San Joaquin County Employees Retirement Association

A G E N D A

SPECIAL MEETING
SAN JOAQUIN COUNTY EMPLOYEES RETIREMENT ASSOCIATION
BOARD OF RETIREMENT
FRIDAY, SEPTEMBER 1, 2023
AT 9:00 AM

Location: San Joaquin County Agricultural Center 2101 E. Earhart Avenue, Stockton, CA 95206

Persons who require disability-related accommodations should contact SJCERA at (209) 468-9950 or ElainaP@sjcera.org at least forty-eight (48) hours prior to the scheduled meeting time.

1.0 ROLL CALL

2.0 PLEDGE OF ALLEGIANCE

3.0 PUBLIC COMMENT

3.01 The public is welcome to address the Board during this time on matters within the Board's jurisdiction and are encouraged to complete a Public Comment form, which can be found near the entry to the room. Speakers are limited to three minutes, and are expected to be civil and courteous. Public comment on items listed on the agenda may be heard at this time, or when the item is called, at the discretion of the Chair.

Except as otherwise permitted by the Ralph M. Brown Act (California Government Code Sections 54950 et seq.), no deliberation, discussion or action may be taken by the Board on items not listed on the agenda. Members of the Board may, but are not required to: (1) briefly respond to statements made or questions posed by persons addressing the Board; (2) ask a brief question for clarification; or (3) refer the matter to staff for further information.

4.0 ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG) INVESTING AND PROXY VOTING

4.01 Fiduciary Considerations for ESG Investing and Proxy Voting

01 Presented by Ashley Dunning of Nossaman, LLP 3

4.02 Investment Considerations for ESG Investing and Proxy Voting

01 Presented by David Sancewich of Meketa Investment Group 18

4.03 ESG and Proxy Voting Discussion

01 Ashley Dunning of Nossaman, LLP to facilitate a Board discussion to define and document the Board's approach to ESG and Proxy Voting

4.04 Board to review, discuss and give direction to staff and consultants as appropriate

5.0 COMMENTS

5.01 Comments from the Board of Retirement

6.0 CALENDAR

6.01 Board Meeting September 8, 2023 at 9:00 a.m.

6.02 Board Meeting October 11, 2023 at 9:00 a.m.

6.03 Investment Roundtable October 12, 2023, at 8:00 a.m.

6.04 Board Meeting November 3, 2023 at 9:00 a.m.

7.0 ADJOURNMENT

Ashley Dunning
Partner

Fiduciary Considerations for “ESG” Investing and Proxy Voting

Presentation to the Board of Retirement
San Joaquin County Employees’ Retirement Association

September 1, 2023

NOSSAMAN LLP

Overview

- What is “ESG” Investing?
- Fiduciary standards applicable to California public pension plans.
- Fiduciary considerations particular to ESG investing.
- Department of Labor (DOL) guidance to plans governed by the Employee Retirement Income Security Act of 1974 (ERISA).
    - SJCERA is exempt from ERISA, but governmental plans sometimes look to DOL rules for guidance.
- Summary and next steps for SJCERA re ESG investing.

What is ESG Investing?

- Environmental-Social-Governance (ESG) Investing:
  - Use of factors that consider environmental footprint, social impacts and/or corporate governance.
  - Ranges from minimal (applying ESG factors to inform economic analysis) to direct (applying ESG screens or selecting only ESG-specific funds in designated investment options (i.e. economically targeted investments ("ETIs")).

Fiduciary Standards Applicable to Public Pension Plans Under California Law

- Duty of Care
- Duty of Loyalty

Fiduciary Duty of Care

- **Prudent Expert Rule**: make decisions that a prudent person acting in like capacity, familiar with these matters would use.

- **Duty to Assure Competency of Retirement System Assets.**

- **Duty to Monitor** and take corrective action.

- **Duty to Consult with Experts** to make informed investment judgments [such as legal, actuarial and investment counsel].
    - Demonstrate an informed, reasonable, and prudent rationale for failing to follow guidance.

Fiduciary Duty of Loyalty

- **Exclusive Benefit Rule**: use trust fund only to provide retirement and related benefits as provided by the plan, and defray reasonable administrative expenses.

- **Primary Duty Rule:** duty to participants/beneficiaries takes precedence over any other duty.

- **No "dual loyalties":** trustees aren't "agents" for the party that appointed or elected them.

- **No collateral interests:** trustee's personal views concerning social or political issues or causes shouldn't be basis of decisions.

Fiduciary Duties of Care and Loyalty as to *Investments* under California Law

- **Diversification mandate**
  - Board of Retirement required to diversify the investments to minimize the risk of loss and to maximize the rate of return, *unless under the circumstances it is clearly not prudent to do so*.

- **Divestment-related rules**
  - Legislature may prohibit certain investments by a retirement board where it is in the public interest to do so, *if that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board.*

Fiduciary Considerations In ESG Investing

- **Common thread:**
  - Social interests may be advanced through investments by fiduciaries only if the interests of trust beneficiaries *are not compromised*.
    - Interest of trust beneficiaries: *risk-adjusted returns used to fund benefits provided by SJCERA.*

Background of DOL ESG Rule for Plans Governed by ERISA (not binding on SJCERA)

- Guidance fluctuated over time:
  - ETIs were not “inherently incompatible” with ERISA’s fiduciary obligations, to “all things being equal” tie-breaker test, to “financial factors” rule with extra documentation requirement, to prioritization of creation of well-paying union jobs and bolstering environmental sustainability.
  - DOL uniformly cautioned, however, against reduced returns or greater risks to secure ESG goals.

DOL Recent Final Rule re ESG Investing By ERISA fiduciaries (not binding on SJCERA)

- "Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights" (effective 1/30/2023).
  - Removes "pecuniary/non-pecuniary" concepts.
  - ESG considerations can be weighed *so long as fiduciary reasonably determines they are relevant to risk and return analysis*.
  - Removes special regulatory documentation requirement.
- Pending litigation in other states challenges this rule, but it is currently in effect for plans that are subject to ERISA.

Legislative Actions Regarding ESG Factors

- State legislatures throughout the country have considered, and some cases enacted, bills either *prohibiting or requiring* the consideration of some or all such factors.
  - Implementation of such mandates typically, but not always, contains a “fiduciary savings clause” allowing trustees to consider whether complying with the governmental mandate would be consistent with their fiduciaries duties of care and loyalty.
- In California, most divestment legislation, which typically seeks to address an environmental, social or governance-related topic, has been directed at state, rather than county or city, retirement systems.

Range of Ways to Consider ESG Factors and Fiduciary Duties

Am I keeping my personal or political views separate from my decision?

What's in the best long-term interest of members in the security of their SJCERA benefits?

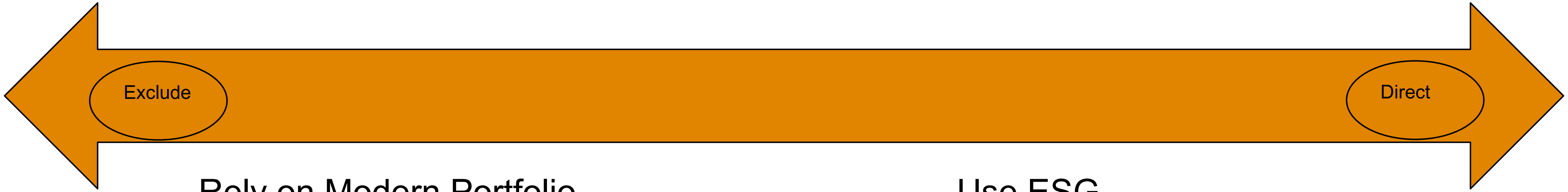
How does performance compare to other investments?

Am I keeping my decision independent from opinions of those who put me in office?

What does investment consultant recommend and why?

Will ESG factors likely affect long-term performance?

Will investment approach diversify portfolio to maximize return, minimize losses?



Rely on Modern Portfolio Theory without explicit ESG directions

Use ESG factors to inform economic analysis

Require certain ESG screens

Exclude ESG factors from decisions

Develop investment beliefs regarding one or more ESG factors

Select only ESG-specific funds

Next Steps in Fiduciary Compliance re ESG

- SJCERA Board has broad (but not absolute) discretion; avoid abuse of discretion.
  - **Process is important** – record should reflect that prudent process: minutes reflecting deliberation, written materials provided by experts.
  - **Rationale for decision-making is important** – explain reasons for actions that reflect goal of serving overall best interest of members and beneficiaries in the security of their SJCERA benefits.
  - **Expert advice regarding prudence is important** – obtain independent investment oversight, including determination by experts that SJCERA may reasonably anticipate equal or better returns, with same or less risk to portfolio, from investments that do, or do not, consider environmental, social and/or governance related risks.

Questions?

Thank You

Ashley K. Dunning, SJCERA Fiduciary and Acting General Counsel
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MEKETA | 45 YEARS
CELEBRATING A MILESTONE

San Joaquin County Employees' Retirement Association

September 2023

ESG Investing

What is ESG

→ The institutional investor market has become increasingly attentive to the potential material impact of ESG factors on investment performance.

→ ESG investing refers to the use of Environmental, Social, and Governance factors in investment decision making and management

ENVIRONMENTAL (E)
Climate Change | Energy Transition | Sustainability Best Practices | Environment Policy | Water Supply | Sustainable Transport | Waste Management

SOCIAL (S)
Consumer Rights | Health and Safety | Product Safety | Labor Relations | Community Relations | Stakeholder Relations

GOVERNANCE (G)
Board Structure | Board Diversity | Independent Directors | Chairman/CEO Split | Executive Pay | Audit/Accounting | Shareholder Rights

What is ESG Investing?

→ Integration of Environmental, Social, and Governance ("ESG") factors into investment decision making.

→ ESG criteria can generate long-term competitive financial returns and have a positive social impact.

→ ESG considerations may be reflected in:

- Investment policy
- Asset allocation
- Manager or fund selection
- Security selection

→ ESG Investing is synonymous with Responsible Investment ("RI") and focuses on investment value.

→ Social Responsible Investment ("SRI"), in contrast, may be more focused on investor values.

ESG In Investment Management

ESG investing refers to the use of Environmental, Social, and Governance factors in investment decision making and management.

→ Also called Sustainable, Impact, and Socially Responsible Investing.

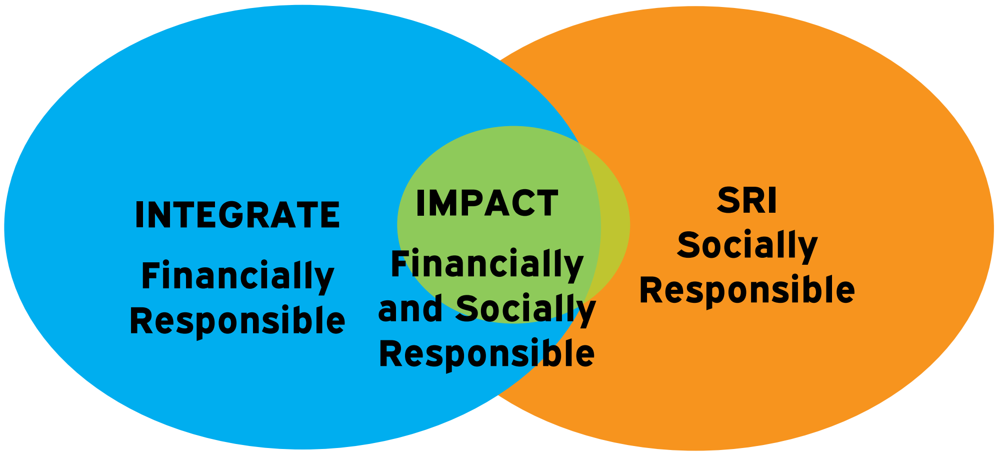
- $17.1 trillion at the start of 2020 in the United States, up from $8.7 trillion in 2016 (US SIF ((Sustainable Investment Forum)) 2020 report).

→ From 2018 through the first half of 2020,

- 149 institutional investors (public pension funds, endowments, foundations, and other institutions) and
- 56 investment managers controlling $1.98 trillion in assets under management ("AUM"), led or co-led shareholder resolutions on ESG issues.

ESG Investment Management Strategies

→ In general investment ESG goals may be broadly categorized in three general types:



Integrate

→ Evaluate and integrate material ESG factors to improve the long-term risk-adjusted return of a portfolio, with no explicit, quantifiable, ESG goals.

Impact

→ Identify specific ESG factors to adjust an investment portfolio to generate specific quantifiable ESG impacts and meet or exceed market risk-adjusted return benchmarks.

Socially Responsible Investing ("SRI")

→ Identify specific ESG factors, typically through positive and/or negative screens, to generate or influence a specific ESG, ethical, or social value, with no explicit regard for the financial returns to the portfolio

ESG Issues

→ No single definition of the ESG issues

→ Definition will continue to evolve

→ Table below, prepared by the CFA Institute, indicates current focus:

Environmental Issues	Social Issues	Governance Issues
Climate change and carbon emissions	Customer satisfaction	Board composition
Air and water pollution	Data protection and privacy	Audit committee structure
Biodiversity	Gender and diversity	Bribery and corruption
Deforestation	Employee engagement	Executive compensation
Energy efficiency	Community relations	Lobbying
Waste Management	Human Rights	Political contributions
Water scarcity	Labor standards	Whistleblower schemes

→ ESG factors are seen as having long term impact on investment risk or return

→ Integration with traditional investment analysis varies across managers and factors

ESG Adoption

→ 85% of CFA Institute survey respondents systematically include some ESG factors in investment analysis and decision making.

→ Most frequent focus is Governance. Board Accountability, human capital, and environmental degradation are currently seen as the issues with the greatest financial impact.

→ Executive compensation, board accountability, environmental degradation, and climate change are the most frequently sited areas for shareholder engagement[2].

→ DOL guidance permits integration of ESG factors with a well-articulated and defensible investment foundation.

→ Client demand as a motivation for investment organizations to consider ESG factors increased significantly in the last three years. Demand as a motivator was highest in the Americas region (65%), an increase of 20% since 2017[1].

1 Based on responses to 2020 CFA Institute ESG Survey of Investment Professionals.
2 Based on responses to 2017 CFA Institute ESG Survey of Investment Professionals.

ESG Investing in Practice

→ No single "right" way to integrate ESG into investments

→ The selected path to ESG integration should reflect the unique needs, circumstances, and investment beliefs of the client

→ This is consistent with other investment decisions – the client's context matters

Five Major Approaches

- ESG Integration – part of investment analysis and decision making
- Negative or Exclusionary Screens – exclude 'prohibited' securities
- "Best in class" investing – adjust for ESG characteristics
- Shareholder engagement and active ownership – focus on stewardship
- Impact and thematic investments – focus on investments that reflect ESG concerns

Implementation

→ ESG approaches vary widely among institutional asset owners, shaped by:

- Type of institution, such as pension fund, endowment, foundation, or faith-based entity.
- Regulatory frameworks across geographies, from Europe to U.S. to Canada, and among states and municipalities within the U.S.

→ For the most part, U.S. public pension plans have not been demonstrably active on ESG. Among those active, there is no one 'right' approach to ESG.

→ The fiduciary responsibility that underpins U.S. public pension plans helps frame their ESG approaches.

→ In contrast to a faith-based organization, endowment or foundation, that might seek to pursue SRI investing without explicit regard for the risk-adjusted returns of their investments, U.S. public pension plans fiduciary responsibility is to its beneficiaries.

Expanded Participation in the UN-PRI Supports Broader ESG Adoption

→ The United Nations Principles for Responsible Investment were launched in 2006.

→ In the first half of 2020 the number of signatories, including Meketa Investment Group, grew by 28%, to more than 3,000 signatories, and the assets under management grew 20% to more than $100 trillion[1].

→ Signatories agree to six principles:

- Incorporate ESG issues into investment analysis and decision-making processes.
- Be active owners and incorporate ESG issues into ownership policies and practices.
- Seek appropriate disclosure on ESG issues by the entities in which we invest.
- Promote acceptance and implementation of the Principles within the investment industry.
- Work together to enhance effectiveness in implementing the Principles.
- Report on our activities and progress towards implementing the Principles.

→ The Principles provide a voluntary framework by which all investors can incorporate ESG factors into their decision-making and ownership practices and so better align their objectives with those of society at large.

1 Source: CFA Institute: Future of Sustainability in Investment Management: From Ideas to Reality.

Sample U.S. Public Pension Plan ESG Implementation												
			Investment Policy		Asset Allocation	Manager Selection		Monitor	Engagement			
Pension Plan	State	Total AUM ($ Billions)	Beliefs	Policy	Climate Scenario Analysis	Integrate	Impact	Managers and Portfolio	Proxy Voting Policy	Regulatory	Managers	Companies
CalPERS	CA	444	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
CalSTRS	CA	309	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
NYSCRF	NY	268	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
FSBA	FL	200	No	No	No	No	No	No	No	No	No	No
NCRS	NC	107	No	No	No	No	No	No	No	No	No	No
LACERA	CA	72	Yes	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes
MSRPS	MD	68	No	Yes	Yes	Yes	No	Yes	Yes	No	Yes	No
IPERS	IA	43	No	No	No	No	No	No	No**	No	No	No
SCRS	SC	37	No	No	No	No	No	No	No	No	No	No
INPRS	IN	37	No	No	No	No	No	No	No	No	No	No
SFERS	CA	35	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes
DCRB	DC	11	No	Yes	No	Yes	No	Yes	Yes	No	Yes	No
MOSERS	MO	10	No	No	No	No	No	No	No***	No	No	No
SJERS	CA	8	No	No	No	No	Yes	No	No	No	No	No
MEABF	IL	4	No	Yes	No	No	No	Yes	No	No	No	No
EBMUD	CA	2	No	Yes	No	No	No	No	Yes	Yes	Yes	No

* Meketa gathered the information in this table from public information on asset owner websites. Additional information for some funds was gathered from direct contact with staff.

**According to its IPS, IPERS shall periodically review each investment manager's proxy voting policy and its compliance with such policies.

***According to its IPS, MOSERS CIO will establish a proxy voting policy, if and when participating in proxy voting, which ensures that the interests of the System are adequately protected.

Manager ESG Evaluation

→ Meketa evaluates the following for each investment manager, taking ESG considerations into account at each level:

- Organizational structure and culture
- The strategy's investment philosophy and process
- The quality of the investment team
- Investment performance over multiple time horizons
- Investment vehicles and fees

Regulatory Environments

→ ESG regulatory environments differ considerably geographically

→ Geographic differences have shaped the development of ESG in different markets, with much greater adoption of ESG integration into investment products in Europe than the U.S. to date.

- European and the UK markets were early movers in sustainability regulations.
- In the U.S., the SEC has begun implementing new rules to help ensure consistent information is provided to investors. In addition, the SEC has set up a task force to enforce current guidelines regarding marketing and disclaimers etc.

Investment Tools

→ U.S. public pension funds that have adopted ESG initiatives rely on investment tools available generally to institutional asset owners and implement ESG initiatives within the constraints of their fiduciary responsibilities.

- ESG investment tools may include:
- Investments
- Proxy Voting
- Engagement with Regulators, Asset Managers, and Companies
- Participation in Active Ownership Investment Campaigns
- Investment approaches may encompass any or all of the following aspects of a portfolio's investment strategy

Conclusion

→ ESG Investing is focused on creating value in an investment program

→ Focuses on integrating E, S, & G factors into investment decision making

→ Investor's goal may be to:

- Better control investment risk
- Potentially enhance long term investment returns
- No one size fits all approach

→ Combination of ESG Integration and active ownership/shareholder engagement is currently most likely to gain widespread adoption

→ ESG issues are continuing to grow amongst public pension plans

→ SJCERA should consider adding language to IPS that relays how the board chooses to deal with these issues moving forward.

- The ESG landscape is evolving from a regulatory and investment standpoint

Proxy Voting

Proxy Voting

Long-term evolution away from automatic vote with management (may not always be aligned with shareholders' interests)

Long-term rise in both filing and voting for ESG shareholder proposals

→ Governance proxies have the longest history and greatest traction

- Proxy access, Board diversity, executive compensation

→ Environment proxies have had the fastest increase – disclose/report on climate risks

→ Social is recently gaining more attention

SJCERA's Current Proxy Voting Policy

→ SJCERA's current proxy voting policy:

- Under current policy, proxy votes are delegated to SJCERA's investment managers and custodian
  - Votes cast on behalf of the fund are done with the primary goal of supporting or improving shareholder interest
  - Should significant or unusual issues arise on proxy voting matters that directly affect shareholder interest, the CEO or the IO are to be contacted to make a recommendation.
- SJCERA's proxy voting policy is set to be reviewed every three years.

Proxy Voting Policy - Options

Management Style	Definition
Current Policy	Delegated voting authority lies with SJCERA's investment managers and custodian. Voting is done in the interest of shareholders and not individual shareowners
Proxy Advisory Firm	Provide a broad range of research and data on proxies. These firms can make recommendations and act on the plan's behalf when voting proxies.
In House Mgt.	Utilization of in-house employees to monitor and vote proxies on behalf of SJCERA.

	Advantages	Disadvantages
Current Policy	→ Little to no cost → Focused on shareholder return	→ Little to no control of proxy votes → Decreased transparency
Proxy Advisory Firm	→ Quarterly and annual proxy reports → Proxies can be voted in the interest of SJCERA	→ Requires additional Policy and Procedures → Additional cost and expenses
In-House Mgt.	→ Maximizes SJCERA's voting interests → Increased transparency	→ High cost and time consuming → Requires additional Policy and Procedures

→ SJCERA's 2023 Goal:

- Define and document SJCERA's approach to proxy voting.
  - Proxy voting policy should align with the Board's ESG approach.

Appendix

Glossary of ESG Institutional Investor Organizations

CA100+: Climate Action 100+ is a voluntary investor-led initiative that brings together – and builds on – a number of pre-existing investor-led engagement initiatives that had been operating in different regions of the world to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change.

Ceres: Ceres works to address the world's greatest sustainability challenges through networks and global collaborations of investors, companies and nonprofits. Ceres coordinates stakeholder engagements, delivers science-based research, and innovative tools that inspire best practices; co-leads global initiatives that drive collective action and economy-wide solutions; mobilizes advocacy campaigns to advance strong policy and regulatory actions; and leverages the power of the media to promote bold sustainability leadership.

IIRC: The International Integrated Reporting Council is an international cross section of leaders from the corporate, investment, accounting, securities, regulatory, academic and standard-setting sectors as well as civil society.

NZAOA: The UN convened Net Zero Asset Owner Alliance is an international group of 49 institutional asset owners representing $7 trillion in assets under management, committed to transition their investment portfolios to net-zero greenhouse gas ("GHG") emissions by 2050, taking action to align their portfolios with a 1.50 scenario, addressing Article 2.1c of the Paris Agreement.

NZAMI: The Net Zero Asset Manager Initiative is an international group of asset managers committed to supporting the goal of net zero greenhouse gas emissions by 2050 or sooner, in line with global efforts to limit warming to 1.5 degrees Celsius; and to supporting investing aligned with net zero emissions by 2050 or sooner. Launched in 2020, the NZAMI currently has 128 signatories with a combined $43 trillion in assets under management.

Glossary of ESG Institutional Investor Organizations (continued)

NZICI: The Net Zero Investment Consultants Initiative brings together investment consultants to support the goal of net zero emissions by 2050 or sooner. Launched in September, 2021, with an initial group of twelve investment consultants committed to supporting their clients in achieving the goal of global net zero greenhouse emissions by 2050; help clients prioritize real economy emissions reductions, reflecting the interim target of 50% global emissions reduction by 2030 or sooner, in alignment with objectives set out in the Paris Agreement.

NZFSPA: The Net Zero Financial Services Providers Alliance launched in September 2021, is a global group of Financial Service Providers, committed to aligning all their relevant products and services to achieve net zero by 2050 at the latest, and to set meaningful interim targets for 2025 within 12-months of joining, supporting the goal of global net zero greenhouse gas emissions by 2050 or sooner, in line with the ambition to limit the global temperature increase to 1.5°C above pre-industrial levels. The world's two largest credit rating agencies, six major audit networks, three leading index providers, and two global stock exchanges are among the 18 organizations behind the alliance.

SASB: The Sustainable Accounting Standards Board standards guide the disclosure of financially material sustainability information by companies to their investors. Available for 77 industries, the standards identify the subset of environmental, social, and governance issues most relevant to financial performance in each industry. SASB standards can be used by companies as a practical tool for implementing the principles-based framework recommended by the Task Force for Climate-related Financial Disclosures ("TCFD"). More than half of the global S&P 1,200 now disclose using SASB standards.

Glossary of ESG Institutional Investor Organizations (continued)

PRI: The UN Principals for Responsible Investing, founded in 2005, today represents a network of over 4,000 international investors working together to voluntarily put six Principles of Responsible Investment into their decision-making and ownership practices. The Principles were developed by the global investment community and reflect the view that ESG factors can affect the performance of investment portfolios and, therefore, must be given appropriate consideration by investors if they are to fulfill their fiduciary duty.

TCFD: The Task Force on Climate Related Financial Disclosures was created by the Financial Stability Board to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit, and insurance underwriting decisions and, in turn, enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks.

TPI: The Transition Pathway Initiative, established in 2017, is a global, asset-owner led initiative, supported by asset managers, which assesses companies' preparedness for the transition to a low carbon economy. Aimed at investors and free to use, it assesses companies' preparedness for the transition to a low-carbon economy, supporting efforts to address climate change.

US SIF: The Forum for Sustainable and Responsible Investment is a non-profit collaborative network committed to investment practices that consider environmental, social and corporate governance criteria to generate long-term competitive financial returns and positive societal impact in the United States. Members, representing $5 trillion in assets under management or advisement, include investment management and advisory firms, mutual fund companies, research firms, financial planners and advisors, broker-dealers, banks, credit unions, community development organizations, non-profit associations, and asset owners.

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