



Investment Committee

Item number 4 – Open session

Subject: CalSTRS Stewardship Priorities Annual Update

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Attachment(s): Attachment 1 – 2024 Stewardship Highlights

PowerPoint presentation(s): PowerPoint 1 – Stewardship Priorities Annual Update

Item Purpose

This item presents an annual update to the Investment Committee of the three-year Stewardship Priorities (“Priorities”) adopted in January 2024. The Priorities guide the Stewardship team to deploy CalSTRS’ influence as a significant global investor and drive long-term value creation on behalf of California’s educators. This update includes both a review of major Stewardship activities in 2024 (Attachment 1) and a look-ahead to focus areas for CalSTRS in 2025.

Executive Summary

2024 Activities

Upon adoption of the Stewardship Priorities in 2020, staff committed to report regularly on the activities and tactics undertaken to implement the Priorities. **Attachment 1** details the achievements relating to the current set of Priorities over the first three quarters of 2024. Given the timing of this Investment Committee meeting, the fourth quarter’s activities are not included, but will be available on the [CalSTRS website](#) in early January. Staff will also continue to report quarterly through the web-based [Engagements in Action](#) and inform the board of significant and high-profile engagement activities, in response to emerging situations, as needed.

2025 Focus Areas

The breadth of stewardship activities and the tools and tactics investors use to influence positive change in the financial markets have expanded dramatically over the last several years. Staff has

identified Focus Areas within each Stewardship Priority based on our conviction that CalSTRS can achieve impact with the tools available to us as investors.

Detailed Engagement Plans identifying tactics to achieve the goals for each Focus Area are reviewed and revised annually. These Plans help staff measure outcomes and determine whether our work is leading to meaningful change to drive and protect shareholder value.

The Focus Areas, including key engagement activity, for each Stewardship Priority are described below.

Corporate and Market Accountability

- **Board Effectiveness:** Strong board leadership and oversight are key drivers of prudent risk management, and value creation. Engagement will focus on:
 - **Board Diversity:** CalSTRS will continue its direct company engagement, and collaboration with California institutional investors, to increase diverse director representation on boards and ensure clear guidance in company policies addressing board diversity and recruitment practices.
 - **Board Competency:** Through direct company engagement and collaborative efforts, CalSTRS will encourage companies to disclose board skills, experience, background, and diversity in a matrix and explain how those attributes enhance the long-term strategy of the company.
 - **Compensation:** One of the primary responsibilities for a board of directors is overseeing executive compensation and aligning it with a company’s long-term strategy. As part of direct company engagement with high emitters in the CalSTRS portfolio, and as part of collaborative efforts, staff will ask companies to link compensation to their net zero emissions commitments and enhanced climate and human capital-related disclosures.

- **Sustainability Disclosures:** Consistency and transparency around sustainability-related risks and opportunities impacting companies allow investors to make better decisions. Engagement will focus on:
 - **International Sustainability Standards Board (ISSB) Standards:** Through engagement efforts with regulators and policy makers, CalSTRS will advocate for the adoption of ISSB standards, which fully incorporate the Taskforce on Climate-related Financial Disclosures (TCFD) framework, as a global baseline for corporate sustainability disclosures. Staff will also encourage adoption through direct company engagements.
 - **Human Capital Management Disclosure:** CalSTRS will continue to advocate for universal, mandatory metrics on human capital with regulators and in cooperation with the [Human Capital Management Coalition \(HCMC\)](#). Staff will also encourage companies to disclose the foundational metrics through direct company engagement.

- **Shareholder Rights:** When necessary, CalSTRS will use our influence to protect shareholder rights and the long-term interests of the fund. Staff is monitoring the SEC’s new leadership and priorities and will take appropriate action if shareholder rights are threatened.

Net Zero Transition

- **Highest Emitters:** One of the three components of CalSTRS pledge to reach net zero portfolio emissions by 2050, or sooner, is to use our influence to accelerate the transition to manage risks in our portfolio. This Focus Area supports that component by engaging the highest carbon and methane emitters in the CalSTRS portfolio to set emissions reduction targets through three primary areas of activity:
 - **Climate Action 100+:** CalSTRS continues its work with this global investor collaborative effort to engage the highest carbon emitters. Investors are influencing companies to set short-term, medium-term, and long-term goals and targets to reduce greenhouse gas emissions and strengthen their business resilience. In addition, investors are asking for the implementation of tangible climate transition plans.
 - **‘Priority 45’:** The Priority 45 is a subset of companies that account for approximately 7% of CalSTRS global equity emissions and are not covered through Climate Action 100+. Staff are directly engaging these 45 companies to optimize their business strategies by: 1) Setting goals and targets to reduce emissions, 2) Obtaining audit assurance for emissions reporting, and 3) Linking compensation to emission reductions goals.
 - **Methane Mitigation:** Through direct company engagement with companies that emit methane (one of the most potent greenhouse gases), staff are focused on companies implementing cost-effective abatement opportunities that result in lower emissions and improving methane management and reporting in alignment with the [Oil & Gas Methane Partnership 2.0 \(OGMP 2.0\)](#).

Workforce and Communities

- **Workforce Culture and Engagement:** Diversity at the executive level and strong operational practices to promote diversity, equity and inclusion at all levels of the workforce create enhanced workplace culture and improved retention, which is correlated with financial outperformance. Engagement will focus on:
 - **Workforce Composition Data:** To understand how effectively a company is managing its workforce and workforce related risks, greater disclosure of basic workforce metrics is essential, but currently lacking. CalSTRS will continue to advocate for universal and mandatory metrics with regulators and in direct company engagements.
 - **Diversity, Equity and Inclusion (DE&I):** CalSTRS will continue to advocate for greater transparency on company DE&I practices which contributes to an inclusive culture and healthy workforce. CalSTRS continues to be an active participant with Invest Ahead (formerly the [Thirty Percent Coalition](#)) as it expands its diversity efforts

beyond the Board of Directors and encourages greater transparency of workforce diversity.

- **Just Transition in the Utility Sector:** Transitioning the world to a low-carbon economy will require major changes in the business models of the utility sector. CalSTRS will influence energy utility companies to provide enhanced disclosures on board-level oversight and support for workers and communities affected by the transition. Much of this engagement will be conducted in cooperation with Climate Action 100+.
- **Responsible Firearms:** CalSTRS continues to focus on reducing reputational and financial risks to the portfolio by encouraging companies involved in the civilian firearms industry to address firearms safety. Engagement will focus on:
 - **Retailers: Staff engages** with retailers to establish best practices in the sale of commercial firearms. The goal is to limit the risk of selling firearms to individuals who are excluded from purchasing firearms.
 - **Finance:** Credit card companies, banks, and online payment services can all be involved in the purchasing of firearms. These engagements seek to understand how companies track purchases to ensure their services are not used for illegal transactions that contribute to violence associated with the misuse of firearms.

New Engagements Launched in 2024

- **Impact of Artificial Intelligence (AI):** Staff has been researching how our portfolio companies are addressing the impacts and opportunities of AI. This work is incorporated in an engagement plan encompassing all three Focus Areas:
 - **Corporate and Market Accountability:** Staff is engaging with companies on how Boards are overseeing the implementation of AI in their operations. These topics include board education, data privacy and cybersecurity.
 - **Net Zero:** In April, Goldman Sachs projected AI data center energy demand would grow from 3% to nearly 8% of U.S. energy demand by 2030. Staff continues to research demand projections as well as engage with utilities, hyperscalers and technology companies to determine the impact of this new energy demand on the net zero transition of the broader economy.
 - **Workforce and Communities:** Engagement in this area touches on two topics. First, the impact to communities hosting AI data centers such as increased water demand and noise pollution. Second, the just transition impact of a company's workforce with regard to employee development or potential job losses.
- **Biodiversity:** Agriculture, forestry, and land use are major contributors to global carbon emissions and species loss and therefore also play a critical role in achieving a net zero emissions economy. CalSTRS has a history of engaging companies on supply chain and water risks to mitigate financial impacts to shareholders. CalSTRS recently joined [Nature Action 100](#) and is engaging four food and beverage companies along with other investors.

CalSTRS is also a member of the [FAIIR Initiative](#) and uses its data to support engagement work.

- **DEI Rollback:** CalSTRS believes that robust DEI programs and disclosures can be a positive indicator of inclusive workplace culture. This helps to attract and retain staff, drive productivity, and reduce reputational risk which all contribute to financial return objectives. Last summer, as some companies announced the rollback of their DEI programs and disclosures, staff quickly initiated contact with 30 high profile companies. This included companies making large scale changes in response to activist pressure as well as those companies we encouraged to maintain their robust programs and workforce disclosure.

Background

The market in which we operate as institutional investors has transformed dramatically over the past 20 years, not only in the tools we have at our disposal to influence change, but also in the number of material sustainability issues that global investors focus on. However, the fundamental purpose for why we engage has remained constant: **To mitigate risk in the CalSTRS portfolio, support long-term value creation, and promote practices that provide for a sustainable financial market.**

CalSTRS has a long history of proactive engagement with both 1) portfolio companies on sustainability issues that impact long-term company performance and 2) policy makers to ensure efficient markets and proper shareholder rights. CalSTRS thoughtful, analysis-based approach to engagement is well-respected in the global marketplace. Our reputation and our size make CalSTRS an attractive partner on a wide variety of initiatives. This creates significant opportunities, but also requires the team to be able to prioritize and allocate resources appropriately, both to align with CalSTRS goals, and to affect change where we have the greatest potential for success and the largest impact.

CalSTRS Stewardship Priorities

The Priorities adopted by the Investment Committee last year enable the Stewardship Team to plan and meet our goals in a systematic way. Staff uses our influence as a significant global investor to promote sustainable business practices and public policies. The categories below clarify why we prioritize specific engagement issues, particularly given the increasing interest in a wide range of sustainability matters and the role of investors in addressing them.

Corporate and Market Accountability: Basic governance rights and well-functioning, efficient markets, including effective and diverse boards, are vital components for CalSTRS to effectively mitigate risk in the portfolio. CalSTRS is committed to influencing regulators, standard-setters, and policy makers to promote sustainable markets, effective and diverse boards, and protect shareholder rights.

Net Zero Transition: Climate change presents a material and significant risk to society, the economy, and our portfolio. CalSTRS is committed to engaging the highest carbon emitting companies to reduce emissions in the global economy. This is aligned with CalSTRS pledge to achieve net zero portfolio emissions by 2050, or sooner.

Workforce and Communities: A company’s workforce is an important asset for any organization. Corporate boards should play an active role in properly overseeing the management of human capital and ensuring investors have adequate disclosures to oversee workforce-related risks and opportunities. CalSTRS is committed to influencing portfolio companies to ensure a healthy and engaged workforce and to be good stewards in the communities in which they operate.

As detailed in the [Sustainable Investment & Stewardship Strategies Program and Portfolio Policy](#), the Priorities were developed based on the following criteria:

1. Relevance to the long-term performance of the Portfolio.
2. Capacity to influence meaningful change based on the tools available to staff as shareholders.
3. Ability to deliver measurable outcomes.

Stewardship Tools and Tactics

CalSTRS utilizes a variety of tools and tactics to implement our Stewardship Priorities to achieve the stated objective, as described in the Focus Areas. The four main tactics are described in greater detail below:

- 1) Proxy Votes:** At CalSTRS we treat proxy votes as plan assets and vote all proxies internally, both domestic and international, in alignment with [CalSTRS Corporate Governance Principles](#). We use our proxy votes as a lever to hold directors accountable and require companies to respond to risks and opportunities. In addition to company management ballot items, we often support shareholder submitted proposals (“shareholder proposals”) that align with our goals and call on companies to better manage risk or improve public disclosure.
- 2) Direct Company Engagement:** Direct company engagement can be an effective tool for targeting companies that are ‘under-engaged’ by the wider marketplace or in instances where CalSTRS has a specific outcome we are trying to achieve that is directly tied to one of the Focus Areas. From January 1, through November 30, 2024, the team engaged 478 public companies with a collective market value of \$46.5 billion.
- 3) Collaborative Engagements:** Collaborative engagements allow CalSTRS to scale our influence as a global investor with other like-minded investors. Effective engagements that result in substantive commitments from companies is time intensive and utilizing collaborative engagements provides for an effective use of resources. Staff always adheres

to the Policies and Principles adopted by the Investment Committee when analyzing and voting proxies and engaging companies.¹

- 4) **Policy Advocacy:** Like proxy voting, policy advocacy is applicable to wide-ranging aspects of CalSTRS’ portfolio. We influence regulators and policy makers to support actions that provide for well-functioning and efficient markets that support long-term value creation.
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Strategic Plan linkage: Goal 1 of the Strategic Plan. Trusted stewards – Ensuring a well-governed, financially sound trust fund.

Board Policy linkage: This item is covered under the CalSTRS [Sustainable Investment & Stewardship Strategies Program and Portfolio Policy](#) (Teachers’ Retirement Board Policy Manual, Section 1000, C-1) and the [CalSTRS Corporate Governance Principles](#).

Optional reference material:

[Investment Beliefs](#) Linkage:

Investment Belief 7: Responsible corporate governance, including the management of environmental, social and governance (ESG) factors, can benefit long-term investors like CalSTRS.

Investment Belief 9: Investment risks associated with climate change and the related economic transition – physical and technology-driven – materially impact the value of CalSTRS’ investment portfolio.

¹ Participating investors are independent fiduciaries responsible for their own investment and voting decisions. Investors act independently in setting strategies, policies and practices and deciding whether and how to engage with focus companies based on their own understanding of their best interests.