


2018

Ohio Public Employees Retirement System

# Corporate Governance ANNUAL REPORT





THIS REPORT PROVIDES A HIGH-LEVEL OVERVIEW  
OF THE OPERS CORPORATE GOVERNANCE  
PROGRAM, INCLUDING OUR FOCUS ON  
BOARD DIVERSITY, ADVOCACY, ENGAGEMENT,  
TRANSPARENCY AND STEWARDSHIP.  
YOU'LL ALSO FIND ANNUAL PROXY VOTING  
INFORMATION AND GOVERNANCE HIGHLIGHTS.

# SNAPSHOT

## CORPORATE GOVERNANCE OBJECTIVES

Our goal is to enhance the long-term value of our investments by promoting activities that ensure management and boards of directors act in the best interest of shareowners. We encourage corporate accountability, financial transparency and responsibility while supporting governmental policies and regulations that are in the best interest of OPERS.

## PROXY VOTING

Proxy voting is a primary strategy of the program. OPERS uses a proxy agent for research and a voting platform. Although our proxy agent provides vote recommendations, OPERS votes in accordance with our own proxy voting guidelines.



**\$94.1B**

ASSETS UNDER  
MANAGEMENT



**\$6.1B**

PENSION PAYMENTS

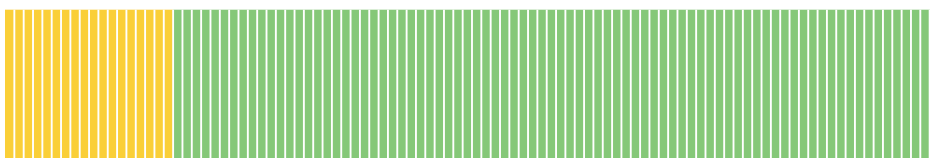


**2/3** (approx.)

OF PENSION  
BENEFITS DERIVED  
FROM INVESTMENT  
EARNINGS



ACTIVE TO  
RETIREE  
RATIO  
1.3:1



**10,388**  
meetings voted

U.S. 1,857

INT'L. 8,531

# BOARD DIVERSITY

The election of directors is perhaps the single most important action shareholders can take as these directors represent shareholder interests within a company. OPERS believes diversity is a key component steering corporate performance. Qualified directors with varied experiential knowledge and backgrounds serving on company boards optimizes performance and protects shareholder value.

We are dedicated to increasing gender diversity within the boardroom. Research indicates gender diverse boards are at an advantage, as they:

- Experience less governance risk<sup>1</sup> (which can lower shareholder returns through reputational damage, etc.)
- Make better decisions due to diversity of thought<sup>2</sup>
- Outperform companies without gender diverse boards<sup>3</sup>

Based on OPERS voting statistics, the number of companies in our holdings with female representation on boards is increasing. We voted against directors at companies that did not show progress towards increasing diversity on their boards. Though there has been a noticeable increase in the number of women on boards, the pace of change is slow.

## Companies in OPERS holdings without women board representation

2016	1410	13.50%
2017	717	6.87%
2018	713	6.78%



### Board Independence Issues: Directors with AGAINST vote

2016	970	53.56%
2017	226	31.39%
2018	173	22.73%

### Over boarded Directors and Executives: Directors with AGAINST vote



2016	226	12.48%
2017	167	23.19%
2018	184	24.18%

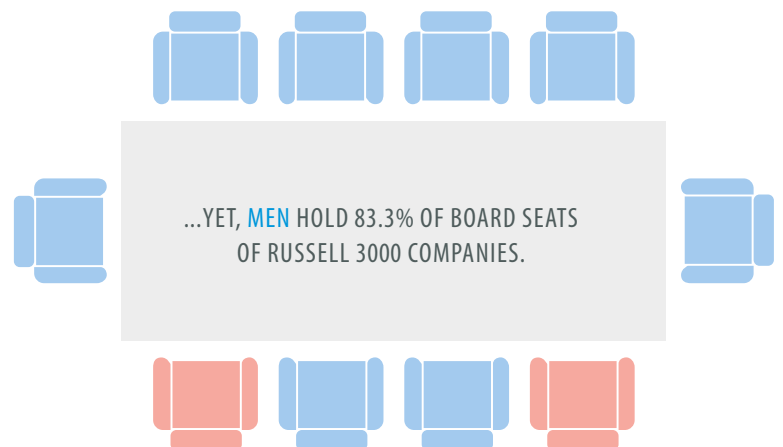
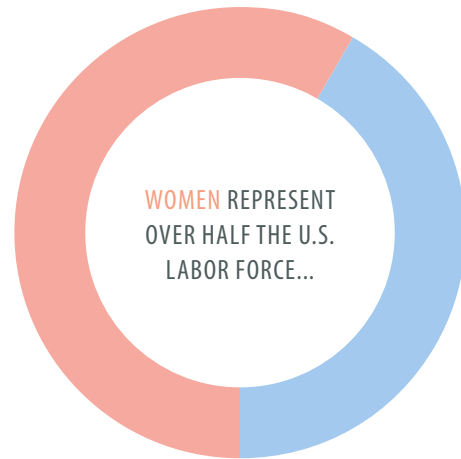
Statistics for our holdings reveal that when there are no women on the board, there are typically issues of board independence and directors being over boarded.

# BOARD DIVERSITY

A 2007 Catalyst study found that companies with more women on their boards performed better than companies with fewer women, relative to metrics such as return on equity, return on sales and return on invested capital.<sup>4</sup> Furthermore, a study examining 2007-2011 board characteristics analyzed the effect of female representation on companies' 2010-2014 financial outcomes. Female representation was found to positively influence firm financial performance as measured by ROA.<sup>5</sup>

Women often gain seats when companies increase the number of seats on their board rather than through the board refreshment process. Half the Russell 3000 companies remain without a single woman on their board.<sup>6</sup> Even though women:

- Are over half of the labor force<sup>7</sup>
- Earned more bachelor's degrees than men since 1982<sup>8</sup>
- Earned more master's degrees than men since 1987<sup>8</sup>
- Earned more doctorate degrees than men since 2006<sup>8</sup>



# ADVOCACY

OPERS Corporate Governance continued advocacy work in 2018 by focusing on governance-related rules and regulatory proposals that impact good corporate governance. When appropriate, Corporate Governance staff collaborated with related organizations to engage companies on governance concerns and comment on regulatory policy and legislation.

In 2018, OPERS submitted comment to the U.S. Senate Chairman and Ranking Member to oppose HR 4015, the Corporate Governance Reform and Transparency Act of 2017. Under HR 4015, proxy advisory firms would be required to share their research reports and proxy voting recommendations with the respective companies prior to publishing. In a letter to the U.S. Senate Banking Committee undersigned by 48 investors (including OPERS), the Council of Institutional Investors (CII) stated its opposition of HR 4015 as follows:

- Grant companies the right to review proxy advisory firms' research reports before the paying customers (i.e., investors) receive the reports
- Mandate that proxy advisory firms hire an ombudsman to receive and resolve corporations' complaints

- Require proxy advisory firms to publish a company's statement "detailing its complaints" in the proxy advisory firms' final reports to their clients, if the ombudsman is unable to resolve these complaints and if the company makes the request in writing
- Increase barriers to new entrants and potentially lead some current proxy advisory firms to exit the industry altogether
- Provide no clear benefits to institutional investors

OPERS is aware of criticisms surrounding the proxy advisory firms and the purported influence over proxy voting decisions. To govern our own proxy voting decisions, the OPERS Board of Trustees adopted a Corporate Governance Policy and Proxy Voting Guidelines. As noted in our [comment letter to the U.S. Senate Banking Committee](#), OPERS makes all voting decisions independently, and all OPERS proxy votes are cast in alignment with the guidelines and implemented via a custom vote policy with our proxy advisory firm. Staff also performs an annual review of the custom vote policy.



# ADVOCACY

The Securities and Exchange Commission (SEC) finalized a pay ratio-disclosure rule in 2018 requiring certain publicly traded companies to disclose the ratio of the compensation of the CEO to that of the median employee. OPERS joined with several other [investor signatories](#), representing \$3.3 trillion in assets under management, to request that fortune 500 companies provide supplemental pay ratio disclosures in the proxy statement.

Examples of supplemental disclosures were provided to the companies for consideration:

- Identification of the median employee's job function
- Breakdown of the workforce by job function and/or business unit
- Geographic location of the median employee
- Country-level breakdown of global employee headcount
- A breakdown of full-time vs. part-time employment status

- Use of temporary or seasonal employees
- Use (or non-use) of subcontracted workers
- Tenure and experience of the workforce
- Workforce education levels and skillsets
- The company's overall compensation philosophy
- Employee compensation mix (benefits and incentives)
- Alignment of CEO pay practices with pay practices for other employees

Lastly, in 2018 we worked with Ohio state legislators to introduce [House Concurrent Resolution \(HCR\) 23](#) to encourage equitable and diverse gender representation on boards and in senior management of Ohio companies and institutions. Former Rep. Dorothy Pelanda (R-Marysville) sponsored the resolution with 11 co-sponsors. Staff are working with potential sponsors to reintroduce the resolution in 2019.

# ENGAGEMENT

The OPERS Corporate Governance staff engages directly with companies to address long-term performance risks and affect change. We maintain a dialogue with these companies and have frequent opportunities to connect on issues of proxy voting, analysis and corporate governance topics. Engaging the companies in which OPERS invests in this manner improves reporting and disclosure.

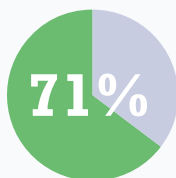
We work alongside national and international colleagues to engage with U.S. companies that lag behind their peers respective to board diversity. We reach out when there is poor female representation on boards or long-tenured directors. OPERS is part of three coalitions aimed specifically at increasing gender diversity on boards: [The Thirty Percent Coalition](#), [The Midwest Investors Diversity Initiative \(MIDI\)](#) and the [Coalition for U.S. Board Diversity](#).

“SHAREHOLDER ENGAGEMENT IS A HALLMARK OF OUR PUBLIC CAPITAL MARKETS, AND THE PROXY PROCESS IS A FUNDAMENTAL COMPONENT OF THAT ENGAGEMENT.”

*SEC Chairman Jay Clayton*

## Coalition for U.S. Board Diversity

Our member organizations are global investors representing a combined **\$2.5 trillion** assets under management as of Jan. 31, 2019.



**Success to date**  
**51 of 72** companies have appointed at least one woman to the board

## Topics for Discussion

We ask companies to consider taking **four concrete actions**:

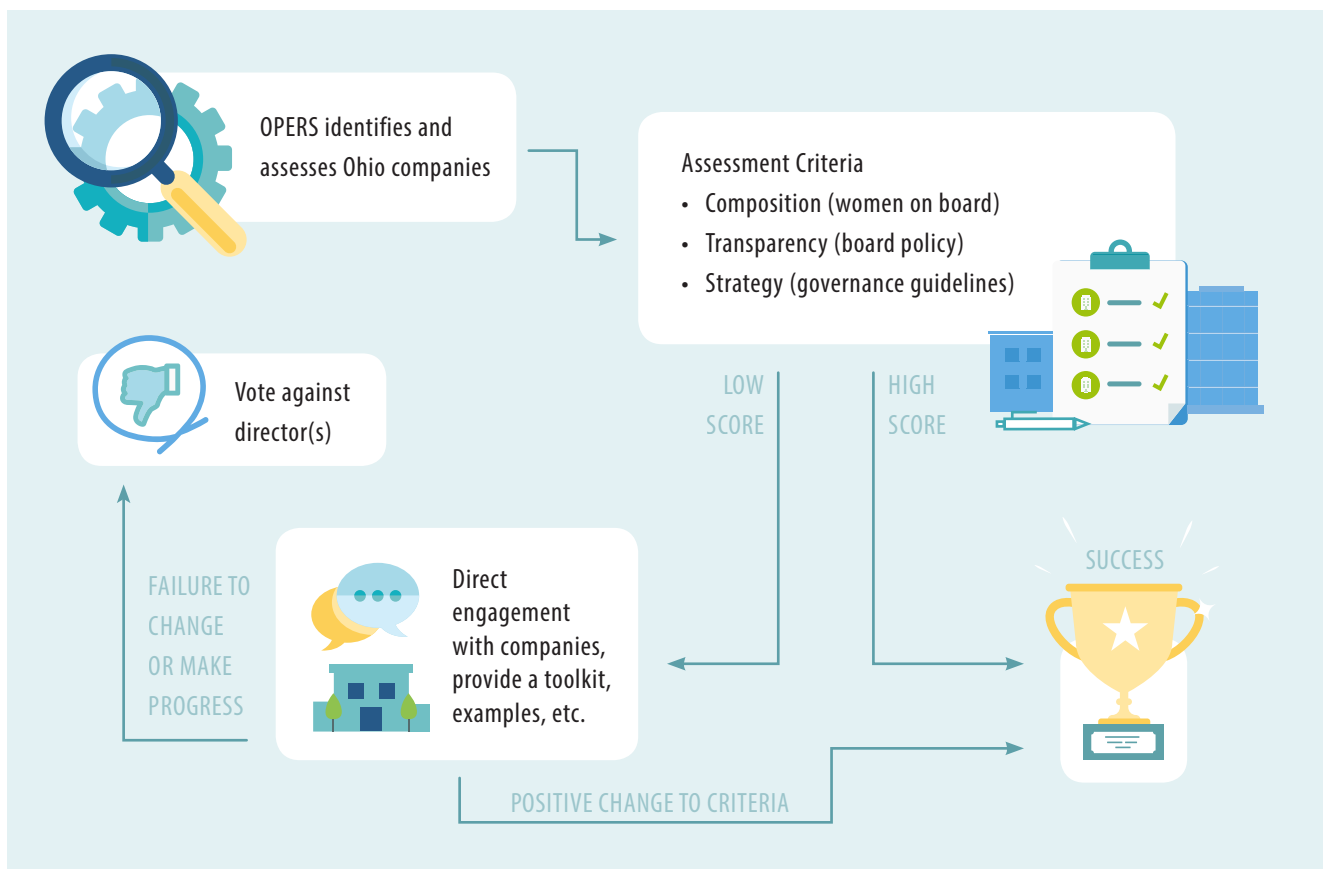
-  **Disclose** in the company's proxy the board's skill set and alignment to the company's strategy
-  **Affirm** in governance policies and committee charters a commitment to incorporate the "Rooney Rule" – a commitment to identify qualified candidates of diverse gender, racial and ethnic background for board nomination
-  **Attest** in governing documents that director searches will consider suitable nominees from corporate backgrounds beyond the executive suite (academia, government, nonprofit, etc.)
-  **Commit** to increase gender parity on the board



# ENGAGEMENT

In addition, OPERS continued our own board diversity initiative (initiated in 2017), engaging Ohio companies where there were fewer than two women on the board. The initiative promotes diversity in board composition while sharing the benefits of a diverse board, including: lowered risk of governance issues, increased decision making and higher profits.

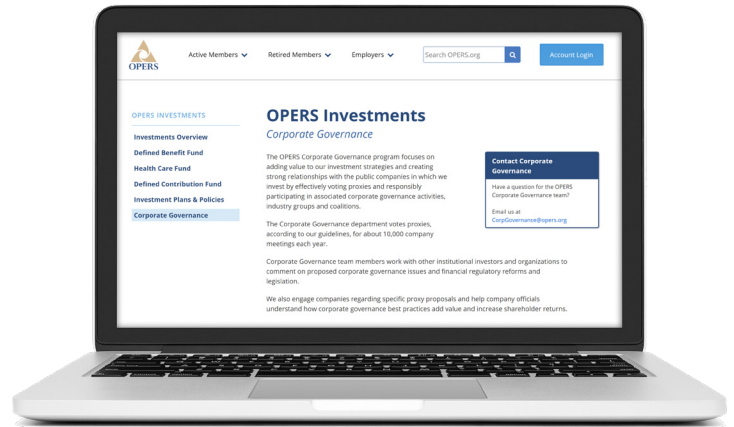
Following our initial analysis, we have been engaging constructively with those Ohio companies to discuss the company's philosophy on board diversity, board refreshment, and board recruitment. If a company fails to meet our minimum standards to make progress toward increasing gender diversity on their boards, we may cast a vote against company directors.



*The OPERS Model of Engagement is based upon quiet diplomacy, which means we initiate discussion with companies and ongoing engagement to influence movement towards governance best practices.*

# TRANSPARENCY

Just as OPERS requests transparency from the companies in which we invest, we support transparency through our Corporate Governance Program as well. Our vote results are available online the day following a meeting. Likewise, our [Corporate Governance Policy](#) and [Proxy Voting Guidelines](#) are also accessible online.



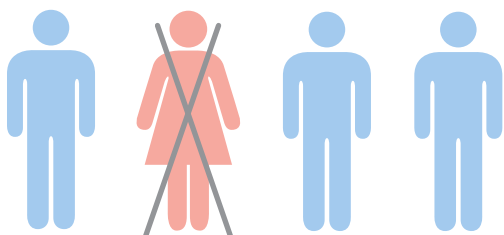
Search for **CORPORATE GOVERNANCE** to view the Policy, Guidelines or voting disclosures on [opers.org](http://opers.org).

# STEWARDSHIP

It is our fiduciary responsibility to ensure proxies are voted in the best interest of our current and future retirees. We consider our proxies to be plan assets. We take the utmost care to review the policy and guidelines and align with best practices. In fact, 2018 was the first year OPERS voted against directors who failed to make progress toward increasing gender diversity on their boards.

Once we've engaged a company, we look for text changes in its nominating and governance committee charter to substantiate a commitment to diversity. We also discuss board refreshment with companies to gauge whether they explore non-traditional sectors, such as academia, not-

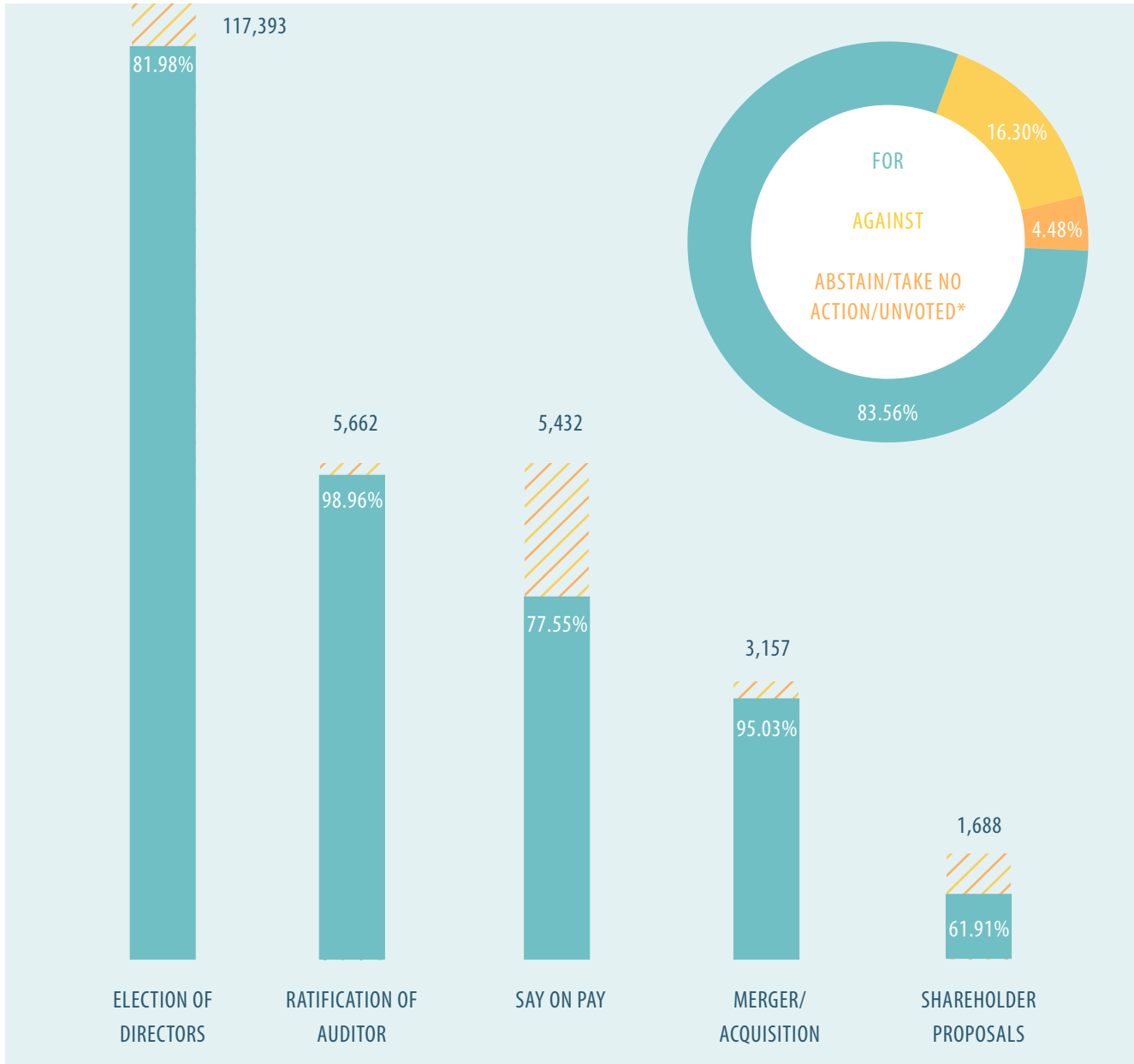
for-profit or government, when searching for candidates. Whether working on their own or in conjunction with a search firm, it is important to include diverse candidates in every candidate pool. Statistics suggest that it's virtually impossible for a woman to be elected to a board seat when there is only one female candidate in the candidate pool. We expect the board to select the best candidates, but also understand there is no shortage of diverse candidates available. Throughout 2018, our company engagements revealed that many are open to first time board candidates – a positive trend that we applaud when coupled with a comprehensive mentoring or onboarding program.



*"Statistics suggest that it's virtually impossible for a woman to be elected to a board seat when there is only one female candidate in the candidate pool!"<sup>9</sup>*

# PROXY VOTING STATISTICS

OPERS approved votes on 10,388 public company proxies covering 251,403 total proposal items. Below are the top five proposal topics and cumulative statistics.



\* VOTE OPTIONS OPERS MAY CAST WHEN NO OTHER VALID OPTION EXISTS, THE COMPANY IMPLEMENTS SHAREBLOCKING, OR OUR POSITION WITH THE COMPANY HAS TRADED DOWN TO ZERO SHARES.

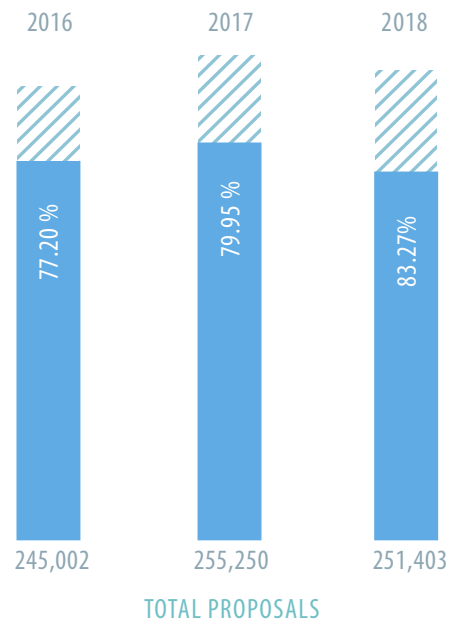
# PROXY VOTING STATISTICS

Director elections represent one of the most critical areas in voting since shareowners rely on the board to monitor executive management.

OPERS staff supported 81.98 percent of individual nominees for boards of directors, voting against any remaining directors primarily due to concerns with the candidate's independence, attendance at meetings, board seats and/or overall board performance.

We also withhold votes from directors who fail to observe good corporate governance practices or clearly show disregard for the best interests of shareowners.

While our Corporate Governance staff is not predisposed to disagree with company management recommendations, some management positions may not be in the best interest of all shareowners. So, we analyze and evaluate all vote recommendations to determine if they fall in line with our policy and guidelines. Particular attention is paid to decisions related to director elections, executive compensation, proposed mergers and acquisitions and companies that appear on a watch list.



Votes consistent with management

*Of all the votes cast, over 83 percent were consistent with the company management recommendations.*

# GOVERNANCE HIGHLIGHTS

## KEY GOVERNANCE ISSUES FOR THE YEAR.

### The #MeToo movement

How were boards thinking about mitigating the risk of sexual harassment within the workplace? Some notable cases emerged, such as the Google walkout that started in Asia and spread across continents.<sup>10</sup> ISS lists equality in the workplace as one of the top 10 governance topics to watch as a result of #MeToo, which primarily addresses concerns over sexual harassment, but touches also on the gender pay gap, workplace discrimination and gender diversity.<sup>11</sup>



REUTERS/Jeenah Moon

### Enhanced disclosure around board composition

Shareholders were interested in seeing the tie between a director's skill set and the long-term strategy of the company. An institutional investor survey by Morrow Sodali cited the skill of each director as the most critical factor.<sup>12</sup>



# GOVERNANCE HIGHLIGHTS

## **Increasing gender diversity on boards**

State Street announced policies to start voting against directors whose boards were not diverse.

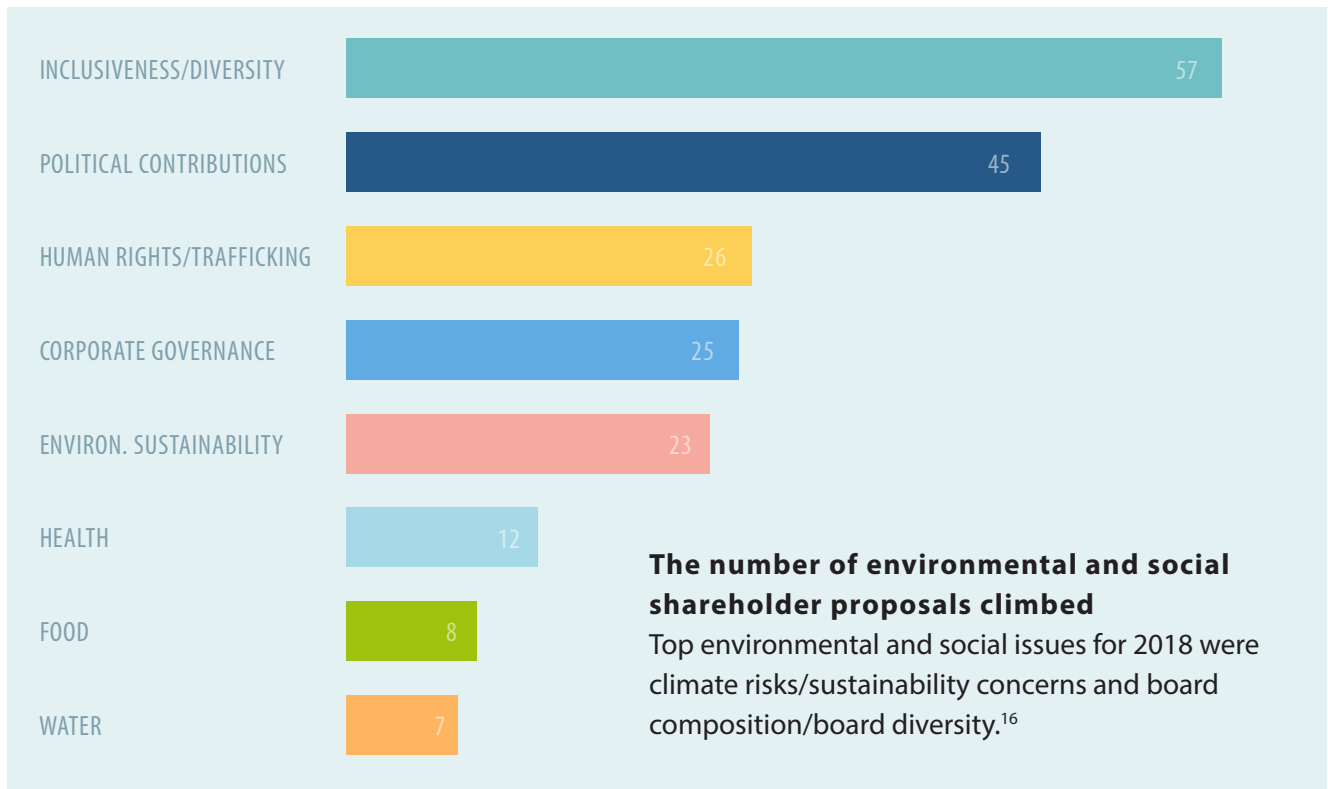
State Street's policy will be effective for the 2020 proxy voting season and will target firms that have no women representation on their boards and have failed to engage in "successful dialogue on State Street Global Advisor's board diversity program for three consecutive years."<sup>13</sup> BlackRock's 2018 proxy voting guidelines indicated they "may" vote against nominating/governance committee members of companies without board diversity.<sup>14</sup>

Proxy advisory firms Glass Lewis and ISS announced their recommendations would begin to reflect a vote against directors without a diverse board. Glass Lewis will recommend a vote against nominating committee chairs at companies without board diversity beginning in 2019 for companies in the Russell 3000 Index unless the company can provide sufficient rationale for the lack of diversity.<sup>15</sup>

ISS will recommend voting against nominating committee chairs and potentially other directors beginning in the 2020 proxy season unless certain mitigating factors apply.<sup>15</sup>



# GOVERNANCE HIGHLIGHTS



*Interfaith Center on Corporate Responsibility*

**FIRMS DISCLOSING HUMAN CAPITAL COSTS OUTPERFORM NON-DISCLOSERS IN TERMS OF VALUE CREATION.**

## **Shareholders requested more disclosure around human capital management metrics.**

OPERS is a member of the Human Capital Management Coalition (HCMC), which submitted a [petition](#) to the SEC outlining eight metrics for disclosure if relevant to the industry at hand. The current disclosure requirements are limited and include only the number of employees, median compensation and CEO compensation.<sup>17</sup>

Institutional investors are interested in how companies are investing in their workforces. Studies have found there is a positive correlation between human resource initiatives and investment outcomes, such as total shareholder return, return on assets, return on investment and return on capital employed.<sup>18</sup>

# GOVERNANCE HIGHLIGHTS

**Companies were required to include the pay ratio disclosure on their proxies, transparently reflecting the ratio between the CEO and the median worker's pay.**

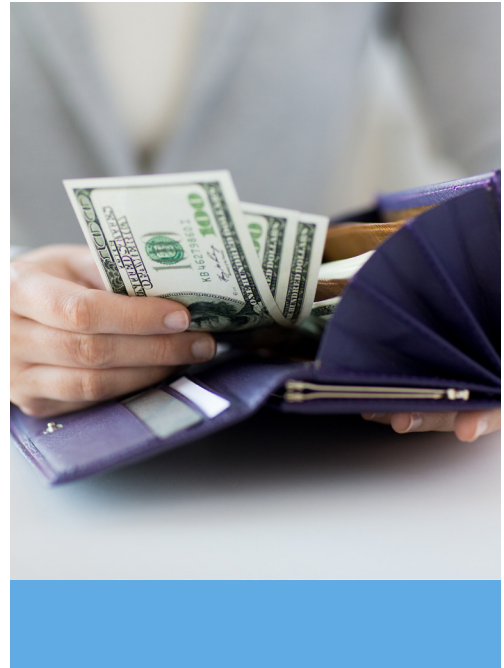
This requirement was part of the Dodd-Frank Wall Street Reform and Consumer Protection Act signed into law in 2010 and applied to fiscal years ending on or after Dec. 31, 2017.<sup>19</sup>

The ratio of the CEO's annual pay to the median-paid employee varied by industry and company size as expected. Shareowners are evaluating the new data and requesting enhanced disclosures to learn more about pay policies and the workforce structure. Late in the year, OPERS joined a group of pension funds asking S&P 500 companies to provide more information about their workforce in 2019.<sup>20</sup>

**The SEC held a staff roundtable to evaluate topics, including proxy advisory firm's influence over voting, proxy plumbing and shareholder proposals.**

While the year ended without definitive direction, data does not support the position that proxy advisory firms exercise undue influence over the voting habits of institutional investors. The two largest firms, Glass Lewis and ISS, each report the majority of their largest clients have their own proxy voting guidelines that are used to cast their votes, whether done so automatically via the firm's voting platform/workflow or evaluated manually by the client's staff. OPERS participated in the roundtable as the only pension system on the panel evaluating proxy advisory firms.

OPERS continues to advocate against additional regulation that could result in lengthened timeline to receive the proxy report, reduced independence of research provided by the firms, or costs passed along to the institutional investor.



*Image courtesy of the Securities and Exchange Commission*



# GOVERNANCE HIGHLIGHTS

**On Sept. 30, 2018, Gov. Jerry Brown signed Senate Bill 826, making California the first state to pass legislation requiring women on corporate boards.**



[SCR62](#)  
CA. 2013

A resolution encouraging equitable and diverse gender representation on corporate boards and a specific number of female directors on boards by 2016.

[S1007](#)  
MA. 2015

A resolution seeking equitable and diverse representation on boards by encouraging companies doing business in the state to adopt policies and practices that increase gender diversity on boards and publicly disclose how many women serve on their boards.



[HR0439](#)  
IL. 2015

A resolution encouraging equitable and diverse gender representation on corporate boards.

[HJR1017](#)  
CO. 2017

A resolution to increase the presence of women on corporate boards of directors.



[HR273](#)  
PA. 2017

A resolution urging businesses to reach a board membership that is 30% women by 2020 and to publicly track goal progress.

[HCR23](#)  
OH. 2018

A resolution encouraging equitable and diverse gender representation on the boards and in senior management of Ohio companies and institutions.



[BILL 826](#)  
CA. 2018

A bill requiring a specific number of women on boards of directors by 2019 and more by 2021. Authorizes fines for non-compliance.

LOOKING FORWARD TO THE 2019 PROXY VOTING SEASON, THE OPERS CORPORATE GOVERNANCE PROGRAM WILL REMAIN FOCUSED ON ACTIVITIES THAT STRENGTHEN COMPANY PERFORMANCE AND INCREASE SHAREHOLDER RETURNS.

AS EMPHASIS ON SUSTAINABILITY GROWS, WE INTEND TO ENGAGE COMPANIES THAT LAG THEIR PEERS IN DISCLOSING SUSTAINABILITY FACTORS TO INVESTORS IN AN EFFORT TO MITIGATE GOVERNANCE CONCERNS.

WE'LL ALSO CONTINUE TO ADVOCATE FOR PUBLIC COMPANIES HEADQUARTERED IN OHIO TO INCREASE GENDER PARITY ON THEIR BOARDS AND WILL SEEK A NEW SPONSOR FOR AN OHIO RESOLUTION.

LASTLY, OUR EMPHASIS ON BOARD DIVERSITY, ADVOCACY, ENGAGEMENT, TRANSPARENCY AND STEWARDSHIP WILL CONTINUE.

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