



# Parnassus ESG Engagement Report

February 2019



**Dear Responsible Investor:**

**We are pleased to introduce Parnassus Investments' first ESG Engagement Report.**



**Environment**

Our approach to engagement is rooted in Parnassus's decades-long experience integrating deep fundamental and environmental, social and governance research to find high-quality companies to invest in on behalf of our clients. Today, as more and more people are choosing to use their capital to further ESG causes, we believe it is vitally important to continue sharing our perspective that ESG integration is beneficial for investors, companies and society.



**Social**

As the largest pure-play ESG mutual fund company in America, we own sizeable quantities of company stock, which opens up opportunities for us to make the voices of investors heard by some of the largest companies in the world. In our experience, building positive relationships with management—which is more likely to happen when they know we are significant stockholders—is an impactful way to effect corporate change. When companies see that we are offering constructive suggestions, they sometimes even approach us for advice. This report includes two components: engagement and proxy voting. We are currently studying options for adding a measurement section to future reports.



**Governance**

**Engagement**

Parnassus defines engagement as meaningful dialogue with company representatives for the purposes of better understanding the firm's operations and sharing our views about relevant ESG topics. The ultimate goal of our engagements is to encourage action on matters that are important to investors. We seek an exchange of ideas to deepen our understanding of how the company operates, what management is thinking and the level of effectiveness of the board's oversight. Our approach is collegial, constructive and focused on the best interests of stakeholders.



## Proxy Voting

Proxy voting is an impactful element of our engagement strategy, particularly because we hold large stakes in companies. We vote based on our guidelines, and we are transparent with our complete voting record (see [parnassus.com](http://parnassus.com)).

We welcome your comments on this inaugural report, and thank you for being a trusted investment partner.

Sincerely,

Benjamin E. Allen  
President and CEO

Jerome L. Dodson  
Founder and Chairman

# Engagement

We define engagement as meaningful dialogue with company representatives for the purposes of better understanding the company's operations and sharing our views about relevant environmental, social and governance topics. The ultimate goal of engagement is to encourage action on matters that are important to investors.



## Workplace Focus

---

### **Sysco:** Eliminating Slavery in the Supply Chain

When it came to our attention that food distributor Sysco Corporation was one of several large U.S. companies that were buying fish caught by people who were trafficked into slavery in Indonesia, we immediately initiated an engagement. Parnassus's goal was to convince Sysco to take decisive action to eliminate slavery in its supply chain, because we will not hold the stock of companies that profit from slavery.

The use of forced labor on fishing boats is widespread in Indonesia, with thousands of slaves from Myanmar (Burma), one of the poorest countries in the world, forced to fish on Thai-owned boats. The men who are enslaved have described working 20 to 22 hours each day and reported that they are beaten or whipped with toxic stingray tails if they try to rest. They are housed in cages, and many have died at sea. The fish caught using forced labor is difficult to track because it is mixed with catches from other boats and moved through multiple countries, processing plants and distributors.

When Parnassus initially engaged with Sysco, the company had various sourcing policies for key product lines in place, but had not yet introduced an enterprise-wide social auditing program to address labor and human rights risks throughout its supply chain. However, Sysco was willing to begin moving in that direction. Parnassus connected Sysco with experts on social supply chain management issues and, at our urging, the company decided to implement a comprehensive supplier code of conduct for their branded products that includes requirements related to human rights, child labor, freedom of association, forced labor, discrimination, wages and benefits.

Parnassus has checked in with Sysco about this issue every six months for the past three years. Over that time, the company has demonstrated tremendous improvement in managing its social supply chain. The company's achievements include:

- Eliminating 38% of its seafood suppliers because they did not meet Sysco's supplier code of conduct standards

- Hiring Southeast Asian employees with local language expertise to monitor suppliers on the ground
- Partnering with the World Wildlife Foundation, which maintains a database of acceptable and controversial suppliers, to audit its branded seafood business

---

Sysco has demonstrated tremendous improvement in managing its social supply chain.

Most recently, when Parnassus suggested that Sysco encourage customers in their non-branded business to transition their supply chain-related business to Sysco because of the company's careful supply chain monitoring practices, the company responded very positively.





## The Opioid Crisis: Distributors Miss the Mark; CVS Steps Up

The opioid crisis is a complex national public health emergency, with addiction affecting more than two million Americans and overdose deaths reaching more than 70,000 in 2017 alone. Systematic failures along the entire drug supply chain—including manufacturers, distributors, pharmacies, prescribers, payors and regulators—have exacerbated the spreading opioid epidemic. Drug distributors in particular have unique visibility into drug distribution patterns. In addition, they have a legal obligation to monitor and report suspected diversion of controlled substances from legitimate medical to illicit non-medical uses, as well as to prevent suspicious orders from being shipped.

We at Parnassus share the widely held belief that addressing this epidemic is an urgent priority, which led us to initiate a series of dialogues with senior management at McKesson Corporation and Cardinal Health, Inc. These two companies are among the largest drug distributors in the United States. We aimed to discuss allegations that these firms had neglected their legal obligation to monitor controlled substance distribution and prevent suspicious orders from being shipped. Following these discussions, we concluded that the responses of both companies were insufficient and too slow, given the growing scope and urgency of the problem—and we sold both holdings.

---

CVS is addressing opioid abuse, both behind the pharmacy counter and with the patient community.



Our discussions with retail drug distributor CVS Health yielded a different result. The head of corporate social responsibility at CVS revealed that this company is addressing opioid abuse, both behind the pharmacy counter and with the patient community. CVS is monitoring and enforcing limits on prescriptions, training pharmacists and offering safe drug-disposal receptacles to the public. Based on the positive steps CVS is now taking to help stem the opioid epidemic, Parnassus decided not to divest our CVS holdings as part of this engagement.



## Gilead: New Stewardship

Gilead Sciences, Inc., produces novel therapies for diseases with large patient populations, such as hepatitis C, HIV/AIDS and cardiovascular disease, by investing heavily in scientific research. With the company's acquisition of Kite Pharma, Inc., the firm has increasingly focused on cancer treatments. Gilead is undergoing significant leadership changes; the company's Chief Medical Officer left in August, and both the CEO and Chairman also announced their intentions to resign.

In the midst of the executive search, the Gilead Lead Independent Director initiated an engagement with Parnassus, which provided us with an opportunity to share our views on effective governance, as well as specific leadership skill sets that may best support the long-term success of Gilead. The Board selected a new CEO in December.



### **MDU: Cleaner Power Generation**

MDU Resources Group, Inc., is a diversified natural gas utility, construction materials and services provider, and oil and gas producer. With our encouragement, MDU divested from its pipeline and refinery businesses—which were poor performers from both a fundamental and an ESG perspective. The company has also expanded its wind capacity over the years we have held the stock. MDU took the initiative in states that do not have stringent renewable mandates, reducing exposure to coal generation and increasing the renewable component of its utility segment to 22% through the development of Thunder Spirit Wind farm in 2015. More recently, MDU has expanded this wind project, boosting the company’s renewable portfolio to 27%. We are encouraging MDU to continue increasing its sustainable energy use.

#### **A Note on Wells Fargo Engagement and Divestment**

Parnassus conducted an extensive engagement with Wells Fargo in 2016 and 2017 before divesting during the first quarter of 2018. You can read more about this engagement on our website.



### **Clorox: Life Cycle Design**

The Clorox Company is a good ESG performer that is very open to our suggestions about ways to improve its sustainability practices. Parnassus has visited Clorox’s R&D facilities multiple times, and we are currently monitoring the company’s product life cycle design. Many of its products are single use, such as plastic trash bags and wet wipes. Clorox is working to make its products more sustainable, and we have asked the company to prioritize life cycle design in its next five-year plan. Parnassus has also requested that Clorox add a sustainability expert to its board who would oversee the company’s sustainability strategy, goals and progress. Management has agreed to engage with us on these issues.

---

Clorox is working to make its products more sustainable, and we have asked the company to prioritize life cycle design in its next five-year plan.



# Proxy Voting

## Why we vote

Proxy voting has the power to influence corporate behavior, by, for example, mandating progress on environmental goals or remediating controversies facing the company. Knowing which resolutions other shareholders are raising at annual company meetings may also help investors pinpoint emerging issues before they become major problems.

## How we vote

Parnassus's proxy votes are guided by the firm's ESG values and research, as illustrated on the following page. Further details on our proxy voting policies are contained in the Parnassus Funds Statement of Additional Information. You can view our full voting record on [www.parnassus.com](http://www.parnassus.com).

## Environment

**For** increased disclosure, elimination of toxins in products and reducing negative operational impacts

## Philanthropy

**For** increased disclosure and more philanthropy

## Diversity

**For** increased disclosure, nondiscrimination policies and improvements in diverse representation, both within the workforce and at the executive level

## Corporate Governance

**For** independent boards, separation of CEO and Chairman roles and engaged board members

## Election of Directors

**For** increasing diverse perspectives at the board level, including those of qualified women and minorities

## Employees and Supply Chain

**For** increased disclosure, codes of conduct, fair wages, safe working conditions and the right to organize

## Business Practices

**For** promotion of ethical business practices

## Community Relations

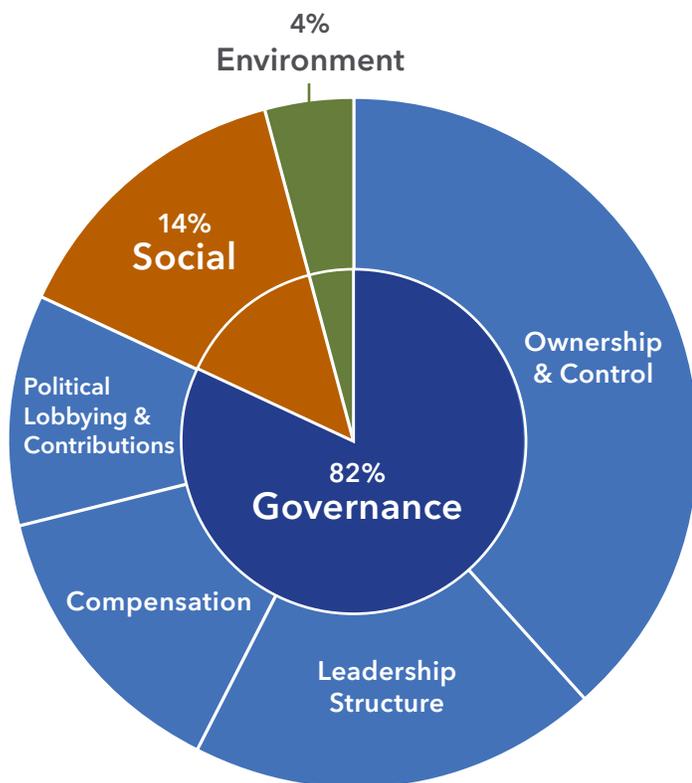
**For** good corporate citizenship and community sensitivity



## Proxy Voting Highlights

Parnassus regularly votes proxies to further fundamental and ESG goals. Most of the votes pertain to management resolutions addressing routine matters, such as non-controversial election of board members. However, the non-routine matters, such as ESG resolutions brought by shareholders, require careful research and consideration. On the following page, we offer insight into some of the objectives we are pursuing as responsible investors with our votes.

### Proxies voted between January and June 2018



**82%** Governance-related issues represented 82% of the shareholder resolutions

#### Governance vote breakdown

- 38%** Ownership & Control
- 19%** Leadership Structure
- 14%** Compensation
- 11%** Political Lobbying & Contributions

## Executive Compensation

Parnassus voted against ratifying executive compensation in cases where we identified a misalignment between named executive officer pay and company performance. Examples of companies include Allergan, Disney, Hologic and Qualcomm.

## Election of Directors

We voted against directors for a variety of reasons, generally related to poor company performance or weak corporate governance structures. For example, at Alliance Data Systems, we voted against five directors due to poor company performance, long tenures and waivers of the company's requirement for routine retirement of board members who have reached mandatory retirement age. In the case of Belmond, we withheld votes for all directors for maintaining an unusual controlling structure that prevents shareholders from holding board members accountable. At T-Mobile, we voted against three directors who are non-independent, yet serve on key board committees.

## Diversity Disclosure

We voted in favor of resolutions requesting annual disclosure on workforce diversity at Applied Materials, Charles Schwab, First Republic Bank and Starbucks.

## Environmental and Social Issues

We voted in favor of resolutions addressing the risk management of environmental and social issues. At Alphabet, Bristol-Myers Squibb, Expeditors International and UPS, we supported resolutions requesting that the company incorporate sustainability metrics into executive compensation plans. We also voted for resolutions at Apple and Mondelez asking the board to establish a committee to address environmental and social issues. We voted in favor of a resolution asking Motorola Solutions to add expertise on environmental and social issues to the criteria considered for director nominees.

**77%** Of the **shareholder resolutions focused on ESG topics**, Parnassus Investments disagreed with management recommendations 77% of the time.

**13%** Parnassus Investments voted against management's recommendation for ratifying executive compensation 13% of the time.

A shareholder resolution is a proposal put forth by shareholders for a company's management or board requesting a specific action.

Following is an outline of companies mentioned in the report. Each percentage listed represents the percentage of total net assets (TNA) as of 12/31/18. Sysco Corp. represented 2.8% of the Parnassus Core Equity Fund and 2.4% of the Parnassus Mid Cap Fund. CVS Health Corp. represented 3.9% of the Parnassus Fund, 4.6% of the Parnassus Core Equity Fund, 3.8% of the Parnassus Endeavor Fund and 1.8% of the Parnassus Fixed Income Fund. The Clorox Company represented 3.8% of the Parnassus Core Equity Fund, 3.2% of the Parnassus Mid Cap Fund and 1.6% of the Parnassus Fixed Income Fund. MDU Resources Group Inc., represented 1.0% of the Parnassus Core Equity Fund and 2.0% of the Parnassus Mid Cap Fund. Allergan PLC represented 2.3% of the Parnassus Fund and 2.0% of the Parnassus Endeavor Fund. The Walt Disney Company represented 4.9% of the Parnassus Core Equity Fund and 1.8% of the Parnassus Fixed Income Fund. Hologic, Inc., represented 4.0% of the Parnassus Fund, 2.5% of the Parnassus Core Equity Fund, 2.0% of the Parnassus Endeavor Fund, 4.4% of the Parnassus Mid Cap Fund and 1.7% of the Parnassus Fixed Income Fund. QUALCOMM, Inc., represented 3.2% of the Parnassus Endeavor Fund. Alliance Data Systems Corp. represented 4.5% of the Parnassus Fund and 4.1% of the Parnassus Endeavor Fund. Belmond Ltd. represented 2.9% of the Parnassus Fund. T-Mobile US, Inc., represented 2.8% of the Parnassus Fund. Applied Materials, Inc., represented 5.9% of the Parnassus Endeavor Fund. Charles Schwab Corp. represented 2.5% of the Parnassus Fund, 3.1% of the Parnassus Core Equity Fund, 3.5% of the Parnassus Endeavor Fund and 1.8% of the Parnassus Fixed Income Fund. First Republic Bank represented 2.6% of the Parnassus Core Equity Fund and 2.7% of the Parnassus Mid Cap Fund. Starbucks Corp. represented 3.7% of the Parnassus Fund, 3.6% of the Parnassus Core Equity Fund, 5.2% of the Parnassus Endeavor Fund and 2.1% of the Parnassus Fixed Income Fund. Alphabet Inc., represented 3.7% of the Parnassus Fund, Class A, 2.9% of the Parnassus Core Equity Fund, Classes A and C, 3.8% of the Parnassus Endeavor Fund, Class A and 1.7% of the Parnassus Fixed Income Fund, Class A. Bristol-Myers Squibb Co. represented 2.7% of the Parnassus Endeavor Fund and 1.6% of the Parnassus Fixed Income Fund. Expeditors Intl., Inc., represented 0.9% of the Parnassus Mid Cap Fund. Apple Inc., represented 2.0% of the Parnassus Core Equity Fund, 1.2% of the Parnassus Endeavor Fund and 2.5% of the Parnassus Fixed Income Fund. Mondelez represented 4.0% of the Parnassus Fund and 1.4% of the Parnassus Fixed Income Fund. Motorola Solutions represented 3.9% of the Parnassus Fund, 2.1% of the Parnassus Core Equity Fund and 4.3% of the Parnassus Mid Cap Fund.

Parnassus Funds fully divested all McKesson shares owned by the Parnassus Core Equity Fund, the Parnassus Endeavor Fund, the Parnassus Mid Cap Fund and the Parnassus Fund by 12/13/17 and all Cardinal Health shares owned by the Parnassus Mid Cap Fund by 12/21/17. Parnassus Funds also fully divested all Wells Fargo shares owned by the Parnassus Fund, the Parnassus Core Equity Fund and the Parnassus Endeavor Fund by 3/8/18.

Fund holdings are not intended to represent future portfolio composition. Fund holdings are subject to change and should not be considered a recommendation to buy or sell any securities. The views expressed are subject to change at any time in response to changing circumstances in the markets and are not intended to predict or guarantee the future performance of any individual security, market sector or the markets generally, or the Parnassus Funds. Mutual fund investing involves risk and loss of principal is possible.

The Parnassus Funds are underwritten and distributed by Parnassus Funds Distributor, a subsidiary of Parnassus Investments and a FINRA member.

**Before investing, an investor should carefully consider the investment objectives, risks, charges and expenses of the fund and should carefully read the prospectus or summary prospectus, which contains this information. A prospectus or summary prospectus can be obtained on the website, [www.parnassus.com](http://www.parnassus.com), or by calling (800) 999-3505.**

