
JANUARY 28, 2019

AGENDA ITEM 5
ACTION ITEM

CALIFORNIA SECURE CHOICE RETIREMENT SAVINGS INVESTMENT BOARD

Resolution 2019-01: Approval of Contract(s) for Environmental, Social, Governance Investment Option

Background

At the November 19, 2018 meeting, the Board approved the release of a request for proposals (RFP) for an Environmental, Social, and Governance (ESG) investment option. The Board had initially solicited ESG proposals as part of the program recordkeeper and investment manager RFP in May 2018. During that evaluation, the committee did not find a suitable ESG fund to recommend to the Board for inclusion in the investment lineup.

The Board received nineteen bids and the evaluation committee evaluated them with assistance from the Program's investment consultant, *Meketa*. The evaluation committee was composed of Executive Director Katie Selenski; Deputy Director Brian Gould; Board members Heather Hooper and Jacqueline Wong-Hernandez, representing Director of Finance Keely Martin Bosler; as well as Stanley Zeto, Deputy Director of the ScholarShare program.

Analysis and Evaluation Committee Recommendation

The committee received bids covering a wide range of structures and solutions. The committee reviewed the proposals and identified five finalists that were asked to respond to a series of additional clarifying questions in the finalist interview stage of the review. A summary table of information on the finalists is included as Attachment 1.

After reviewing the responses to the finalist interview questions, the committee updated the scoring and selected Newton Investment Management North America Limited (Newton) to recommend to the Board for inclusion in the investment lineup.

Structure and Cost

The recommended ESG investment option from Newton is a balanced fund, composed of 60% active ESG equity, run by Newton as a Sustainable Global Equity strategy, and 40% passive ESG bond strategy managed by Mellon Investments Corporation. The proposed fund will carry a cost of 15 basis points.

ESG Values Screening

The equity component uses an actively managed ESG methodology with screening that excludes companies in the tobacco business, as well as companies which negatively impact climate change, and also attempts to evaluate the tangible evidence of the non-financial benefits of

investments. In addition to specific exclusions, the approach utilizes additional levers that are available to equity investors, including proxy voting and direct engagement with companies.

While the firm does invest in ESG leaders, Newton prioritizes companies that are improving their ESG performance. By supporting improving companies, and encouraging them to do so via proxy voting or in some cases direct engagement with company leaders. Newton seeks to help drive positive ESG outcomes, while having the potential to achieve financial as well as non-financial benefits through this change.

The fixed income component of the proposed solution is passively managed, and ESG values are expressed through MSCI (formerly Morgan Stanley Capital International) ESG screening methodology. MSCI is an independent provider of ratings and indices that analyzes companies according to their exposure to industry-significant ESG risks and their ability to manage those risks relative to industry peers. The passive nature of this portion of the portfolio leverages the ratings from MSCI to deliver a high-quality portfolio at a streamlined cost to investors.

Specifically, the index eliminates:

- Investments in weapons (including civilian handguns), gambling, tobacco and alcohol
- Oil and gas companies, and the metals and mining sector
- The worst ESG-rated companies as defined by MSCI (below BBB; the lowest rating is CCC)

Company Background

Newton was formed in 1978 by Reed Stenhouse, a Scottish insurance broker. In 1986, the company was reorganized and renamed Newton Investment Management. In 1998, Newton completed an agreement for Mellon Financial Corporation to acquire a majority interest in the company, and in 2002, Mellon completed its acquisition of the Newton Group. Newton was Mellon's first substantial acquisition outside the U.S. In 2007, Newton's parent company, Mellon, merged with The Bank of New York to create The Bank of New York Mellon Corporation (BNY Mellon), which is Newton's parent company today. The merger had no impact on Newton's ownership structure. Newton Investment Management (North America) Limited (NIMNA Ltd) was founded in 1992 as Newton Capital Management Limited (changing its name in 2016).

Scope of Work

If approved by the Board, Newton would provide an ESG investment option to CalSavers participants. Newton would be required to work in concert with the program administrator and investment consultant to provide the Board all necessary data for evaluation of the fund on a quarterly basis, as outlined in the Request for Proposal. In addition, they would provide updates to the Board on the current ESG landscape and trends as requested, but no less than annually. Newton would also provide necessary investment descriptions in multiple languages consistent with other translated materials.

Contract Term and Cost

The agreement(s) would become effective upon approval by the Department of General Services. The term of the agreement(s) would be three (3) years with three (3) one-year extension options the Board may choose to exercise, for a possible total term not to exceed six (6) years. This

contract is considered a zero dollar contract for the Program because the firm(s) would be compensated by fees levied on participants.

Performance

Fund performance would be monitored against a benchmark to be selected once the ESG fund is in place. Performance and analysis metrics would be provided to the Board on a quarterly basis consistent with the Investment Policy Statement.

Staff recommendation

Staff recommend the Board approve resolution No. 2019-01 to execute a contract(s) with Newton Investment Management North America Limited for an ESG investment option.

Attachments

- Attachment #1: Finalist Summary Table
- Attachment #2: Resolution 2019-01 - Approval of Contract(s) for Environmental, Social, Governance Investment Option