Council of Institutional Investors®

2019 SPRING CONFERENCE HIGHLIGHTS

More than 530 CII members attended CII's March 4–6 spring conference in Washington, D.C., which featured discussion topics ranging from the promise of blockchain technology to investor perspectives on the #MeToo movement. You can view the complete conference program here, which includes the full agenda, speaker details, attendee list and more. Video and audio recordings are available for all plenary sessions and current CII members with login credentials may access those files here.

In addition to CII plenary sessions and content, current member organizations hosted their own content during our Member-hosted meetings, which included sessions on the following topics:

- Human Capital Management Risks in the Gig Economy
- Shareholder Proposals at a Crossroads
- Ownership and Control: Economic Exposure and Voting Power
- Diversity: Let's Get on With It
- Renewable Energy: Challenges and Solutions
- Corporate Governance in Emerging Markets
- Understanding ESG Risks at Large Technology Companies

CII ELECTIONS & WORKING GROUPS

Board of Director Elections

At the conference, CII elected a new board of directors for 2019–20, and named Ash Williams, executive director and CIO of the State Board of Administration of Florida, board chair for the second year in a row. In keeping with CII's bylaws, Williams was elected chair by CII's public fund members.

CII members also re-elected the other board officers to a second term. That includes board co-chairs Mary Francis, corporate secretary and chief governance officer, Chevron; Michael Garland, assistant comptroller, corporate governance and responsible investment, New York City Pension Funds; and John Keenan, corporate governance analyst, AFSCME Employees Pension Plan. Scott Zdrazil, senior investment officer-corporate governance, Los Angeles County Employees Retirement Association, was re-elected as treasurer and Cambria Allen-Ratzlaff, corporate governance director, UAW Retiree Medical Benefits Trust, was re-elected as secretary.

Other members of the CII board for 2019–20 are:

- Jerry Albright, CIO, Teacher Retirement System of Texas
- Ron Baker, executive director, Colorado Public Employees' Retirement Association
- Patricia Brammer, corporate governance officer, Ohio Public Employees Retirement System*
- Renaye Manley, deputy director, strategic initiatives, Service Employees International Union
- Aeisha Mastagni, portfolio manager, California State Teachers' Retirement System
- Thomas McIntyre, international representative, International Union of Bricklayers and Allied Craftworkers
- Hope Mehlman, chief governance officer and assistant corporate secretary, Regions Financial
- Simiso Nzima, investment director, global equity, California Public Employees' Retirement System*
- Jennifer Peet, corporate governance director, Office of the Oregon Treasurer and Oregon Public Employees Retirement Fund

*newly elected director

Advisory Councils

CII's newly appointed Corporate Governance and Markets Advisory Councils met during the spring conference and then joined the Board of Directors for a private lunch during the spring conference. You can view a list of the individuals who are currently serving on these advisory councils here.

Corporate Governance Advisory Council

Newly appointed CGAC Chair Sara Donaldson led the March 4 meeting of the council, which included discussions on:

- CII's new board evaluation study
- CII's work on revising its executive compensation policy
- share repurchases
- petitions to stock exchanges on dual-class companies
- why CII is focusing attention on market structure issues
- proxy mechanics in the United States and in Canada
- use of structured/unstructured data to assess ESG
- SASB, SEC rule changes, other efforts to set E&S reporting changes
- proxy roundtable issues, including proxy advisors and shareholder proposal rules
- board diversity
- #MeToo and company practice/policy related to sexual harassment
- gender pay equity

Markets Advisory Council

CII's Markets Advisory Council (MAC), led by its Chairman Daniel Sommers, a partner at Cohen Milstein, met March 4 and discussed the following current market trends affecting institutional investors:

- The growing prominence of auditing and audit committee issues with proxy voters
- The effect on U.S. investors of the EU's markets in financial instruments directive (MiFID II)
- The status of ESG integration in pension fund investing in the U.S. and E.U.
- The divergence between companies' and investors' views on SEC Rule 14a-8 resubmission levels
- Communications between CII and other groups that are concerned about the potential for more regulation of proxy advisory firms
- Best practices for company engagements with investors
- The implications of EU insurance companies engaging in pension plan "buy outs" and "buy-ins"
- Public policy issues concerning the use of derivative collars by activist investors

Pension Fund Trustee Dinner & Roundtable

More than 25 individuals from public pension funds gathered for a private dinner at the Mandarin Oriental Hotel. The dinner was followed by a roundtable with open discussion and a chance for trustees to meet and engage with their peers.

Proxy Voter Working Group

CII staff hosted another successful proxy voter working group with more than 90 people in attendance at the spring conference. The goal of its invitation-only, closed-door meetings and calls is for corporate governance professionals at institutional investor organizations who vote proxies and engage portfolio companies to share their perspectives on voting issues, engagement, shareholder rights and specific company situations, and to discuss potential changes to voting policies or practices.

Capitol Hill & SEC Meetings for Voting Members

CII General Counsel Jeff Mahoney hosted General (voting) members for meetings at the Securities and Exchange Commission and with legislators from the House of Representatives and the Senate.

SUMMARY OF CII PLENARY & BREAKOUT SESSIONS

SEC Commissioner Peirce Thanks, Critiques CII

SEC Commissioner Hester Peirce divided her remarks to CII into two sections, one in which she expressed gratitude and the other in which she aired her "grievances," quoting Seinfeld's Frank Constanza.

In the first part of her speech, she outlined the many times for which she has been grateful that CII offered guidance to the SEC. Peirce cited CII's helpful input on: the use of blockchain technology to track proxy voting, recommended changes to assure vote confirmation, the value of modernizing EDGAR and improving data tagging, market structure in both the equity and the fixed income markets, the use of XBRL, changes to the auditor independence rules and reforms to certain disclosure requirements under Regulation S-K. The SEC commissioner expressed overall gratitude to CII for the role it plays in "thinking through some of the most difficult issues in financial regulation and corporate governance" and she promised to continue to turn to CII for advice.

Then, Peirce offered a list of grievances, first expressing skepticism about the value of the mandatory use of a universal proxy card, but promising to continue to think through the issue. In terms of dual-class shares, she said she is "reluctant to interfere in the relationship between shareholders and issuers unless necessary."

Mandatory arbitration helps companies avoid the cost of defending and settling expensive class action suits, she argued. "Shareholders are ultimately harmed by the very option intended to protect them: first by the company's diversion of resources to defend often meritless litigation, and second by the resulting decline in the value of their shares," Peirce added. She qualified her remarks by saying she is not in favor of mandatory arbitration clauses for all companies. "If shareholders value the ability to bring class actions, they can divert their investments to companies that offer such options," she explained, adding that she believes the SEC does not need to get involved in this issue.

In terms of Rule 14a-8, the SEC commissioner expressed support for raising both the resubmission and ownership thresholds, saying the ones in place now "permit, indeed encourage, a handful of shareholders to put forward proposals that incur considerable costs borne by all shareholders." She said often small groups of shareholders submit losing proposals over and over again, and many of the proposals are not related to core corporate governance issues, but instead promote personal political and social preferences. The current rules prompt companies to negotiate "backroom deals" with proponents that are not in best interests of the companies, she added. Furthermore, said Peirce, the current no-action system "foists SEC staff into an inappropriate policymaking role" and diverts staff's resources away from rulemaking and reviewing disclosures.

She was critical of the Division of Corporation Finance's new compliance and disclosure guidance related to reporting on board qualifications. Peirce expressed concern that making directors' personal characteristics an item of expected disclosure may have unintended consequences such as invasion of board members' privacy and an undue focus on personal features that may have little relation to talent as a director.

Finally, Peirce criticized the International Organization of Securities Commissions' (IOSCO) January statement on ESG investing that directs companies to consider whether ESG factors should be included in their disclosures and endorses the use of private disclosure frameworks intended to get at these factors. "Requiring disclosures aimed at items identified by organizations that are not accountable to investors unproductively distracts issuers," she told CII members.

Head of World's Largest Pension Fund Speaks Out

Hiro Mizuno, executive managing director and CIO of the Government Pension Investment Fund (GPIF), which is the Japanese national pension fund and the world's largest, shared his investment perspectives with CII Chair Ash Williams. GPIF is 100% externally managed due to regulatory restrictions that prevent the pension giant from having any direct investments. To help oversee its external managers, GPIF is working with Sony to develop artificial intelligence that can help the pension fund keep track of investors' trading patterns. On another topic, Mizuno said GPIF demands that its asset managers integrate ESG

into their analysis and decision making and encourages them to engage with companies on these issues. He also recommended that investors spend more time monitoring index providers. "Their role in the investment chain has been neglected," he cautioned.

Directors as Change Agents

The conference's first plenary session, moderated by Prudential Financial Chief Governance Officer, SVP and Corporate Secretary Peggy Foran, featured three women directors who have been change agents on boards of companies that have been confronted with difficult circumstances. Karina Litvack, a director at ENI, an Italian company, described how six weeks after she joined the board the company was raided as a result of suspicious offshore transactions in Nigeria. After the raid, her suggestions for changes at ENI were met with accusations by fellow board members, who called for her resignation from the board's risk committee. Institutional investors helped her fight back against these accusations and to retain her board and committee seats. The company's general counsel and 14 other employees were sentenced to jail time. Litvack said it is important at a global company to have at least one director who is from a country other than the one where the company is based.

Gabrielle Sulzberger, former chair at Whole Foods Market, spoke about the circumstances surrounding the proxy fight that Jana Partners launched at the high-end grocer in 2017. She said the dissidents forced the company to add five new directors to the board and led to Amazon's acquisition of Whole Foods. Without the push from Jana, the company would have been bought out by a conventional grocery store chain, she said. Sulzberger stressed the need for preparedness, saying a crisis is "not only possible, but probable." She also emphasized the need for maintaining a strong relationship with your investors before a crisis hits.

Sandra Guerra, a board member at Vale, which is located in Brazil, described how the company reacted after its Corrego do Feijao mine collapsed in January. Immediately after the disaster, Vale formed two committees, one to investigate the causes of the dam burst and one to focus on the problems caused by the collapse. "In seven days, we were focused on the safety of all of our other dams throughout the world," she said. Guerra advised that, during a crisis, boards maintain calm, focus on what is important and listen to all of the company's stakeholders. "Tone at the top is so important," she asserted.

Blockchain and Securities Trading

In this session, Mark Smith, CEO of fintech firm Symbiont, discussed his vision of how blockchain technology can revamp the proxy infrastructure. To improve investors' experience with share ownership and voting, Smith said that blockchain technology is well suited to create a better system of share provenance. Symbiont's platform uses "smart securities" that can identify who the ultimate beneficial owner of an asset is at any given time and directly provide that owner the economic and voting rights tied to that asset. Smith explained that moving to this more efficient system will require regulatory change since companies and investors are required to participate in the current labyrinthine system of intermediaries. In the absence of this change, Symbiont currently offers its platform only to private companies, but Smith concluded: "Within a decade, we hope to see a majority of public companies using a blockchain structure. It's time to remove the layers of lazy technology and harness solutions that enable real-time tracking of securities and vote confirmation."

Focusing on the 'S' in ESG

Tobias Read, Oregon State Treasurer, issued a call to action, asking CII members to elevate the attention they give to social factors when making investment decisions. He said better metrics need to be available to help investors assess the risks created by social issues and he asked CII members to coalesce around data-driven actions once those metrics are developed. He also hoped that investors' increased focus on social issues would be viewed as a public notice to companies. "Companies create cultures that determine shareholder value," Read emphasized. He urged CII members to "stay tuned and stay engaged!"

Tony West, chief legal officer for Uber Technologies, said Uber has undergone a culture change under its new CEO. He said the chief executive set a new tone at the top and instilled a new set of cultural norms that emphasize transparency, accountability and integrity. West said the company is dealing with the challenges of engaging in a gig economy that ensures "flexibility, security and dignity" for its employees and customers.

Keir Gumbs, associate general counsel for Uber Technologies, explained how the company dropped its mandatory arbitration clause for employees and customers and is now providing full transparency, publishing a detailed safety report. He said Uber also has developed a categorization for the travel industry to use when identifying and reporting sexual assault cases. Gumbs asked CII members to encourage other companies to follow Uber's lead and expand transparency in this area.

Pay Pioneers

John Trentacoste, partner and COO at Farient Advisors, moderated a discussion with representatives from two companies that are bucking the standard approach to pay and an investor that advocates for simpler, more long-term-oriented compensation. Christine Poon, chair of the compensation committee at Regeneron Pharmaceuticals, explained how her company grants stock options to all of its employees. She said this approach has created an ownership culture, fostered innovation, boosted productivity and retained scientific talent. Darian Rich, human resources executive for Barrick Gold, said his company requires its executives to hold their shares for the duration of their employment with the company. The CEO must hold three times his base salary in shares and other executives must hold five times their base salaries. "Being shareowners helps them drive the long-term viability of the enterprise and provides everyone with more connectivity to the decisions being made," said Rich.

Timothy Youmans, a director at Hermes EOS, said pay in the United States and the Americas is way too high. "There has been an experiment to align pay with performance and it hasn't worked," he asserted. Youmans said a new system has to be created that is aligned with long-term strategy and incorporates simplicity, shareholding, accountability and stewardship. He also emphasized the need for pay plans that offer compensation committees the discretion to adjust CEOs' pay downward as well as upward.

Asset Owners Reflect on Reforming Executive Pay

On a panel examining executive pay, TerriJo Saarela of the State of Wisconsin Investment Board gave an update on potential changes on the horizon for CII's official pay policy (see News from CII below). Simiso Nzima of CalPERS described how his fund recently became more aggressive when scrutinizing pay packages, consistent with an uptick in casting "no" votes on say-on-pay. CalPERS pays particular attention to a five-year quantitative model that evaluates pay relative to peers' realizable pay, he explained. He said the pension fund also favors metrics that are hard to manipulate and truly drive long-term value creation. Nzima observed that some pay arrangements, such as those that make the vast majority of compensation variable, can actually de-motivate executives and potentially inhibit certain characteristics that are increasingly important in corporate leadership, such as creativity and openness to innovation.

Tracy Stewart of the Florida State Board of Administration observed that many of her fund's "no" votes on pay are not out of a disagreement over design features per se, but due to a lack of substantive disclosure on metrics and targets. "We can't support something if we don't know how it works," she said. Stewart voiced collective investor frustration with "so many pieces and moving parts" and adjustments to modern executive pay arrangements. She

asked whether a back-to-basics approach might be a better model, in which fixed pay constitutes a significant majority of total compensation and opportunity for a proportionately small bonus is provided. On voting, she urged investors to let their analysis trump "politeness," and consider voting against compensation committee members who adopt poorly designed or poorly disclosed pay packages.

Focusing Capital on the Long-Term

Sarah Williamson, CEO of FCLTGlobal discussed the importance of investing for the long term with Michael Garland, assistant comptroller, corporate governance and responsible investment for the Office of the New York City Comptroller. She stressed the importance of companies providing investors with long-term roadmaps as opposed to quarterly guidance. Quarterly earnings reports are important for transparency, but should provide information beyond the next quarter, she recommended. She used a football analogy, pointing out that in the third quarter of a game, everyone wants to know the whole score, not just the points scored during that particular quarter. Williamson also stressed the need for boards to focus on the long-term and to structure executive pay for the long haul. She pointed out that the average tenure of a CEO is just five to seven years and questioned if that leads to a shorter term perspective at the top. Finally, she encouraged CII members to make sure that their asset managers maintain a long-term focus.

Fixed Income and Corporate Governance

Panelists evaluated why and how corporate governance and sustainability issues matter to fixed income investors during this panel session moderated by CII Executive Director Ken Bertsch. Brendan Sheehan, VP and senior analyst for ESG at Moody's Investor Services, said Moody's created a corporate governance framework after surveying investors about what is material to them and why. The credit rating agency is now conducting a great deal of research about what is material in the environmental and social realms. "We've seen a 200% increase in the level of interest in ESG issues," Sheehan added. He said he anticipates regulation requiring ESG integration into investment decisions in Europe soon. Sheehan emphasized that the risks presented by environmental factors like carbon emissions, air pollution, water pollution and fires are real and he pointed to PG&E. The California utility company, which has had to file for Chapter 11 bankruptcy thanks to its role in the wildfires that decimated the state, may "change the credibility profile for every utility company," Sheehan cautioned.

Yves Denize, managing director and division general counsel at Nuveen, said his firm is building an ESG team that is engaging with companies on these issues and using ESG-branded products to measure outcomes. The team is integrating this approach across all asset classes and products, including fixed income investments.

Elizabeth Seep, executive director at MSCI, said her organization began integrating governance into its core products in 2012, but more recently expanded this integration exponentially. "Governance is now in all of our ratings," she said. Integration of E and S factors is more industry-specific, she explained.

Engaging in Market Policy Reform to Enhance Long-Term Performance

This breakout session with Don Pontes of CalPERS, John Ramsay of IEX and moderated by SEC Investor Advisory Committee Chair Anne Sheehan, explored several market structure issues that affect funds' bottom lines and returns. First, many brokers route their customers' trade orders through proprietary systems that do not always reflect the lowest share price, failing to deliver best execution. Second, investors using the slower, public market data stream provided by NYSE (rather than the exchange's faster, paid stream) experience lags in their data that cause them to pay higher, outdated prices and cost them billions per year. Third, the new MiFID II regulations in Europe unbundling research costs from trading commissions created uneven regulatory regimes that leave U.S. investors to subsidize research across markets.

To mitigate these market structure issues, the panelists called for the unbundling of trading and research costs and encouraged investors to engage with regulators to prioritize best execution. As an example of the success of this approach, the panelists praised the SEC's transaction fee pilot, which the commission approved unanimously in December and limits the fees and rebates that exchanges can charge for trading.

On Leadership and History

Luncheon speaker Michael Beschloss, who is a presidential historian and bestselling author, spoke about the common traits of great leaders and the important perspective that the study of history provides. He said the four common qualities of U.S. presidents that made them great leaders are: 1) a willingness to do things that are unpopular; 2) the ability to explain well difficult decisions; 3) a sense of history and knowledge of how previous presidents dealt with similar circumstances; and 4) the ability to work with those with whom they disagree. To recognize these qualities in previous presidents, a certain amount of time must lapse to provide the proper perspective, he said. Beschloss also emphasized the importance of studying history in the curriculum. "If you ignore history, your life experience will be limited to just you, your family and friends," he warned.

Drivers of Emerging Market Capital Flows/Global Governance Developments

James Andrus, investment officer for CalPERS, moderated a panel discussion on the World Federation of Exchanges and recent developments in Europe. Nandini Sukumar, CEO of the World Federation of Exchanges, said equity market returns, trading activity and good disclosure, especially English language disclosure, were key factors that bring investors to emerging markets. Structural impediments to investing in emerging markets vary, but often are political, she explained. Patience is important when investing in an emerging market, she added. When asked about the race to the bottom that some believe is occurring as a result of the competition among U.S. exchanges, she said the reputation of an exchange is paramount. "If investors don't trust you, they won't buy the stock," she said.

Margriet Stavast-Groothius, senior advisor for responsible investment at PGGM, discussed a range of governance developments in Europe including:

- Proposed legislation in the Netherlands that would impose a 250-day 'stand still' period after an investor makes a hostile offer
- Eumedion, a Netherlands-based organization that matches investors and companies for engagement on governance and sustainability issues
- a survey of PGGM clients and participants to measure how heavily they think sustainability should weigh in investment decisions
- an agreement among more than 70 large Dutch pension funds and NGOs, trade unions and the Dutch government pledging cooperation on sustainable investing

Stavast-Groothius also provided an update on the E.U./U.S. diversity coalition which engages with companies on all sorts of diversity issues, including age, and tries to move the needle toward greater diversity on boards.

Risks Posed to Companies by Sexual Harassment

CII Shareholder Advocacy Committee Co-Chairs Brandon Rees and Patti Brammer moderated a panel discussion on Investors Engage on #MeToo.

Sharon Hendricks, vice chair of CalSTRS and a member of Trustees United, a group of pension fund trustees seeking to mitigate and reduce risks related to sexual harassment, violence and misconduct, outlined her group's four principles:

- Companies must ensure a culture free of sexual harassment and violence.
- Companies must not use non-disclosure agreements and forced arbitration policies, and instead must report sexual harassment and misconduct settlement costs to investors.
- Companies must prioritize diversity at all levels, including the board of directors and C-suite to help create cultures that prevent sexual harassment and related risks.
- Companies should enact policies and agreements, such as collective bargaining agreements and responsible contractor policies that protect workers' rights.

Elizabeth Greenwood, a commissioner at LACERS, explained that her fund adopted a policy that any entity that wants to conduct business with LACERS must have a sexual harassment policy and must disclose any sexual harassment settlements that it has reached. "These settlements represent a threat to our return on investment and we want to earn our returns ethically and honestly," she said.

Vicki Tardif, one of the Google employees who organized a November company-wide walkout over the company's sexual harassment policies, compared the organization of the walkout to a wildfire. She said the fuel on the ground was the lack of disclosure about what was happening within the company and the spark that ignited the movement was The New York Times report on millions of dollars in exit packages that Google paid to male executives accused of harassment. She said employees who walked out in November had six demands: 1) an end to forced arbitration; 2) a commitment to end pay and opportunity inequity; 2) publication of a public sexual harassment transparency report; 3) a clear, uniform, globally inclusive process for reporting sexual misconduct; 5) the promotion of a chief diversity officer to answer directly to the CEO; and 6) the appointment of an employee representative to the board.

CII Members Share Their 2019 Proxy Season Initiatives

Eighteen CII members discussed their plans for the upcoming proxy season during the 'lightning round' portion of the Shareholder Advocacy Committee plenary session. Representatives from the AFL-CIO, As You Sow, CalPERS, Ceres, Climate Majority Project, CtW Investment Group, Deminor, Illinois State Treasurer, LACERA, Lawndale Capital Management, Marin County Employees' Retirement Association, NY State Comptroller's Office, Oregon Public Employee Retirement System, Segal Marco Advisors, Teamster Affiliates Pension Plan, UAW Retiree Medical Benefits Trust, UFCW Capital Stewardship Program and UNITE HERE spoke. Background information about most of their initiatives is available here and recording of the lightning round can be found here.