City of Seattle

Seattle City Employees' Retirement System

ESG Quarterly Update: Second Quarter 2021

Introduction

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

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

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

Positive Action Strategy

Shareholder Advocacy	Sustainability Investments	Integrating Climate Risk into the Investment Process

Investor Organizations and Initiatives

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

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

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

Shareholder Advocacy

Description

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

Current Focus

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

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

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

Shareholder Advocacy

Quarterly Activity

The Coalition United for a Responsible Exxon (CURE), of which SCERS is a member, published a report detailing several recommendations that **Exxon** should take to improve its financial performance. The key recommendations were to strengthen governance to avoid repeating past mistakes and establishing and disclosing a plan in line with the Paris Agreement to prepare for the energy transition.

The **Climate Action 100+** investor initiative released a benchmark for evaluating the ambition and action of fossil fuel companies to a net-zero transition. The Net-Zero Company Benchmark[2] compares company performance against three high-level goals: reducing greenhouse gas emissions, improving governance and strengthening climate-related financial disclosures.

[1] https://curexxon.org/wp-content/uploads/2021/05/CURErecommendations_20210505_fin.pdf
[2] https://www.climateaction100.org/progress/net-zero-company-benchmark/

Shareholder Advocacy

Quarterly Activity

SCERS joined other institutional investors in a letter to **Congress** that urged the use of the Congressional Review Act to overturn a Securities and Exchange Committee (SEC) rule that makes it more difficult for investors to submit shareholder resolutions[1]. The rule was put in place in the waning days of the Trump administration and has the potential to increase the power of management at the expense of shareholders.

[1] https://www.ussif.org//Files/Public_Policy/Investor%20sign-on%20letter%20urging%20Congressional%20Review%20Act%20disapproval%20of%20the%20SEC's%20Rule%2014a-8%20amendments.pdf

Sustainability Investments

Description

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

Current Focus

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

Monitor investments in green bonds by SCERS-invested managers and continue evaluating other sustainability investments

No Updates during the Quarter

Integrating Climate Risk into the Investment Process

Description

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

Current Focus

Understand and assess how SCERS's managers are integrating ESG considerations into their investment processes in comparison to best practices

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

Integrating Climate Risk into the Investment Process

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BLACKROCK

BlackRock, a SCERS-invested manager, published a paper introducing their development of climate-aware capital market assumptions. These assumptions can be used in strategic asset allocation decision-making and replace their prior methodology that had not directly incorporated climate change. The development of climate-aware capital market assumptions can complement NEPC's climate scenario analysis methodology that was incorporated in SCERS's 2019 asset-liability study.

[1] https://www.blackrock.com/corporate/literature/whitepaper/climate-aware-investing.pdf

Staff Activity and Informational Items

Pensions&Investments

Jason Malinowski will be participating on a panel at the Pensions & Investments' ESG Investing Virtual Series on May 17th. The panel entitled "Investing for Climate" will focus on engagement and collaboration opportunities related to climate change and tools and data that can be used to evaluate climate risks.

FUNDfire

FundFire, a Financial Times publication, published an article that covered the effort by several mayors to push their city's pension funds to divest from fossil fuel companies. SCERS is discussed in the article, which can be found in full in the Appendix.

Appendix

Fossil fuel company allocation

SCERS Public Equity Allocation to Fossil Fuel Companies

As of December 31, 2020

SCERS Ownership	Account Type	Exposure ($ million)	% of SCERS Total Portfolio
Direct	Separate Account	$24.3	0.7%
Indirect	Commingled Fund	$37.3	1.1%
Total		$61.6	1.7%

Source: Bloomberg, Fossil Free Indexes, SCERS calculation; excludes overlay program, transition holdings

Note: Fossil Fuel companies as defined by the Carbon Underground 200, a list generated by Fossil Free Indices of the top 100 public coal companies globally and the top 100 public oil and gas companies globally ranked by the potential carbon emissions content of their proven reserves; Carbon Underground 200 constituents as of July 2016

FUNDfire

Mayors Want to Divest. Pension Staff, Trustees Have Other Ideas

By Bridget Hickey May 7, 2021

Last September, the mayors of New York, Los Angeles, New Orleans, and Pittsburgh signed a pledge: to take all possible steps to divest from fossil fuel companies and call on their city pensions to do the same.

They are not the first local government officials in the U.S. to do so. Across multiple municipalities, mayors and councilmembers have led the charge to decarbonize pension assets. But some have found that compelling their retirement systems to drop fossil fuels has not been straight forward.

Unlike endowments and foundations, where the movement to divest has steadily gained momentum, only a small number of public pensions have divested from fossil fuel holdings. FundFire identified 10 public pensions that have dropped some of these investments. At many others, staff and trustees tasked with a fiduciary duty to ensure retirees get their benefits remain unconvinced that divestment will not lead to lower returns.

In Seattle, a fight has emerged between the city's mayor, **Jenny Durkan**, and the trustees of the $3.5 billion Seattle City Employees' Retirement System, over whether the pension should ditch fossil fuels.

The mayor wrote to trustees in January requesting that the pension develop a plan to divest from fossil fuels by July and to adopt a 2040 goal for net-zero carbon emissions for its investments. Her call was supported by Seattle City councilmember **Teresa Mosqueda**, who is the chair of the pension's board.

The pension's executive director, **Jeff Davis**, backed by some trustees, declined the mayor's request, however. The pension will instead stick with its current ESG policy, which explicitly rules out divestment, according to a letter from Davis to the Mayor and meeting minutes.

In another example, the **Los Angeles City Council** requested in December that the $21 billion Los Angeles City Employees' Retirement System report within six months on the feasibility of developing a climate transition risk framework and divesting from “uncooperative” fossil fuel companies.

In the pension’s corresponding report, which was submitted to the council in late April, investment staff conclude that the pension’s current ESG risk framework represents a “wider perspective and more inclusive approach,” which “more accurately reflects the Board’s understanding of its fiduciary responsibility to its members and beneficiaries.”

Some officials promoting divestment have had more luck.

In January, roughly four months after he signed the pledge, New York City Mayor **Bill de Blasio** announced that two city pensions would drop an estimated $4 billion in fossil fuel securities, a move expected to be one of the largest divestments in the world, as reported.

But that decision was years in the making.

Trustees first announced their goal to divest within a five-year timeframe in January 2018. The City then undertook an “extensive and thorough fiduciary process” to assess the portfolio’s exposure to fossil-fuel-stranded-asset risk, industry decline, and other financial risks from climate change. Draft reports provided to the pension systems by BlackRock and **Meketa**, published on the **Institute for Energy Economics and Financial Analysis**’ website, provide insight into this process. Both firms identified divestment options they deemed to align with the pensions’ fiduciary duty and protect returns.

Many smaller public pension plans do not have the staff resources or in-house expertise to allow fiduciaries to feel comfortable excluding a specific sector from their portfolio, says **Chris Ito**, CEO and chief investment officer of **FFI Advisors**, the investment manager affiliated with **FFI solutions**, which was formerly known as **Fossil Free Indexes**.

"While politicians and legislators in various legislatures would want to feel like divestment would be important, they should also recognize that as the fiduciary… it does come back to one thing, which is securing the promised benefits of the beneficiary," he says.

New York City’s commitment to divest is a watershed moment, says **Eric Becker**, a partner and portfolio manager at **Clean Yield**, a Vermont-based asset manager that has testified in support of legislation calling for the Vermont and Massachusetts state pension funds to divest.

Related Content

April 13, 2021
New York State Pension Divests from Seven Oil Companies

February 3, 2021
Vermont Pension to Divest from Fossil Fuels

January 26, 2021
New York City Pension Funds to Divest $4B from Fossil Fuels

"It will be much easier for smaller pension funds to follow suit, as fiduciaries can point to New York's action as well as the accumulating research showing that it is consistent with fiduciary duty to do so," Becker says by email. "I expect that the momentum for pension fund divestment will accelerate in the coming years."

Some other pensions have heeded their city officials' calls. Pittsburgh's $826 million **Comprehensive Municipal Pension Trust Fund** is divesting from fossil fuels, for-profit prisons, and guns, in response to a request from Pittsburgh Mayor **William Peduto**, as reported. Peduto, who sits on the pension's board, was a signatory to September's pledge. The **District of Columbia Retirement Board** divested from fossil fuels in 2016 in response to a resolution by the city council, as reported.

In Seattle, Durkan is not the first mayor to implore the city's pensions to divest. Former mayor **Mike McGinn** wrote to the employees' pension and to the **City of Seattle Voluntary Deferred Compensation Plan** as far back as 2012, as reported by climate group **350.org**.

At the pension's January meeting, staff told trustees that the fund had undertaken six studies of fossil fuel divestment since 2013, and that each study had found divestment to be "financially imprudent" and in conflict with the board's fiduciary responsibilities, minutes show.

"We share your belief in the importance of climate change and the risks that it poses," Davis's letter to Durkan states, but the pension's current ESG policy "both recognizes climate change as an important risk to our portfolio and outlines actions we can take that are consistent with our fiduciary responsibilities."

"Through this strategy, we have had an impact beyond what should be expected for a system of our size," he writes.

Mayor Durkan and Councilmember Mosqueda told FundFire in an emailed statement that they "continue to believe that there [are] opportunities for the Seattle City Employees' Retirement System to better incorporate the risks of climate change into their investment decisions and looks forward to continuing to work with the Board Members as they learn more from other cities and states about their decisions to adjust investment decisions to the risks posed by the changing climate."

Davis and the pension's chief investment officer, **Jason Malinowski**, declined to comment for this story.

*Contact the reporter on this story at **bhickey@fundfire.com** or 212-542-1248.*