January 30, 2022

To: Thomas J. Golonka, Chair
Vermont Pension Investment Commission

Kimberly G. Gleason, Vice Chair
Vermont Pension Investment Commission

From: Eric Henry, Chief Investment Officer
Vermont Pension Investment Commission

Re: Concerns over the provisions of S.251

I write to express staff's concerns over the provisions of Senate Bill 251 regarding divestment from fossil fuel reserves. We are very appreciative of the legislature's efforts to improve VPIC's governance with the passage of Act 75 of 2021 but are concerned that implementation of S.251 would not only present the negative financial impacts described below, but would also represent a significant distraction from the important ongoing governance studies and initiatives stemming from Act 75. While VPIC has not yet had a chance to formally take a position on S.251, I wanted to express our concerns and give you some insight into our ongoing initiatives on this extremely important issue.

Specifically, we are concerned that enactment of S.251 would reduce investment returns, increase expenses, increase unfunded liabilities and funding requirements, and lower our ability to affect positive change by the companies in which we invest.
We strongly believe that environmental, social, and governance factors present material investment risks and opportunities, much like the many other financial factors we consider in the development of VPIC's investment strategies, and we expect our investment managers to proactively address them.

One of our equity managers, for example, considers the impact of carbon on future earnings and valuations when making stock selections. In another case early last year, VPIC seeded a passive investment vehicle with that seeks to invest in global companies that are well-positioned to maximize returns and minimize risks associate with the transition to a global, low carbon economy. If this strategy performs as expected, VPIC will increase its commitment beyond the initial $200 million. Further, VPIC is considering opening this strategy up to other investors to generate economies of scale, lower costs, and increase its global impact. This is not a divestment strategy, rather, it is a proactive strategy to invest in companies the investment manager deems better relative to their peers given the transition to a low carbon economy. We believe the low carbon transition will affect all sectors and excluding a sector is too simplistic an approach to mitigate risk. Further, reducing the investable universe by excluding companies and/or sectors carries a high opportunity cost. Through this strategy, we will engage with companies on ESG issues, rather than abdicating our seat at the table to ensure positive progress on mitigation of ESG and other risk factors.

In addition to the investment strategies implemented by our investment managers, VPIC had developed and implemented a thoughtful and proactive set of proxy voting guidelines to assure that the votes tied to our equity investments are voted to maximize returns, but in a responsible way regarding environmental, social, and other governance factors. We take this responsibility so seriously that we recently drafted a policy on this topic and recommend VPIC and its new ESG Committee consider it in the coming weeks (Appendix B). Through our proxy votes, we engage with publicly traded companies on a wide array of company specific issues. A list of proxy engagements VPIC pursued in the last year alone is shown in Appendix A.

Recommendation:
We believe enactment of Senate Bill 251 will reduce investment returns, increase expenses, increase unfunded liabilities and funding requirements, and lower our ability to affect positive change by the companies in which we invest. Accordingly, we ask that you consider taking a position in opposition to S.251 and refer the draft Carbon Reduction and Mitigation Policy in Appendix A to the ESG Committee. We look forward to discussing these matters with VPIC and its ESG Committee in the coming weeks.

Appendix A
Recent VPIC Engagements

On November 8, 2021, staff engaged with CenterPoint Energy on the resolution filed on October 22, 2021 with the Company. As a reminder, VPIC is requesting the Company "adopt a policy that when the Company adjusts or modifies any generally accepted accounting principles ("GAAP") financial performance metric for determining senior executive compensation, the Compensation Committee's Compensation Discussion and Analysis shall include a specific explanation of the Compensation Committee's rationale for each adjustment and a reconciliation of the adjusted metric to GAAP." Staff is negotiating with the Company on actions that would be agreeable to VPIC for a withdrawal.

On November 9, 2021, staff participated on a Climate Action 100+ Exxon Mobil engagement call with many other institutional investors. A follow up Climate Action 100+ meeting on November 17, 2021, Staff participated on a North America Engagement Planning call.

On November 29, 2021, Staff engaged with Activision in a follow-up discussion regarding the report requested in the resolution filed during the 2021 proxy season. Previously VPIC had requested of the Company, and its Board approved, to "provide a public report that discloses whether a gender pay gap exists among its employees, and if so, details actions the Company will take in response."

On December 14, 2021, Staff participated in the Human Capital Management Committee meeting.

On January 13, 2022, Staff participated in the Carbon Asset Risk working group planning call.

Staff is currently evaluating a recommendation to the VPIC that they request in all limited partnership side letters a number of representations regarding the general partner's identification, analysis, mitigation, and disclosure of ESG risks associated with its portfolio company investments.

Staff met with a public utility company to discuss their disclosure of modifications to GAAP when calculating executive compensation on November 8, 2021. VPIC filed a resolution with the Company to request they "adopt a policy that when the Company adjusts or modifies any generally accepted accounting principles ("GAAP") financial performance metric for determining senior executive compensation, the Compensation Committee's Compensation Discussion and Analysis shall include a specific explanation of the Compensation Committee's rationale for each adjustment and a reconciliation of the adjusted metric to GAAP." Staff is negotiating with the Company on actions that would be agreeable to VPIC for a withdrawal. We hope to have more information for the Commission in the coming months.

On November 22, 2021, VPIC staff met with a computer software company to discuss VPIC's request for inclusion of Rooney Rule language in Board governance documents to create a process for improved Board diversity. The Company indicated that they will present VPIC's request to the Board at the next Board meeting. We anticipate a response from the Company in the coming weeks.

Staff met with a gaming company in a follow-up discussion regarding the report requested in the resolution withdrawn during the 2021 proxy season to evaluate pay equity. The Company had previously agreed to "provide a public report that discloses whether a gender pay gap exists among its employees, and if so, details action the Company will take in response." Staff will follow-up with the company again in the spring to receive an update on the Company's progress in anticipation of the report's release before the Company's Annual General Meeting in 2022. The Company confirmed at the meeting on November 29, 2021, that they are examining as part of the report pay gaps among non-gender conforming and racial categories of employees.

Staff met with another US oil and gas company as part of the Climate Action 100+ engagement team. VPIC requested additional disclosure at the meeting on December 7, 2021, around a "Just Transition" assessment that details with qualitative and quantitative metrics how the company anticipates their workforce will be impacted as part of meeting the company's long term decarbonization targets.

Staff led a meeting on December 10th with several institutional investors and an oil and gas company to discuss a transition of the Board Chair to an independent party rather than the CEO to improve governance. VPIC filed a resolution with the Company in October with this request and this meeting was in response to that filing.

VPIC signed onto a letter sent to Hilton Worldwide Holdings, Park Hotels & Resorts, and Xenia Hotels & Resorts requesting consideration of incorporating an ESG metric into executive pay that ties guest satisfaction to the compensation calculation. This letter was organized by Segal Marco as lead of the Say-on-Pay Working Group in which VPIC participates

VPIC distributed its 2021 Manager ESG Survey to all VPIC managers. Responses have been received and are currently being reviewed and analyzed by staff. The intent is to make these responses public on the VPIC website, as summarize managers 'progress in an executive brief for the Commission, and engage where further action is warranted.

With the assistance of Segal Marco and VPIC's custodians, Staff filed eight shareholder resolutions on behalf of VPIC, inline with the approved engagement plan. The ESG Committee will update the commission on these engagements as they progress. Of the eight resolutions filed with companies, three were requesting amendments to governance procedures to improve Board diversity, two were requesting better disclosure of GAAP financial adjustments, two were requesting a plan forward for an independent chairperson, and one was requesting a change in governance procedures to allow consideration of hourly employees on the Board. VPIC is the lead filer on 75% of the resolutions, while the remaining 25% VPIC is re-filing as a co-filer to continue the engagement effort with the companies and a coalition of institutional investors.

Last summer, the VPIC signed onto several company engagement letters, including:

- The Investor Agenda's "The 2021 Global Investor Statement to Governments on the Climate Crisis" letter to be presented at the 26th United Nations Climate Change Conference (COP26).
- A follow-up letter for the Russell 3000 Diversity Disclosure Initiative led by the Office of the Illinois Treasury. This initiative started in October 2020 and it engages companies on the topic of Board Diversity.
- A letter to Russell 1000 companies regarding diversity disclosure. The letter was organized by As You Sow, as follow-up and expansion of the mission to a 2019 letter to S&P 100 companies, "Investor Statement Calling for Corporate Workplace Equity Transparency".

VPIC, the Minnesota State Board of Investment, Ceres, and Segal Marco held an engagement meeting with the leadership of an energy company regarding its flaring target and 2020 sustainability report. This is a follow-up engagement after the resolution filed by VPIC in 2020 was withdrawn on condition that the Company's Board of Directors adopt a Bakken flaring reduction metric as part of its 2021 annual incentive plan for employees worldwide. This action ties executive compensation to the company's environment, health, safety, and climate change goals.

Staff participated in the completion of several ClimateAction 100+ biannual engagement surveys that were due on June 30, 2021. These surveys are used to document the Coalition's progress at each target company.

Staff participated on behalf of VPIC in the Ceres 'Shareholder Initiative on Climate and Sustainability (SICS) summer strategy meeting. During this meeting institutional investors discuss goals and strategy for the 2022 proxy season.

On behalf of VPIC, Treasurer Pearce presented Proposal #4: Independent Chair proxy resolution at the **Exxon Mobil Annual General Meeting** on May 26, 2021. The governance focused resolution received 22.1% support from shareholders. This initiative is part of a greater environmental engagement effort that VPIC participates in through Climate Action 100+ with the company.

In what has been described in news reports as "groundbreaking" at the May 25th ExxonMobil annual meeting, three dissident directors replaced three management nominees to the 12-member board. VPIC backed the activist investor, Engine No. 1, which contested the board elections, with votes in favor of two of the four dissident nominees. These Directors have experience in sustainable business consulting and diversification of operations at large corporations. This ensures Exxon's Board has the expertise needed to prepare the company for a transition to a low-carbon economy and maintain shareholder value for the long-term.

At the Exxon Mobil Annual General Meeting, VPIC voted in favor of the following:
- Proposal 6: Issue Audited Report on Financial Impacts of For IEA's Net Zero 2050 Scenario (48.9% shareholder support)
- Proposal 8: Report on Political Contributions (30.5% shareholder support)
- Proposal 9: Report on Lobbying Payments and Policy (55.6% shareholder support)
- Proposal 10: Report on Corporate Climate Lobbying (63.8% shareholder support)

Two received majority votes by shareholders. Proposals 6 and 8 received 48.9% and 30.5% approval votes, respectively.

At the **Chevron Annual General Meeting**, VPIC supported and 61% of shares voted in favor of a proposal asking the Company to cut Scope 3 emissions, which come from activities within the Company's value chain, aligned with the Paris Agreement.

At the **AbbVie Annual General Meeting** on May 7th VPIC co-filed with Rhode Island an Independent Chair resolution. 28.4% of shareholders supported the resolution.

At the **Amazon.com Annual General Meeting** on May 26th VPIC co-filed a resolution that proposed a worker representative serve on the board. It received 17.5% shareholder support.

At the **Duke Energy Annual General Meeting**, VPIC voted against two Directors, citing the Company's failure to align capital expenditures with its stated goal of achieving net-zero carbon emissions by 2050 which creates significant systemic climate risks for investors.

At the **Facebook Annual General Meeting**, VPIC co-filed a proposal seeking a policy that an independent chair lead the corporate board. The proposal received 17.1% support. However, if you exclude the shares held by CEO and Chairman Mark Zuckerberg the proposal received 51.9%.

VPIC's proposals to Activision Blizzard on pay parity reporting, Hess on a flaring reduction target, and Prosperity Bancshares on inclusive recruitment policies in support of board diversity were successful in implementing positive policy changes at these companies and each agreed to implement the respective proposals. All of VPIC's shareholder proposals, whether adopted or not, resulted in significant dialogue on the issues and will potentially foster resubmissions future years, which often results in increased support.

As a recent signatory of the U.N. Principles for Responsible Investment (PRI), VPIC submitted its first annual reporting and assessment survey for PRI signatories. VPIC will be scored on its responses and results will be publicly disclosed by both VPIC and PRI.

VPIC, the Minnesota State Board of Investment, Ceres, and Segal Marco scheduled an engagement meeting with an energy company regarding their flaring target and 2020 sustainability report for July 2021. This is a follow-up engagement after the resolution filed by VPIC in 2020 was withdrawn after their Board of Directors adopted a Bakken flaring reduction metric as part of their 2021 annual incentive plan for employees worldwide. This action ties executive compensation to the company's environment, health, safety, and climate change goals

Early last year, VPIC participated in a Climate Action 100+ engagement call with an oil and gas company regarding their 2020 Sustainability report and plans for progress toward a net zero emissions commitment.

VPIC, through its membership in ESG coalitions, including the Council of Institutional Investors, voiced its objections to the recent SEC rule that substantially reduced shareholder rights*.* CII sent a letter on April 27th to the Senate Banking, Housing & Urban Affairs Committee Chair Sherrod Brown and Ranking Member Pat Toomey in support of the use of the Congressional Review Act (CRA) to overturn 2020 amendments to the SEC's shareholder proposal rule, which, among other changes, raised the requirements for investors that wish to submit a shareholder proposal (see above) . The SEC's own Investor Advocate found the rulemaking process to be fundamentally flawed The SEC vote at the time was 3-2 While the CRA provides the ability to nullify federal agency rules adopted near the end of a prior administration with a joint resolution from Congress and the President, this was not taken up by the Senate. Investor groups have since filed a complaint on June 15th in U.S. District Court challenging the rule amendments.

Early last year, VPIC signed onto a letter to the Biden Administration calling for Methane and Flaring regulations at the Federal level. Methane emissions from the industry expel greenhouse gases that are 84 times more powerful than carbon dioxide in its first two decades after release. The letter, organized by CERES, requests that the government appropriately regulate this activity.

In line with the VPIC's request to engage on political expenditures, the VPIC signed onto a letter that will go to 81 companies requesting they disclosure whether and how they will update the Company's political spending policies to preclude any corporate political donations to legislators that support suppression of voting rights.

Early last year, VPIC signed onto two comment letters issued by the investor coalitions UN PRI and Ceres in response to the request by the SEC to support regulation of ESG disclosures by companies to create consistent, comparable, and reliable standards for information on climate change.

Early last year, VPIC agreed to a conditional withdrawal for its proposal with an entertainment company after its Board of Directors, in response to VPIC's engagement, agreed to conduct and publish an analysis of Companywide median pay by gender and non-binary populations in its 2022 environmental, social and governance (ESG) report. Staff will continue to meet with the Company to review progress on the report. The resolution has been formally removed from the proxy.

Treasurer Pearce and Chair Golonka joined Illinois Treasurer Frerichs and CalPERS ' Head of Corporate Governance for an interview with P&I for an article, "Proxy season action on climate change will be hard to avoid." It was published on March 8th to the P&I website and on the front page of the print issue.

VPIC agreed to a conditional withdrawal for its proposal with an oil and gas company after the Company's Board of Directors, in response to VPIC & co-filer Minnesota State Board of Investment (MSBI) engagement, adopted a Bakken flaring reduction metric as part of their 2021 annual incentive plan for employees worldwide. This action further ties executive compensation to the company's environment, health, safety, and climate change goals. The Company withdrew its No Action Letter with the SEC following the VPIC's conditional withdrawal.

A publicly traded bank accepted and confirmed VPIC's offer to a conditional withdrawal of the shareholder proposal upon confirmation that the Board has approved an amendment with specified language to their Corporate Governance Guidelines. This resolution was filed to improve the diversity of the Board. The resolution has been formally removed from the proxy.

In line with the proxy voting policy amendments it approved January 23, 2021, VPIC endorsed a joint proposal with other States to hold accountable Company's Board of Directors for oversight of systemic risks, such as climate change, that may have material impact on Company performance.

VPIC co-filed, alongside the lead filer Oxfam America, at an Internet & Direct Marketing Retail company on a resolution to include hourly employees as part of Board candidate search pools. The Company filed a No Action Letter with the SEC, which was overturned. The resolution will be included on the proxy ballot.

VPIC led an engagement discussion with co-filer Minnesota State Board of Investments (MSBI) at an oil and gas company on a resolution requesting a report on if and how the company will curtail its impact on climate change from routine flaring and venting. The Company filed a No Action Letter with the SEC, which the Treasurer's Office and MSBI will be filing a response for SEC consideration. Engagement with the Company continues.

VPIC participated in two engagement calls with Segal Marco and a financial company regarding the resolution on diversity filed by VPIC. The firm agreed to amend the Board's Corporate Governance Guidelines to meet the request of the proposal. A conditional withdrawal was agreed upon by the Treasurer on behalf of VPIC once the Company's Board approves the amendment.

The Investor Alliance for Human Rights, a coalition of which VPIC is a member, submitted comments on behalf of the alliance members to the European Parliament as part of their Sustainable Corporate Governance public consultation/survey. Note that this was an effort of the entire coalition, and not a direct effort of VPIC individually.

Appendix B:
Vermont Pension Investment Commission
Draft Carbon Reduction and Mitigation Policy

Section 523 of the Vermont Pension Investment Commission's enabling statute tasks VPIC with the responsibility "for the investment of the assets of the Vermont State Teachers' Retirement System, the Vermont State Employees' Retirement System, and the Vermont Municipal Employees' Retirement System." This section explicitly states VPIC "shall strive to maximize total return on investment, within acceptable levels of risk for public retirement systems, in accordance with he standards of care established by the prudent investor rule."

This policy sets forth VPIC's policy for responding to external or internal initiatives to divest of individual or groups of securities for purposes of achieving certain carbon reduction goals that do not appear to be primarily investment related. VPIC opposes any divestment effort that would either implicitly or explicitly attempt to direct or influence us to to engage in investment activities that violate and breach the Commissioners' fiduciary responsibility. Consistent with its fiduciary responsibility and the concepts of diversification and passive index investment, the Commission does not and will not systemically exclude or include any investments in companies, industries, countries or geographic areas, except in cases where it creates an economic risk to the fund or a potential for materials loss of revenue exists.

When pressured to divest, VPIC firmly believes that active and direct engagement is the best way to resolve issues. Face to face meetings with shareowners and senior management, or the Board of Directors, are essential to bringing about change in a corporation. No further action will be taken until all efforts at engagement have been fully exhausted. Efforts at engagement include, but are not limited to, shareholder resolutions, media campaigns, and other efforts at engagement.

VPIC's commitment to engagement with companies rather than divestment is based on several considerations:

- Divestment would eliminate our standing and rights as a shareowner and foreclose further engagement.
- Divestment would be likely to have negligible impact on the portfolio or the market.
- Divestment could result in increased costs and short-term losses.
- Divestment could compromise VPIC's investment strategies and negatively impact investment performance, further increasing unfunded liabilities and funding requirements.

If engagement fails to resolve the risk factor sufficiently, the CIO will bring the issue before the Commission for consideration of divestment from the applicable securities. The Commission will receive input from its investment staff, investment managers, investment consultants, and other experts in the particular field or issue. If the Commission determines that the making of an investment or continuing to hold a security is imprudent and inconsistent with its fiduciary duty, it will instruct investment staff to remove the security from the portfolio.

VPIC will exclude or eliminate investments that fall within the terms of a state or federal law regarding divestment, if it finds that divestment is consistent with its fiduciary duties and divestment is not determined to be imprudent.