

# 2019

Ohio Public Employees Retirement System

# Corporate Governance ANNUAL REPORT



## PURPOSE

The reason for which something exists or is done, created or made, etc.

An intended or desired result; end; aim; goal.

Determination; resoluteness.



IN 2019, THE BUSINESS ROUNDTABLE REDEFINED THE PURPOSE OF A CORPORATION, IN TURN MOVING AWAY FROM SHAREHOLDER PRIMACY IN FAVOR OF COMMITMENT TO ALL STAKEHOLDERS. **THIS YEAR'S CORPORATE GOVERNANCE REPORT IS PRESENTED THROUGH THE LENS OF PURPOSE.** INSIDE YOU'LL FIND A HIGH-LEVEL OVERVIEW OF THE OPERS CORPORATE GOVERNANCE PROGRAM, INCLUDING OUR COMMITMENT TO BOARD DIVERSITY, ADVOCACY, ENGAGEMENT, TRANSPARENCY AND STEWARDSHIP. THIS REPORT ALSO PROVIDES INSIGHT ON OUR ANNUAL PROXY VOTING ACTIVITY AND GOVERNANCE HIGHLIGHTS.



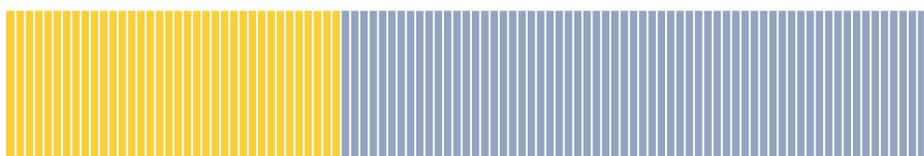
# SNAPSHOT

## OPERS MISSION

To provide secure retirement benefits for our members.

## 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.



**10,200**  
meetings voted  
MEETINGS MANUALLY  
REVIEWED BY OPERS  
STAFF - 3,500



# THE PURPOSE OF A CORPORATION

Aug. 19, 2019 marked a pivotal point on the corporate governance landscape. The Business Roundtable announced they updated their statement on the purpose of a corporation. This was the first time shareholder primacy was downgraded to equal rank among all stakeholders. The statement was signed by 181 CEOs committed to aligning their companies to benefit all stakeholders – customers, employees, suppliers, communities and shareholders.

The new statement drew much debate and headlines. OPERS professes that corporations with exemplary corporate citizenship are more likely to be sustainable. The new statement appeared to lessen managerial accountability to shareholders.

“...Boards and managers need to sustain a focus on long-term shareholder value. To achieve long-term shareholder value, it is critical to respect stakeholders, but also to have clear accountability to company owners”.

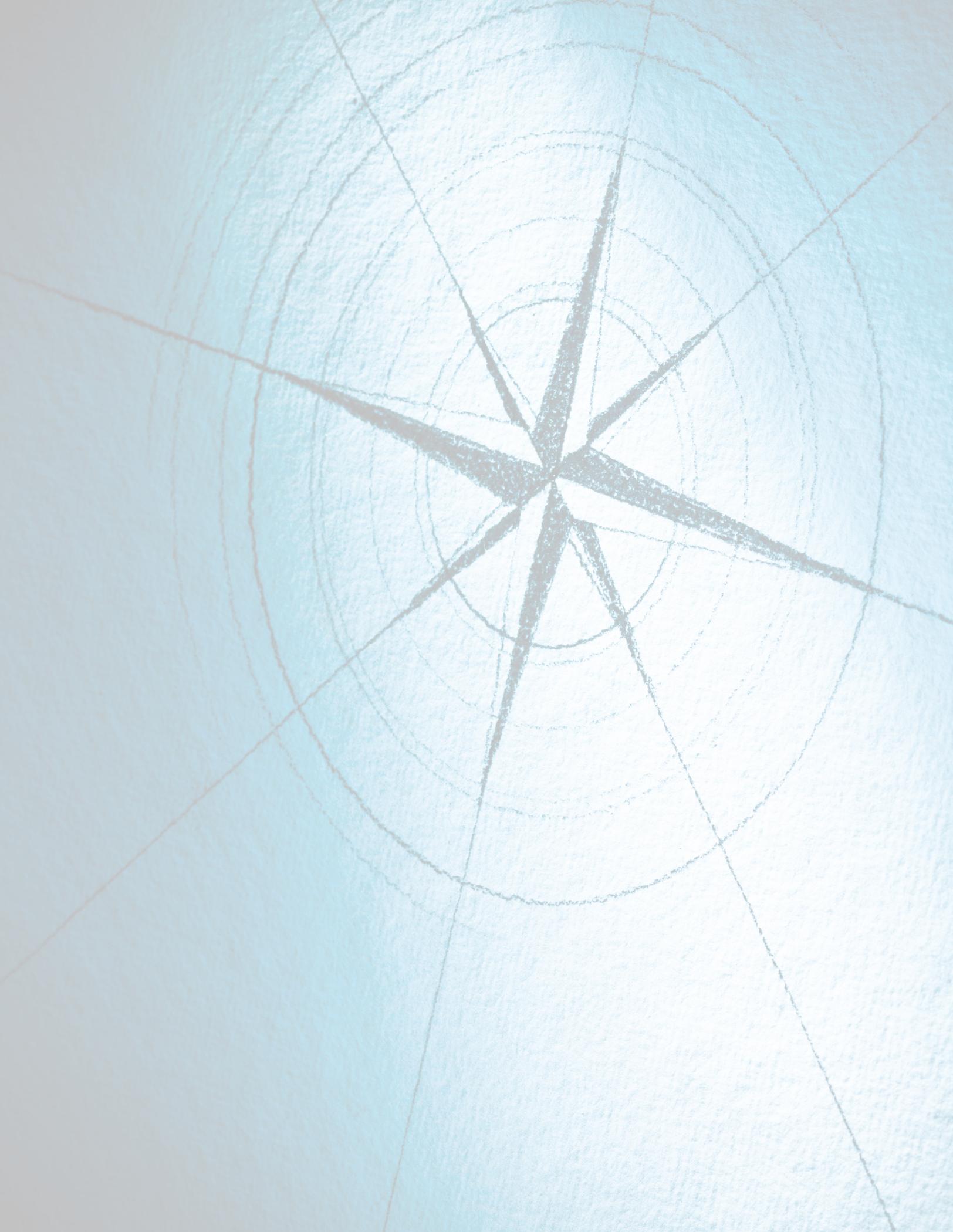
The Council of Institutional Investors (CII) responded to the Business Roundtable stating, “CII believes boards and managers need to sustain a focus on long-term shareholder value. To achieve long-term shareholder value, it is critical to respect stakeholders, but also to have clear accountability to company owners.”<sup>1</sup> OPERS agrees with CII’s position. Corporate governance consistently initiates discussion as the first means of enacting change. OPERS has been successful in addressing human capital management concerns, board gender diversity and other governance issues.

Shortly following the Business Roundtable’s updated statement, the U.S. Securities and

Exchange Commission (SEC) proposed new regulations including: Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice<sup>2</sup> and Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8<sup>3</sup>. These rules were intended to modernize the proxy process, but appeared to many investors to be a solution in search of a problem. OPERS advocated against regulation but requested that if the SEC was intent on making changes, it would do so in a way to maintain the independence of research, without increases to costs for proxy advisory firm services and/or the timeline for investors to review the research they purchase from PAFs. The proposed regulations were released Nov. 5, 2019, and provided a short 60-day window for comment, closing the year on a note of diminished shareholder rights.

OPERS is diligent regarding the funds used to purchase services from proxy voting advisors and performs monthly audits to ensure compliance with our proxy voting policy and guidelines. OPERS also performs daily share reconciliation to ensure we are upholding our fiduciary duty to vote all shares and proxies in the best interest of members and beneficiaries.

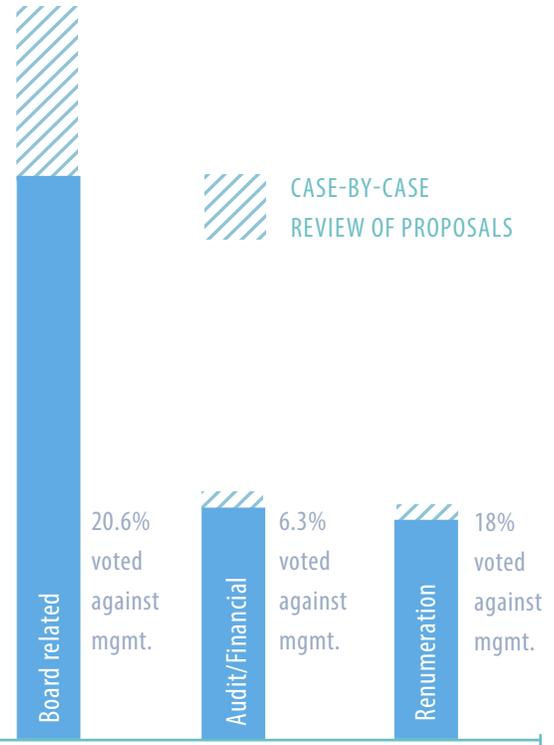
There is an unsupported assumption that institutional investors “robo-vote” or simply vote according to their PAF’s recommendations. This is a point of contention for issuers, some of whom claim proxy voting advice contains errors. Without an economic impact study performed prior to rulemaking, OPERS can only rely on our organization’s own experience, which does not support automatic vote alignment with our PAF, nor does it suggest an abundance of errors.



# PROXY VOTING

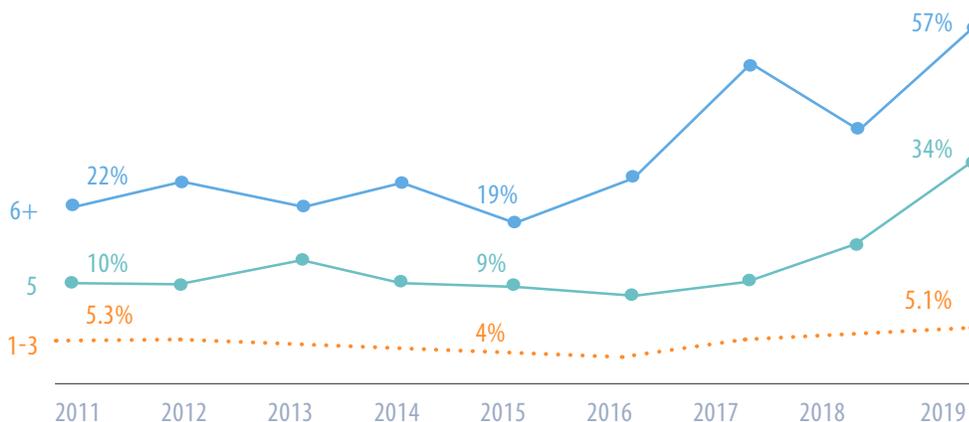
Proxy voting is the primary means for a shareholder to influence a public company's operations, corporate governance or ESG (environmental, social or governance) activities. OPERS votes proxies to optimize long-term shareholder returns, as over two-thirds of retirement benefits are funded from investment returns. OPERS' corporate governance program concentrates on the 'G' in ESG – governance best practices that mitigate risk and increase shareholder returns. We evaluate environmental and social proposals by management and shareholders on a case-by-case basis, balancing the issue against the best interest of our members and beneficiaries.

During the 2019 proxy season OPERS customized vote guidelines were applied to over 10,200 unique meetings in 66 different markets. Roughly one-third, or 3,500 meetings, were manually reviewed and voted by OPERS staff.



OF PROPOSALS VOTED, APPROXIMATELY 81% WERE RELATED TO BOARD, AUDIT AND COMPENSATION.

Voting against directors considered to be over-boarded was a trend during 2019. Large asset managers implemented stricter policies regarding the number of board seats a director can hold. Harvard Law reports a review by ISS of the Russell 3000 indicates four board seats is the new standard for non-CEO directors.<sup>4</sup>



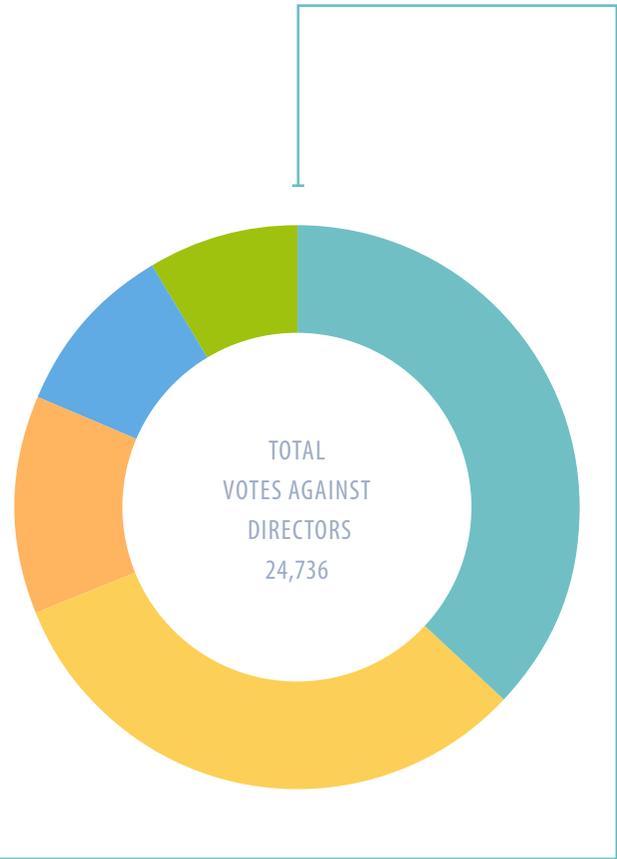
PERCENTAGE OF NON-CEO DIRECTORS WHO RECEIVED SUPPORT BY LESS THAN 80% OF VOTES CAST BY TOTAL NUMBERS OF BOARDS SERVED AND BY YEAR.

ISS COVERAGE - RUSSELL 3000

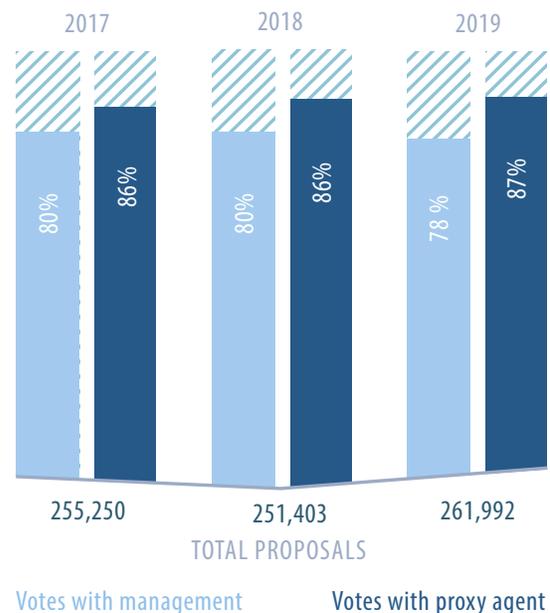
# PROXY VOTING

Of the board-related votes OPERS cast against directors, the reason in order of magnitude was:

- 37% A non-CEO director sat on more than four boards
- 32% Nominees were considered insiders or affiliates and sat on the nominating/governance, audit or compensation committees
- 13% The board was not sufficiently independent
- 10% An executive director of a public company that sat on more than two public company boards
- 8% Nominees continually served on the compensation committee and the company received a pay for performance grade of F or D or lower in two consecutive years



OPERS' vote history does not support issuer claims that investors automatically vote against management and in alignment with proxy advisory firms. Our votes are cast according to our own corporate governance policy and proxy voting guidelines.



# BOARD DIVERSITY

Diversity continues to be a hot topic within the corporate governance landscape. Most company board directors agree on the benefits of a diverse board, and yet change continues to be slow in this area. We understand the role of the board is to identify and evaluate risks and opportunities

...We believe a board must be experienced, collaborative and possess a breadth of diverse perspectives...

as they relate to the organization’s mission. To do this, we believe a board must be experienced, collaborative and possess a breadth of diverse perspectives to foster robust discussions and make well-rounded decisions. Additionally, diversity has a proven economic impact. It is statistically proven that companies with diverse boards outperform companies lacking diversity. Most board directors

are keenly aware their performance on the board greatly increases when gender diversity, cultural diversity, diversity of thought, and diversity of perspectives are rampant around the board table. As a long-term investor, OPERS’ focus is on increasing shareholder returns, thus the case for focusing on board diversity.

We believe corporations that are slow to increase diversity on their boards will be met with increasing regulatory pressure. Regulatory bodies have moved from making recommendations to issuing quotas, in addition to demanding enhanced compliance and/or explanation. Without voluntary action to increase board diversity, future legislative remedies may force the issue. OPERS does not favor quotas, but rather chooses to collaborate with companies to discuss succession planning strategies and raise awareness of pipelines of board-ready candidates possessing the skill sets companies seek.

## Companies in OPERS holdings without women board representation

2016	1,410	13.50%
2017	717	6.87%
2018	713	6.78%
2019	1,267	12.27%

*The large increase in companies in OPERS’ holdings without gender diverse boards is directly attributable to markets that have significantly fewer women serving on boards of directors where our holdings almost doubled from 559 companies in 2018 to 10,327 in 2019.*

# BOARD DIVERSITY

OPERS is part of two coalitions aimed specifically at increasing gender diversity on boards: The Thirty Percent Coalition and The Midwest Investors Diversity Initiative (MIDI).

Members of The Thirty Percent Coalition include public and private companies, professional services firms, institutional investors, government officials and advocacy groups. Together, it represents \$6 trillion in assets under management.

Formed in 2016, MIDI is a coalition of Midwest institutional investors representing \$873 billion assets under management and advisement.

Both groups are dedicated to increasing racial, ethnic, and gender diversity on corporate boards to protect shareholder value and maximize returns.

## 2019

### NOTABLE ACHIEVEMENTS OF THE THIRTY PERCENT COALITION

- 85** Companies appointed a woman to their board for the first time
- 16** Companies appointed a second woman
- 28** Companies adopted public language committing to diversity in their governance documents
- 30** Shareholder proposals filed urging action and disclosure on board diversity
- 27** Proposals were withdrawn due to investor engagement leading to mutually agreeable outcomes

## MIDI

### WORKS WITH COMPANY NOMINATING AND GOVERNANCE COMMITTEES TO:

-  Adopt a policy for diverse search
-  Require female candidates to interview for every open seat
-  Instruct search firms to include such candidates in the initial pool
-  Expand pool to include candidates from non-traditional sources

## 2019

### SUCCESSFUL ENGAGEMENTS WITH OIL, TECHNOLOGY, TRANSPORTATION AND FINANCE COMPANIES

- 8** Adopted a diverse search policy
- 6** Added a diverse candidate



# ADVOCACY

Shareholder advocacy encompasses strategies investors use to effectively engage with companies in their investment portfolios about environmental, social and corporate governance issues. In addition, investors often weigh in on public policy when legislators seek to strengthen or weaken regulations that govern the activities of corporations. OPERS' advocacy efforts include: submitting feedback during public comment periods, attending hearings and meeting with representatives on Capitol Hill.

The OPERS corporate governance program collaborated with related organizations and peers to engage the U.S. Securities and Exchange (SEC) Commissioners, the Office of the Investor Advocate, the Division of Finance and various legislative staffers on governance concerns and commented on regulatory policy and legislation.

Our Efforts focused on opposing additional regulation on proxy advisory firms that would increase costs to OPERS and other investors, decrease independence of research and shorten the timeframe to review the research prior to voting proxies. The year closed during the comment period.

OPERS also advocated for a blended *rules-based* and *principles-based* approach to proposed changes to *Regulation S-K* to include distinct universal metrics investors use most often for comparison and decision-making, which include the number of people employed, the total cost of the *issuer's* workforce, turnover and workforce diversity data.

## RULES-BASED

A prescribed approach to regulation that instills the code into law with appropriate penalties for transgression.

## PRINCIPLES-BASED

Requires a company to adhere to the spirit rather than the letter of the code. Each company determines how to achieve the outcome of the regulation.

## REGULATION S-K

A prescribed regulation under the US Securities Act of 1933 that lays out reporting requirements for various SEC filings used by public companies. It serves as the central repository for non-financial statement disclosures.

## ISSUER

Companies are also often called issuers (issuing or contemplating issuing shares). They fund their investment activities from the sale of securities.

# ADVOCACY

Locally, Representatives Thomas West (D-Canton) and Sara Carruthers (R-Hamilton) sponsored House Concurrent Resolution 13 (HCR 13)<sup>5</sup> to encourage equity and diversity in Ohio corporate government. It was introduced and referred to the Civil Justice Committee where it received two hearings before the end of the year. Since its introduction, HCR 13 has gained 19 additional co-sponsors, which may provide the impetus behind successful passage by the end of 2020, raising awareness of the positive correlation between gender diverse boards and increased shareholder returns.



“Passing this resolution shows the state is taking the first step in recognizing that increasing gender diversity and equity in corporate leadership would make Ohio a better place to live, work and retire with security.”

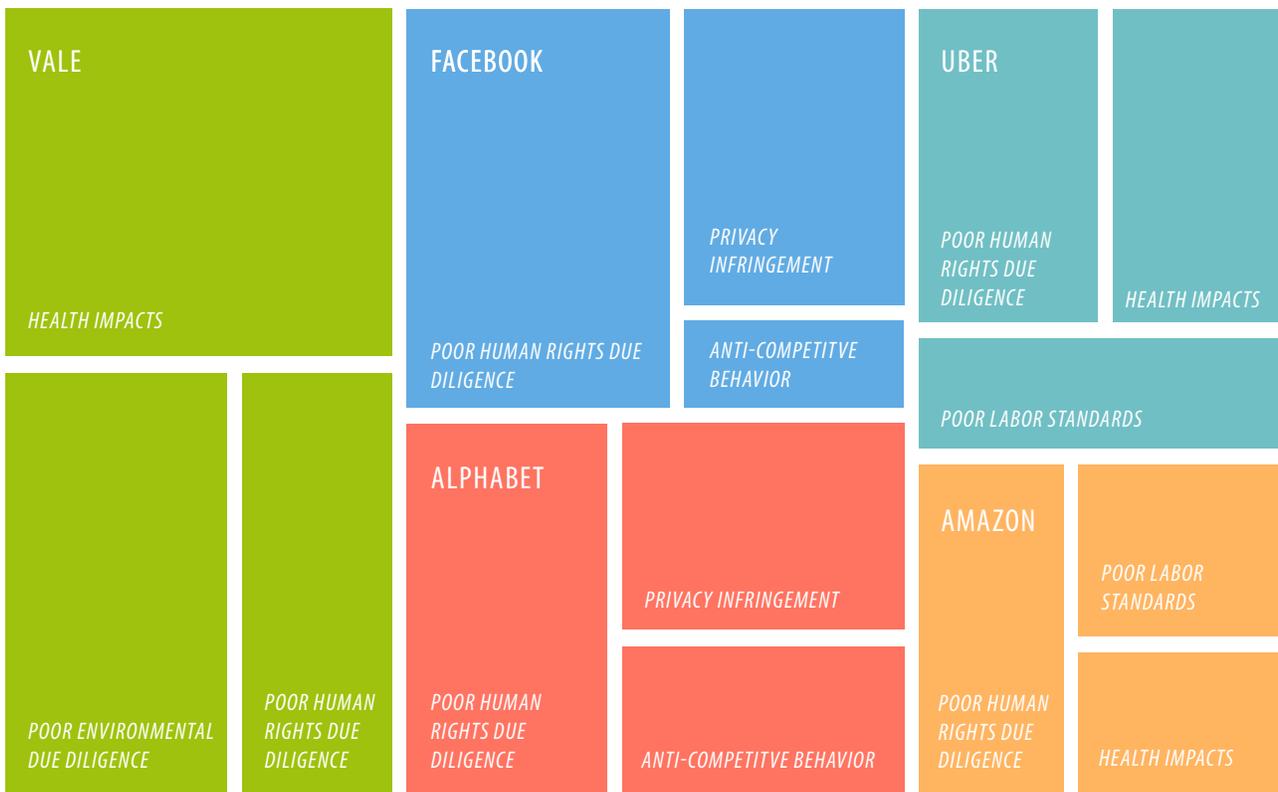
*- Rep. West introducing the resolution in Sept.*

# ENGAGEMENT

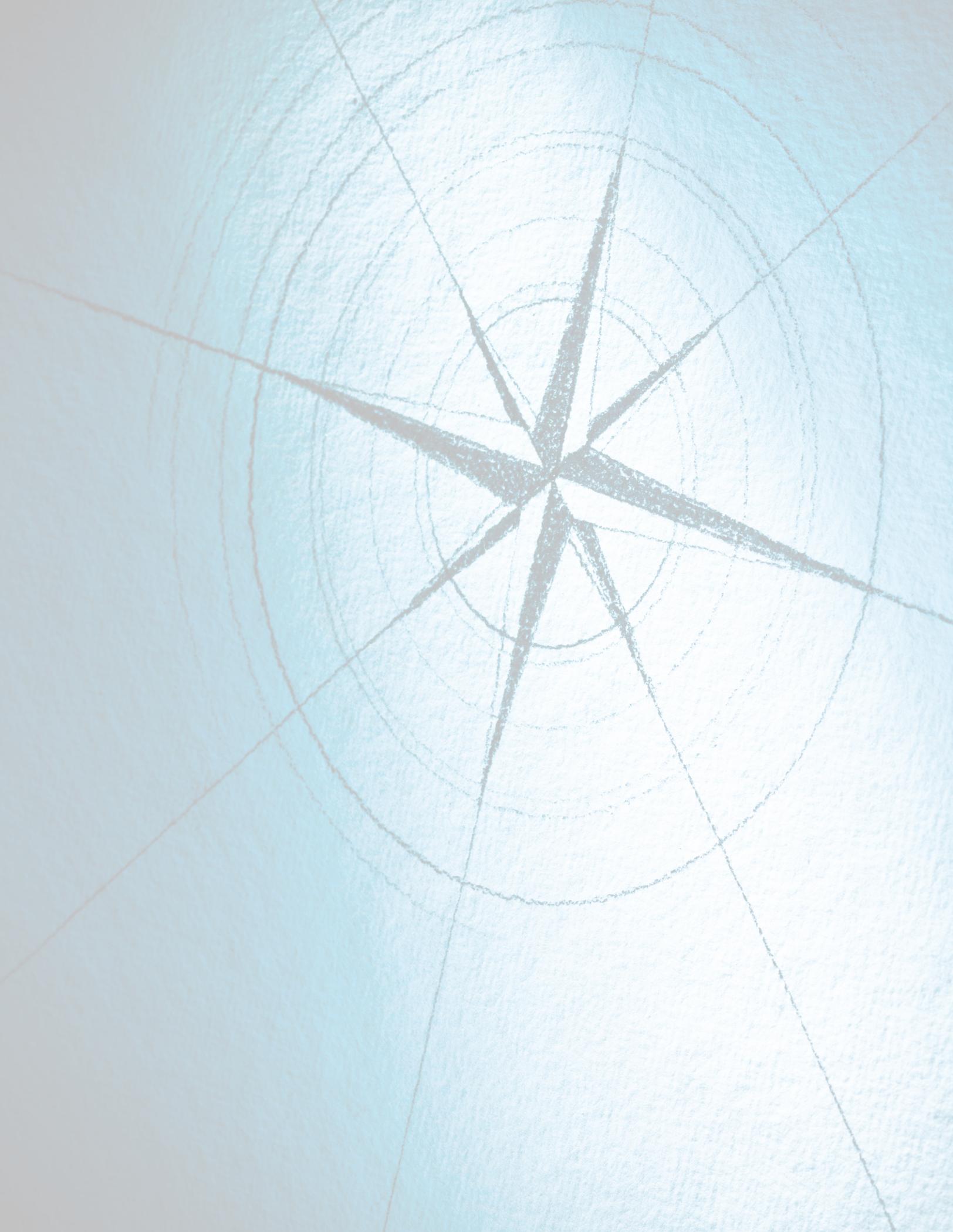
Companies that have strategically increased shareholder engagement have found the practice provides a reliable source of communication directly from shareholders. Shareholders are meeting one-on-one with company representatives to discuss governance issues, company performance and board practices. Shareholder engagement is important to OPERS because it allows staff to personally interact with members of management teams and directors to discuss governance issues. It is also a reliable way for companies to gain shareholder perspective.

The OPERS corporate governance program is built on a platform of quiet diplomacy. We aim to engage companies to address risks and affect change. Based on the density of corporate controversies in the news during 2019, the five highest exposed companies are depicted below.

MOST CONTROVERSIAL COMPANIES<sup>6</sup>



REPUTATIONAL RISK CAN LEAD TO DIMINISHED VALUE FOR SHAREHOLDERS. ENGAGEMENT ENABLES SHAREHOLDERS TO RAISE CONCERNS, LEARN HOW COMPANIES ARE MITIGATING RISK AND COLLABORATE TOWARD IMPLEMENTING CORPORATE GOVERNANCE BEST PRACTICES. SOURCE: ISS ESG



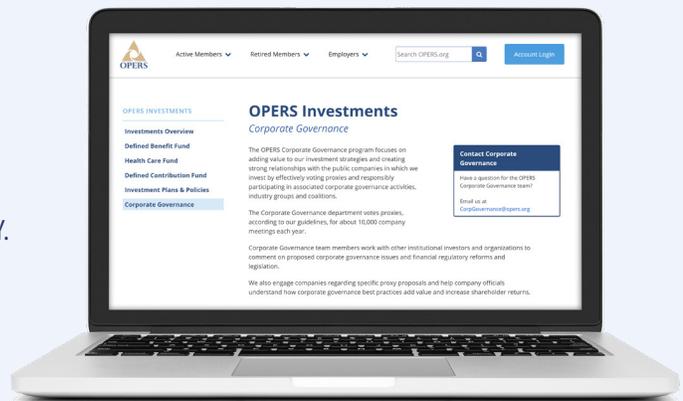
# TRANSPARENCY

Corporate misconduct has the attention of the governance community not only because of its performance risks, but also its reputational risk. Therefore, the idea of transparency has evolved. Companies must actively disclose transactions and deeds intentionally and unintentionally.

OPERS actively reviews how companies in which we invest conduct their businesses, including: accounting methods, earnings, insider trading, conflicts of interest, executive compensation, and the independence of their boards of directors. Shareholders deserve the facts about a corporation's financial health and structure. Transparency also has implications to the company's customers, suppliers, international trade and adherence to government regulations. In addition, OPERS seeks to comply with our own disclosure standards by adhering to strict disclosure policies.

THE OPERS CORPORATE GOVERNANCE POLICY AND PROXY VOTING GUIDELINES DOCUMENTS WERE COMBINED TO STREAMLINE INFORMATION. OPERS' VOTE DISCLOSURES ARE AVAILABLE ON OPERS.ORG AND HAVE BEEN OVERHAULED TO ENHANCE USABILITY.

*Search for CORPORATE GOVERNANCE to view the Policy and Guidelines or voting disclosures on opers.org.*



# TRANSPARENCY

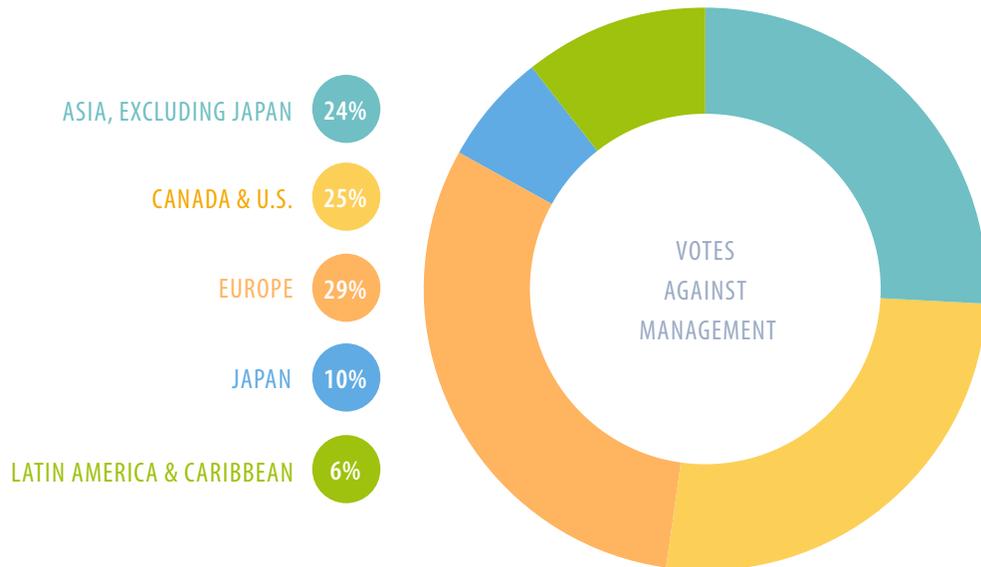
## Remuneration (Say on Pay)

About 12% of the overall proposals were related to votes on remuneration. OPERS voted against management 18% of the time on these proposals. The primary driver for votes against were due to company receiving a grade of D or lower for two consecutive years by the PAF.

Markets with the highest votes against were Europe and Asia (excluding Japan).

Primary reasons were:

- Poor compensation plan structure
- Incentive plans lacking adequate disclosure
- Incentive plans not linked to performance



## RENUMERATION

A broader term than salary, as it consists of bonuses, incentives, stock options, perks etc., in addition to the basic salary of the employee.

# STEWARDSHIP

OPERS has a fiduciary responsibility to ensure proxies are voted in the best interest of our current and future retirees. The Corporate Governance Policy and Proxy Voting Guidelines document is reviewed and approved by the OPERS Board of Trustees at least annually. Corporate governance best practices are embedded within the document and incorporated into the custom vote policy applied to our PAF's proxy voting platform. The custom policy and guidelines document was updated for the 2020 proxy season to provide consistency to the standard of independence used by the PAF and to remove reference to not-for-profit boards in the definition of "over-boarded" resulting from a lack of consistent disclosure amongst public issuers.

Stewardship is a cornerstone of good corporate governance. It ensures protection and care for the

company by creating and maintaining a successful organization. The way in which companies achieve sustainability is through establishing optimal relationships and implementing best practices through all levels of stakeholders. While the Business Roundtable equalized all stakeholders when redefining the purpose of a corporation, OPERS, as a long-term investor believes management should be accountable to shareholders. Boards and managers need to sustain long-term shareholder value, which can only be achieved through respect to all stakeholders.

Additionally, OPERS acts with other investors through the Board of Directors of the Thirty Percent Coalition and the Council of Institutional Investors, both reputable industry organizations aimed at advancing corporate governance best practices.



LOOKING AHEAD TO THE 2020 PROXY VOTING SEASON, THE OPERS CORPORATE GOVERNANCE PROGRAM WILL CONTINUE TO VOTE ALL PROXIES IN THE BEST INTEREST OF OUR MEMBERS AND BENEFICIARIES.

WE'LL CONTINUE TO ADVOCATE FOR PUBLIC COMPANIES HEADQUARTERED IN OHIO TO INCREASE GENDER PARITY ON THEIR BOARDS AND CONTINUE PURSUIT OF HCR 13 ENACTMENT.

LASTLY, WE WILL ADVOCATE FOR THE PROTECTION OF SHAREHOLDER RIGHTS WHILE ACKNOWLEDGING THE IMPORTANCE OF STAKEHOLDER RELATIONS TO SUSTAINABILITY.



# REFERENCES

1. <https://www.cii.org/content.asp?contentid=277>
2. <https://www.sec.gov/rules/proposed/proposedarchive/proposed2019.shtml>
3. <https://www.sec.gov/rules/proposed/proposedarchive/proposed2019.shtml>
4. <https://corpgov.law.harvard.edu/2019/09/17/2019-proxy-season-recap-and-2020-trends-to-watch/>
5. <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA133-HCR-13>
6. [http://images.info.issgovernance.com/Web/ISSGovernance/%7B18fbc0b3-28fa-4ce3-8081-c84824d4a0f8%7D\\_ISS-ESG-Corporate-Controversies-That-Defined-2019.pdf](http://images.info.issgovernance.com/Web/ISSGovernance/%7B18fbc0b3-28fa-4ce3-8081-c84824d4a0f8%7D_ISS-ESG-Corporate-Controversies-That-Defined-2019.pdf)

