Corporate Governance Principles*, the *Corporate Governance Policy*, and other items concerning environmental, social, and governance matters to the Board of Investments for consideration and approval.
- (ii.) Exercises oversight and monitoring of the corporate governance program, including reviewing program priorities and progress.
- (iii.) Reviews reports regarding proxy voting results and trends and develops recommendations for Board approval for any policy recommendations, as appropriate.
- (iv.) Reviews and ensures alignment of strategic initiatives with the *Corporate Governance Principles*.
- (v.) Provides periodic reports on the program to the Board of Investments.
- (vi.) Delegates authority to the Committee Chair to determine LACERA's action on time-sensitive legislative or regulatory matters that are not adequately addressed in the *Corporate Governance Principles* or joint investor engagements affiliated with investor associations to which LACERA has formally affiliated.
- (vii.) Recommends for Board of Investment approval, LACERA representatives for nomination to governing bodies of the corporate governance associations to which LACERA is affiliated. In event the Committee is not scheduled to meet or lacks adequate time to recommend a nomination to the Board prior to a formal deadline, the

Committee delegates authority to the Committee Chair to recommend consideration of the nomination by the Board.

- (viii.) Recommends for Board of Investment approval, time-permitting, LACERA's votes in support or opposition of candidates listed on a formal member ballot and nominated to a governing board of an investor association to which LACERA has formally affiliated. In event the Committee is not scheduled to meet or lacks adequate time to agendaize under the Brown Act a recommendation to the Board for vote determinations prior to a formal deadline, the Committee delegates authority to the Committee Chair to recommend consideration by the Board, time-permitting, of the votes in support or opposition of board candidates. In time-sensitive circumstances where vote deadlines do not permit such vote considerations by the Committee or the Board, the Committee delegates authority to the Committee Chair to consult with staff per Section V(C)(vi.) below on votes.

C. Staff

- (i.) Develops and recommends *Corporate Governance Principles* and related policies for review and consideration by the Corporate Governance Committee.
- (ii.) Executes proxy votes in adherence to the *Corporate Governance Principles*. Staff consults with and seeks the input of the Chief Investment Officer and Chief Counsel, when applicable, to apply the *Corporate Governance Principles*, and the spirit thereof, to unique or new proxy voting items in their best judgment and interpretation of the *Corporate Governance Principles*. Staff recalls shares of loaned securities when doing so is in LACERA's economic interests, such as at portfolio companies where LACERA has sponsored a shareowner proposal.
- (iii.) Communicates and represents the *Corporate Governance Principles* in dialogues and communication with portfolio companies, other investors and stakeholders, related conferences, and other interested parties.
- (iv.) Presents any strategic plans for engagement to the Corporate Governance Committee, per the Committee's review and oversight, to promote alignment with Board-approved *Corporate Governance Principles*. In the event of time-sensitive strategic initiatives, staff consults with the Chair of the Committee, who determines action or recommends consideration of the matter by the Committee or Board, time-permitting.
- (v.) Represents the *Corporate Governance Principles* in written communication to legislators and regulatory agencies, in consultation with the Chief Executive Officer, Chief Investment Officer, and Chief Counsel. Staff may participate in joint investor written communications that are organized as part of formal investor associations to which LACERA has formally affiliated. In event that a time-sensitive legislative or regulatory matter arises that is not adequately considered by the *Corporate Governance Principles* or being addressed by an investor association to which LACERA is affiliated, staff consults with the Chair of the Committee, who determines whether to approve action or recommend consideration of the matter by the Board, time-permitting.

- (vi.) Represents LACERA and its *Corporate Governance Principles* at investor associations, including managing membership surveys, business meeting votes (other than selecting which candidates to a governing board to support or oppose), and other operational interactions, in adherence to the *Corporate Governance Principles* and the spirit thereof, in its best judgment and interpretation. In event that a time-sensitive vote arises on a unique item or an issue that is not adequately considered by the *Corporate Governance Principles*, as well as for governance-related investor associations' formal business meeting ballot items pertaining to support or opposition of candidates to a governing board, and time constraints prohibit such items from being presented to the Committee or Board for consideration, staff may determine a vote in consultation with the Chair of the Committee.

VI. Regular Review and Reaffirmation

LACERA reviews and reaffirms this Policy at least every three years in order to ensure its alignment with LACERA's mission and objectives and in light of evolving market practices on corporate governance, environmental, social, and governance ("ESG"), and responsible investment matters.

APPENDIX A: Procedures for Evaluating Prospective ESG-Related Divestments

As stated in LACERA's *Investment Beliefs*, "LACERA operates in a global financial marketplace, and as such, LACERA believes that in order to diversify its risk broadly, it is vital that LACERA possess a global perspective. Diversification across different risk factors is necessary for risk reduction."

As a diversified, global investor, LACERA is periodically requested to review its public markets investment exposures to certain issues arising from environmental, social, or governance concerns. It is generally the preference of LACERA, in order to promote diversification and minimize risk, to engage rather than divest investment holdings concerning risks to long-term value. However, in order to address prospective divestment issues and identify LACERA's exposure to exogenous risks related to environmental, social, or governance issues and not addressed elsewhere in the *Investment Policy Statement*, the following formal process has been adopted:

1. The issue will be directed to Committee for further direction to Staff.
2. If the Committee decides to review the issue, Staff will assess the potential economic and reputational impact of the issue on LACERA.
 - a. Does the issue violate LACERA's *Corporate Governance Principles*?
 - b. Determine criteria for identification of investment(s).
 - c. Preliminary identification of the investment.
 - d. Preliminary estimate on size of the investment.
 - e. Seriousness of the issue/violation and whether it impacts the economics of the investment(s).
 - f. Consultation with LACERA's CEO, CIO, and legal counsel.
3. Staff will report its findings on the potential economic and reputational impact of the issue on LACERA to the Committee.
4. The Committee may forward the issue and potential economic and reputational impact on LACERA to the Board of Investments (Board) for further direction.
5. If the Board directs staff to continue the analysis, staff will calculate the anticipated resources involved in analyzing the issue including, but not limited to:
 - a. Estimate of staff hours required for research and analysis.
 - b. Estimate of the resource impact on current staff initiatives and projects (for example the delay in an RFP search).
 - c. Estimate of cost to obtain information (e.g.: company list) from external service provider.
6. Staff will report back to the Committee with its resource requirements analysis.
7. Committee may make recommendation to the Board to pursue additional analysis.
8. Upon receiving direction from the Board, Staff will contract with external data provider to identify investment(s) impacted by the issue.

9. Staff will identify investment exposures within the separate accounts of the public markets asset classes (equities, fixed income and commodities).
10. Staff will contact external investment managers to solicit feedback from portfolio managers on reasoning for the investment and potential return and risk trade-off of economic substitution.
11. Staff will present findings to the Board and any recommendation(s) as necessary. If further action is warranted, such as engagement with companies, staff's report to the Board will include the following:
 - a. An estimate of additional staff hours needed to execute engagement.
 - b. An estimate of the impact of diverting resources from current staff initiatives and projects (for example the delay in an RFP search).
 - c. Cost of retaining external resources (3rd party consultant) to assist in the engagement process.
 - d. Feedback from portfolio managers on their investment in the company.
 - e. Discussion of criteria and terms for company engagement.
12. If further action, such as engagement, is recommended and approved by the Board, staff will seek to engage with companies on the issue. Letters will be written to the company's executive management and their boards requesting responses within 60 days.
13. If company response is determined to be insufficient, staff will assess the need to place the company on an economic substitution list¹ and present recommendation(s) to the Board for approval. Included in the recommendation(s) will be the following:
 - a. Updated company exposure within separate accounts of public markets asset classes.
 - b. Annual cost to procure company list.
 - c. Criteria by which company will be removed from the economic substitution list.
14. Staff will continuously monitor company status relative to criteria for removal from the economic substitution list. Once criteria have been met, staff will recommend removal of the company to the Board.
15. Staff will provide an economic substitution list update to the Board annually which will include the following:
 - a. All companies currently on the list.
 - b. Issue for which the company was placed on the list.
 - c. Investment exposure within separate accounts of public markets asset classes.
 - d. Current status of mitigating factors.

Revised and Reviewed: August 9, 2017

Reviewed: October 12, 2016

Revised: November 19, 2014

¹ Companies on the list will be covered by the following investment guideline policy language: "Investment managers should refrain from purchasing securities on the economic substitution list when the same investment goals concerning risk, return, and diversification can be achieved through the purchase of another security."