

# AGENDA

## A SPECIAL MEETING OF THE CORPORATE GOVERNANCE

### COMMITTEE OF THE BOARD OF INVESTMENTS

#### and BOARD OF INVESTMENTS\*

LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION

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

8:00 A.M., WEDNESDAY, MAY 15, 2019

*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 Minutes of the Regular Committee Meeting of  
of February 13, 2019

III. PUBLIC COMMENT

IV. REPORTS

A. Navigating Climate in Multidimensional Portfolio Risk Mitigation,  
Adaptation, and Opportunity: Current Efforts and Prospective Steps.  
Scott Zdrazil, Senior Investment Officer  
Dale Johnson, Investment Officer  
(Report dated May 1, 2019)

V. ITEMS FOR STAFF REVIEW

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

VII. ADJOURNMENT

May 15, 2019

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\*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 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. 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.

*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.*

*Persons requiring an alternative format of this agenda pursuant to Section 202 of the Americans with Disabilities Act of 1990 may request one by calling Cynthia Guider at (626) 564-6000, from 8:30 a.m. to 5:00 p.m. Monday through Friday, but no later than 48 hours prior to the time the meeting is to commence. Assistive Listening Devices are available upon request. American Sign Language (ASL) Interpreters are available with at least three (3) business days notice before the meeting date.*

MINUTES OF THE REGULAR MEETING OF THE CORPORATE  
GOVERNANCE COMMITTEE OF THE BOARD OF INVESTMENTS  
LOS ANGELES COUNTY EMPLOYEES RETIREMENT ASSOCIATION  
300 N. LAKE AVENUE, SUITE 810, PASADENDA, CALIFORNIA 91101  
8:00 A.M., WEDNESDAY, FEBRUARY 13, 2019

PRESENT: Alan Bernstein, Chair  
David Muir, Vice Chair  
Joseph Kelly  
Herman Santos, Alternate

ABSENT: Gina Sanchez

MEMBERS AT LARGE: David Green  
Shawn Kehoe

STAFF, ADVISORS, PARTICIPANTS

Jonathan Grabel, Chief Investment Officer

Scott Zdrazil, Senior Investment Officer

Dale Johnson, Investment Officer

Meketa Investment Group  
Stephen McCourt, Managing Principal  
Leandro Festino, Managing Principal

## I. CALL TO ORDER

The Meeting was called to order by Chair Bernstein at 8:00 a.m., in the Board Room of Gateway Plaza. Chair Bernstein stated that Ms. Sanchez was not present and that Mr. Santos, Alternate, would be a voting member.

## II. APPROVAL OF MINUTES

### A. Approval of the Minutes of the Regular Meeting of the Corporate Governance Committee of October 10, 2018.

Mr. Muir made a motion, seconded by Mr. Kelly, to approve the Minutes of the Regular Meeting of October 10, 2018. 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 recommend to the Board of Investments approval of the revised *Corporate Governance Principles*. (Memo dated December 26, 2018)

Mr. Muir made a motion, seconded by Mr. Kelly to approve the recommendation to the revised *Corporate Governance Principles*, with additional incorporation of references for board oversight of climate and broader ESG risks. The motion carried by unanimous vote.

### B. Recommendation as submitted by Scott Zdrazil, Senior Investment Officer: That the Committee recommend approval for Board Investments approval revisions to LAERA's *Corporate Governance Policy*. (Memo dated December 19, 2018)

Mr. Bernstein made a motion, Mr. Kelly seconded, to approve the recommendation to the revisions to LACERA's *Corporate Governance Policy*, with the removal of draft language in Item 8, page 4, regarding availing the Board an option for delegating vote authority. The motion carried by unanimous vote.

- C. Recommendation as submitted by Scott Zdrazil, Senior Investment officer: That Committee approve a formal endorsement of the International Corporate Network (ICGN) Global Stewardship Principles to the Board of Investments for approval.  
(Memo dated January 19, 2019)

Mr. Kelly made a motion, Mr. Bernstein seconded, to approve a formal endorsement of the International Corporate Network (ICGN) Global Stewardship Principles to the Board of Investments. The motion carried by unanimous vote.

## V. REPORTS

- A. 2019 Committee Work Plan Overview  
Scott Zdrazil, Senior Investment Officer  
(Report dated January 24 2019)

Mr. Zdrazil answered questions from the Committee.

## VI. REPORT ON STAFF ACTION ITEMS

There were no items to report.

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

There was nothing to report.

## VIII. ADJOURNMENT

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

May 1, 2019

TO: Each Member  
Corporate Governance Committee

FROM: Scott Zdrazil   
Senior Investment Officer

Dale Johnson   
Investment Officer

FOR: May 15, 2019 Corporate Governance Committee Meeting

SUBJECT: **Navigating Climate in Multidimensional Portfolio Risk Mitigation, Adaptation, and Opportunity: Current Efforts and Prospective Steps**

### **BACKGROUND**

The attached presentation provides an overview of LACERA's steps to date and prospective additional steps to incorporate climate risk into LACERA's investment processes, in furtherance of LACERA's *Investment Policy Statement* and *Corporate Governance Principles* and the Investment Division's 2019 Work Plan. Staff will review the slides and guide a discussion at the May 15, 2019 Corporate Governance Committee meeting.

Attachment

Noted and Reviewed:



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Jonathan Grabel  
Chief Investment Officer

# Navigating Climate in Multidimensional Portfolio Risk Mitigation, Adaptation, and Opportunity Summary of Current Efforts and Prospective Steps

Corporate Governance Committee  
May 15, 2019

Scott Zdrazil, Senior Investment Officer  
Dale Johnson, Investment Officer





# Discussion Outline

## Objective

Maintain proactive, deliberate, informed approach to addressing climate-related investment risks by reviewing progress to date and identifying prospective next steps

## Discussion Outline

1. Stage Setting
  - Climate as material financial risk
  - Climate risk analysis and disclosure frameworks
  - LACERA efforts to date addressing climate risk
2. Discuss prospective additional steps

## Timeline of Recent LACERA Actions Incorporating Climate into the Investment Process

August 2017	October 2017	February 2018	First Half 2018	April-July 2018	August 2018	November 2018
Board education on investment-related climate risks from Paulson Institute	Corporate Governance Committee reviews draft policy language addressing climate risks	Board adopts revised <a href="#">Corporate Governance Principles</a> , incorporating climate risk	LACERA surveys public markets managers on ESG incorporation practices, including climate risks	Corporate Governance Committee discusses engagement priorities, including advocating reliable reporting of climate risks on business strategies	Board approves formal endorsement of <a href="#">Climate Action 100+</a> initiative, global investor coalition on climate reporting	LACERA signs <a href="#">Global Investor Statement to Governments on Climate Change</a> to G7/G20 countries urging climate reporting and action on the Paris Agreement

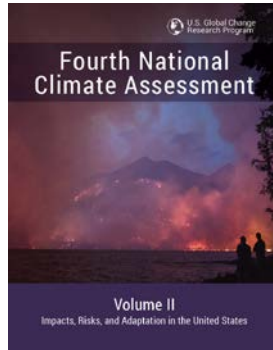


# Climate Through a Materiality Lens

## Recent analysis continues to assess financial risks related to climate change

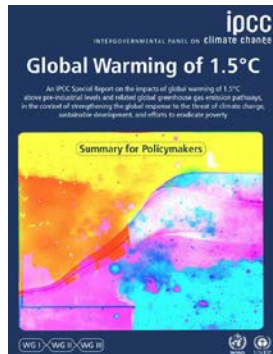
*“Investors who are not thinking about climate-related risks, or who view them as issues far off in the future, may need to recalibrate their expectations.”*

BlackRock. *Getting Physical: Scenario Analysis for Assessing Climate-Related Risks*. April 2019. <https://www.blackrock.com/us/individual/literature/whitepaper/bii-physical-climate-risks-april-2019.pdf>



**U.S. Global Change Research Program.**  
*Fourth National Climate Assessment*. November 2018.  
<https://nca2018.globalchange.gov/>.

“A major scientific report issued by 13 federal agencies... presents the starkest warnings to date of the consequences of climate change for the United States...”\*



**United Nations Intergovernmental Panel on Climate Change.**  
*Global Warming of 1.5°C*. October 2018. <https://www.ipcc.ch/sr15/>

- ✓ “Human induced global warming has already caused multiple observed changes in the climate system (high confidence).” (p177)
- ✓ **“GDP loss [in the U.S.] of 1.2% per degree of warming”**  
(higher in developing economies and the Southern Hemisphere)
- ✓ “Overall global aggregate impacts become moderate at 1°C-2°C of warming, and the transition to moderate risk levels was therefore located at 1.6°C above pre-industrial levels.” (p256)



**Mercer** (follow-up to seminal 2015 investor report)  
*Investing in a Time of Climate Change: The Sequel*. 2019.  
<https://www.mercer.com/our-thinking/wealth/climate-change-the-sequel.html>

“...for nearly all asset classes, regions and timelines, a 2°C scenario leads to enhanced projected returns versus 3°C or 4°C and therefore better outcomes for investors”

“...although incumbent industries can suffer losses in a 2°C scenario, there are many notable investment opportunities enabled in a low-carbon transition” (p9)



# Drivers of Economic Impacts of Climate Risk

Climate change can present **both investment risks and opportunities** in several ways that may vary across industries, geographies, and investment time horizons

## Physical Risks

### Physical Risks

The impact on the value of financial assets and insurance liabilities that arise from acute or chronic climate-related events that damage property or disrupt trade (e.g. storms, draught, crop yields, flood zones, power supply demand)

### Liability Risks

The impacts that could arise from parties who have suffered losses or damage that seek compensation from those they hold responsible (e.g. utilities in wildfires)

## Transition Risks

### Policy Risks

Changes to the regulatory framework that could prompt a reassessment of the value of a large range of assets as costs and opportunities become apparent (e.g. 2° scenario policies; carbon tax; cap-and-trade)

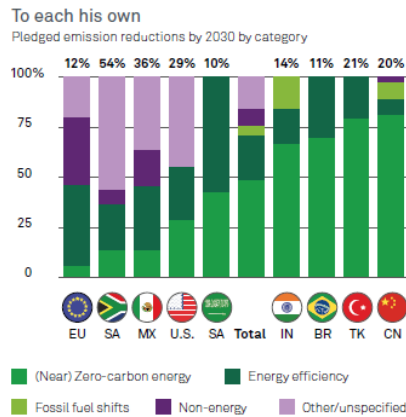
### Technological Risks

Changes in technology resulting from the process of adjustment towards a lower-carbon economy that could prompt reassessment of the value of assets

# Low Carbon Transition Pathways

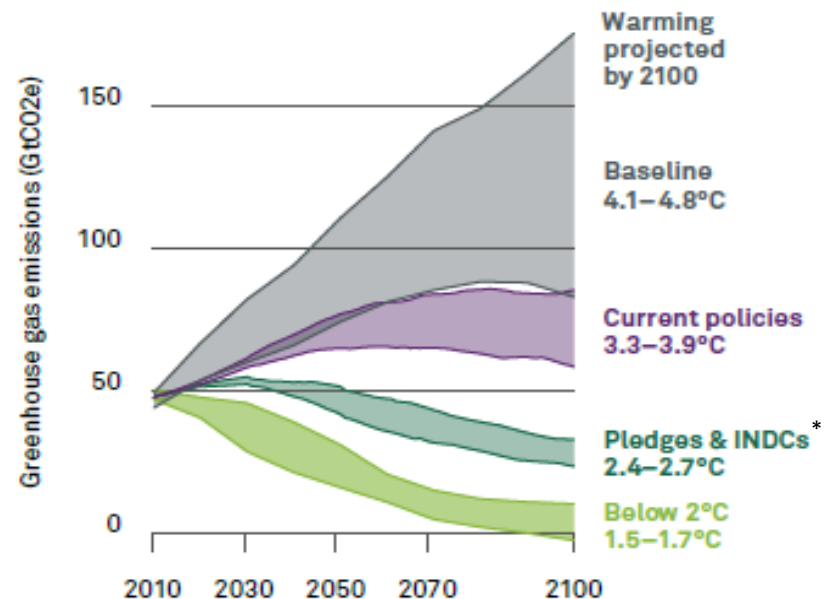
Simplification of policy options describing regulatory pathways that may shape investment risk/return analysis of climate change:

1. **No policy change** leads to estimated 4.1-4.8°C change and resultant economic costs
2. **Cohesive policy responses** adhering to Paris Agreement (i.e. below 2°C scenario) re-prices risk and opportunities across industries, geographies, investment horizons, etc.
3. **Fragmented, chaotic, evolving policy/industry responses** re-shape financial risk and opportunity



## Warming paths

Scenarios for global temperatures, 2010-2100



\* INDC stands for “Intended Nationally Determined Contributions”

Sources: BlackRock. *Adapting Portfolios to Climate Change: Implications and Strategies for All Investors*. September 2016.

<https://www.blackrock.com/investing/literature/whitepaper/bii-climate-change-2016-us.pdf>; BlackRock. *Getting Physical: Scenario Analysis for Assessing Climate-related Risks*.

April 2019. <https://www.blackrock.com/us/individual/literature/whitepaper/bii-physical-climate-risks-april-2019.pdf>.



# Market Hazards and Implications

“Our research suggests many of these risks are not priced in. Why?”\*

## Idiosyncrasies

Climate risks may vary across industries, geographies, and time horizons

*“markets tend to be short-sighted – and underestimate risks that appear uncertain and distant”\**

## Information Asymmetry

Where information is available

## Modelling Variability

Variability and uncertainty in ranges of policy responses and physical impacts

*“climate modeling is an evolving science”\**

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.

*Corporate Governance Principles, §IV, page 17*

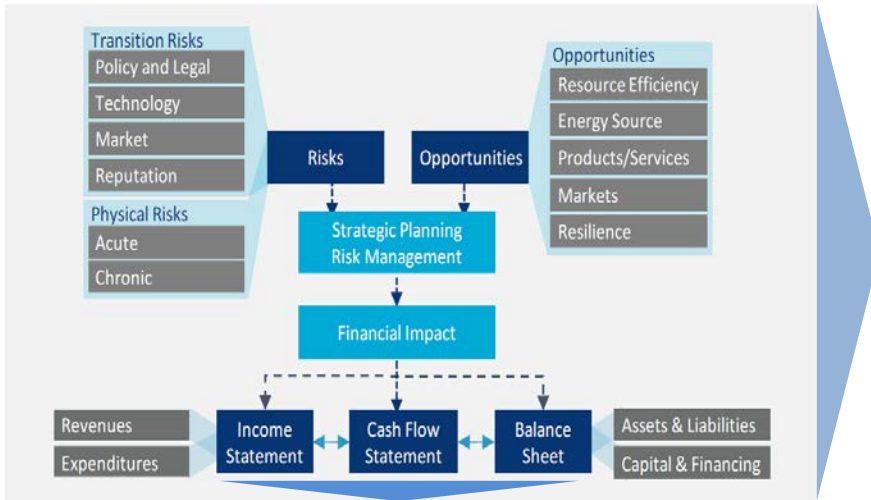
Emerging data and tools aim to identify signals and insights on the scale, trajectory, and dispersion of climate-related investment risks and better assess how climate risks are priced



# Focus on Financial Impact: Pricing Climate

The Financial Stability Board’s Task Force on Climate-related Financial Disclosures (TCFD) focused on the financial impact of climate-related risks and opportunities on a company, rather than the impact of the company on the environment.

Figure 1



Financial impact may span a company’s income statement, cash flow statement, and balance sheet.

Figure 2



**Governance**

The organization’s governance around climate-related risks and opportunities

**Strategy**

The actual and potential impacts of climate-related risks and opportunities on the organization’s businesses, strategy, and financial planning

**Risk Management**

The processes used by the organization to identify, assess, and manage climate-related risks

**Metrics and Targets**

The metrics and targets used to assess and manage relevant climate-related risks and opportunities

The TCFD recommended a four-part approach for **forward-looking** corporate climate risk assessment and disclosures.

Source: Task Force on Climate-related Financial Disclosures (<https://www.fsb-tcfd.org/wp-content/uploads/2017/06/TCFD-Recommendations-Overview-062717.pdf>)

# Pathways to Integrate Climate into Investment Process



**YOU are here!**

LACERA currently addresses climate risks through several strategies

## Governance and Policy on Climate Risk

- 1. Establish governance**
  - ✓ Board of Investments establishes asset allocation and investment policies
  - ✓ Corporate Governance Committee oversight
- 2. Define a policy position**

**LACERA's Corporate Governance Principles state:**

**"Climate Risk:** Climate change may present financial, operational, and regulatory risks to a firm's ability to generate sustainable value, as well as to the broader economy. Firms should assess and disclose material climate-related risks and sufficient, non-proprietary information to enable investors to prudently and adequately evaluate the prospective impact of climate risk on firm value." (SV[B]3; page 20)

## Stewardship Practices Consistent with Policy

- 3. Vote proxies**

Example: Vote FOR resolutions requesting corporate disclosure of climate risks (e.g. 60% support at Exxon)
- 4. Engage companies and policymakers**
  - ✓ Endorsed Climate Action 100+ initiative to encourage carbon-intensive companies to report financial risks and mitigation strategies
  - ✓ Signed 2018 Global Investor Statement to Governments on Climate Change

## Portfolio Analytics and Management

- 5. Assess exposures with portfolio analytics**
  - ✓ Assess securities, managers, and aggregate portfolio exposures
  - ✓ Integrate scenario analysis into total fund risk management
- 6. Pursue investment opportunities**
  - ✓ Identify/track clean energy investments in portfolio
  - ✓ Target clean energy and emerging tech investment opportunities
- 7. Mitigate downside risks**
  - ✓ Integrate climate into strategic asset allocation forecasts
  - ✓ Reduce exposures or tilts in portfolio construction

LACERA might enhance its climate strategies by considering additional avenues



# Prospective Additional Steps

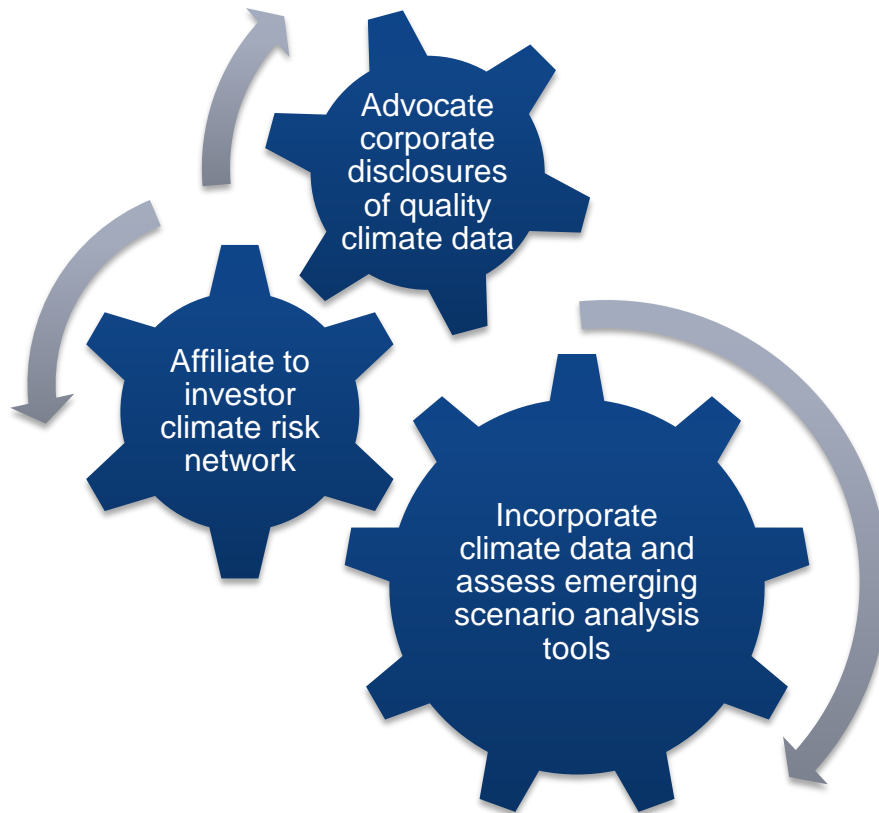




# Pragmatic Near-Term Steps

Staff would like to discuss and receive feedback on several additional steps to further incorporate climate mitigation into LACERA's investment process

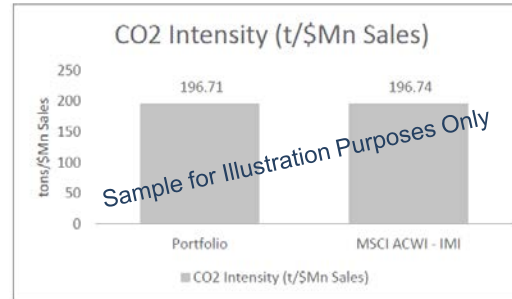
**Proactive**  
**Deliberate**  
**Informed**  
**Intentional**



# 1. Incorporate Climate into Portfolio Analytics

Exploring possible data to incorporate into risk platform to inform investment monitoring and analysis

## 1. Portfolio carbon analysis relative to benchmark (e.g. global equities)



- Aggregate
- Snapshot in time
- Combines direct disclosures and modelling

## 2. Manager level analysis of exposure

*Sample for Illustration Purposes Only*

	Manager Y	Manager Z
Weighted Average Emissions tons CO2/\$m Sales	145.19	182.67
Benchmark	151.12	151.12
<i>Benchmark Comparison</i>	<i>-3.92%</i>	<i>20.88%</i>

## 3. Security level analysis to identify which securities drive exposures

### Questions and considerations:

- Data gaps and evolving models: Is the data complete, consistent, comparable, and reliable?
- Public market bias: Estimated data for non-reporters; Private markets less developed
- Objectives: Does LACERA want to be above or below a defined benchmark?
- Portfolio modeling: How will natural resources allocation impact exposures?

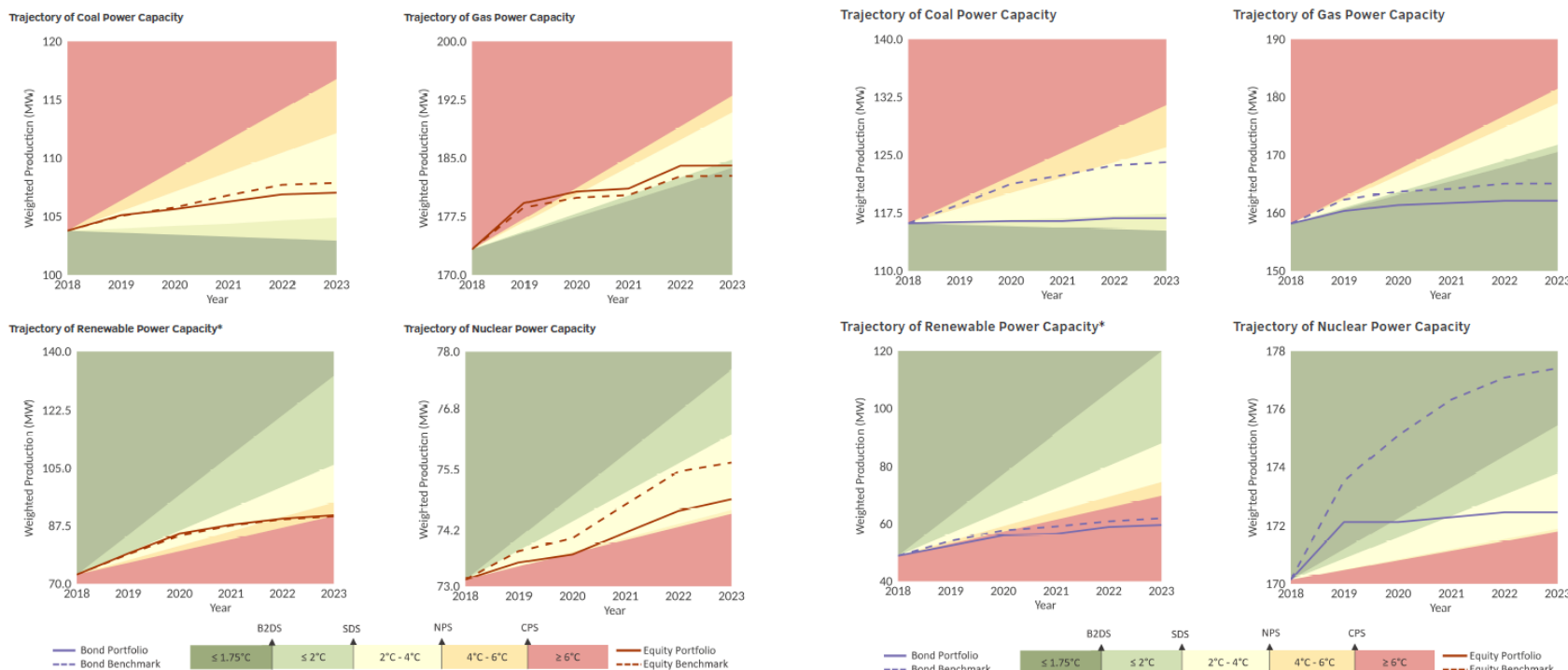
# 2. Assess Emerging Models on Scenario Analysis

LACERA public markets portfolio exposure to 5-year, forward-looking power generation capacity compared to four climate risk scenarios and a benchmark of peers

*Sample for Illustration Purposes Only*

## Global Equities Portfolio

## Fixed Income Portfolio



### Cautions and considerations:

- Generated using [Paris Agreement Capital Transition Assessment](#) tool developed by PRI and the 2 Degree Investing Initiative
- Limitations to methodology replication and granular data opacity; Customization
- Undisclosed peers
- Uncertain future availability and consistency of data service



# 3. Support Efforts to Enhance Data Quality



The [Task Force on Climate-related Financial Disclosure \(TCFD\) final recommendations](#) were released in 2018.

- Voluntary disclosure framework to provide financial risk disclosures to investors, lenders, insurers, and others
- Devised by the private sector

LACERA may wish to formally endorse:

- Investor support communicates market demand for disclosures
- No cost
- LACERA would be listed on TCFD website
- Although primarily aimed at corporations, supporters may wish to adopt TCFD reporting model
- LACERA incorporates the TCFD reporting framework into its annual assessment for all signatories, such as LACERA

Staff may prepare formal recommendation to upcoming board or committee meeting.

**Over 580 TCFD supporters, such as:**

- Alliance Bernstein
- Allianz
- Anglo American
- AP Funds – Sweden
- AQR Capital Management
- Australian Prudential Regulation Authority (insurance regulator)
- Bank of America
- Barclays
- Barrick Gold Corporation
- BlackRock
- Bloomberg LP
- BNP Paribas
- California Department of Insurance
- CalSTRS
- CalPERS
- CBRE
- Credit Suisse
- Dow Chemical
- Dupont
- Fidelity Investments
- GCM Grosvenor
- Goldman Sachs
- Governments of France, Canada, and the UK
- International Assoc of Insurance Supervisors
- International Finance Corporation
- Invesco
- Nasdaq
- New York City Employees Retirement System
- New York State Common Retirement Fund
- Standard Life Aberdeen
- State Street Global Advisors
- Vanguard

## 4. Consider Affiliation to Investor Network

### Ceres Investor Network on Climate Risk and Sustainability

The [Ceres Investor Network](#) is a North American regional network including 160 institutional investors with over \$26 trillion in assets:

- Advance leading investment practices on climate
- Regional coordinating association for investor initiatives such as Global Investor Statement to Governments on Climate Change and the Climate Action 100+
- “Big tent” organization including corporate members

Affiliation considerations:

- Assess climate mitigation research and investment approaches
- Peer-to-peer knowledge exchange
- Coordinate corporate engagements; e.g. Climate Action 100+ and Global Investor Statement to Governments on Climate Change
- Annual fee
- Multi-partite governance structure

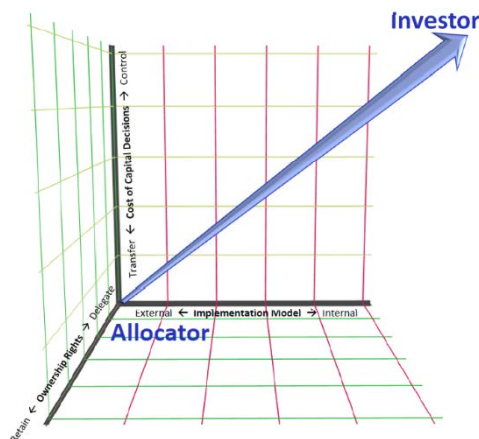
Staff may prepare formal recommendation to upcoming board or committee meeting.

#### Ceres members include:

- AFL-CIO
- BlackRock, Inc
- CalSTRS
- CalPERS
- Connecticut Office of the State Treasurer
- DWS Investments
- Fidelity Investments
- Florida State Board of Administration
- Harvard Management Company
- International Brotherhood of Teamsters
- Maine Employees Retirement System
- Maryland State Retirement System
- Massachusetts Office of the State Treasurer
- Minnesota State Board of Investment
- Montgomery County Retirement System
- Moody’s Investors Services
- Morgan Stanley
- Neuberger Berman
- New Mexico State Treasurer’s Office
- New York City Retirement System
- New York State Comptroller
- Oregon Office of the State Treasurer
- Parametric
- Rhode Island Office of the Treasurer
- San Francisco Employees Retirement System
- Service Employees International Union
- Seattle Employees Retirement System
- State Street Global Advisors
- University of California
- Vermont Office of the Treasurer
- Washington State Investment Board
- Wellington Management Company
- Wells Fargo Asset Management

# Recap of Near-Term Steps

**Consistent with  
2019 Work Plan**



## 1. Execute risk platform search incorporating climate data

- ✓ Access ESG data to assess portfolio, manager, and issuer exposures
- ✓ Incorporate basic carbon data
- ✓ Evaluate adequacy and limitations of carbon data tools

## 2. Assess complementary analytical tools

- ✓ Analyze portfolio under multiple risk factors and scenarios, including climate
- ✓ Assess prospective impact of various regulatory frameworks and physical risks
- ✓ Identify exposures to inform investment decisions

## 3. Support market efforts to improve reliable, quality data

- ✓ Continue support of Climate Action 100+
- ✓ Consider endorsing TCFD

## 4. Explore affiliation to regional investor climate network

- ✓ Consider joining Investor Network on Climate Risk/CERES

## Timeline of Prospective Next Steps

2019 Q3	2019 Q4	2020	2021
Discuss update of Climate Action 100+ engagement and next steps	Conclude risk platform search with ESG and climate data tools	Onboard risk platform and assess adequacy and limitations of climate data tools	Consider analytical tools to incorporate climate into economic modeling for next strategic asset allocation study
Consider TCFD endorsement		Assess advances in scenario analysis modeling	
Consider affiliation with Investor Network on Climate Risk/CERES			

