Integrating ESG Options into Higher Ed Retirement Plans

July 30, 2019

The webinar will begin shortly

www.intentionalendowments.org
Speakers

Chris Walker, Purposeful Strategies
Tony Calandro, Purposeful Strategies
Sam Stephens, ESG Research Analyst, Mirova
Sarah Bratton, Investment Director - Sustainability, Schroders

Moderator: Hannah Bowen, Network Manager, Intentional Endowments Network
The Intentional Endowments Network

A Peer-Learning Network for Higher Education, Philanthropic & Non-Profit Endowments
Aligning Investment Portfolios with Institutional Mission, Values, & Sustainability Goals

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Integrating ESG into Retirement Plans

The responsible retirement plan opportunity for IEN Members

Purposeful Strategies
Chris Walker and Tony Calandro
July 30, 2019
Why should IEN members undertake this initiative:

• IEN Members have sought to make Environmental, Social and Governance (ESG) commitments for their endowments and have begun to align key operational and business priorities with specific Sustainable Development Goals, particularly to address climate change.

• However, a “blind spot” often exists between an organization’s values and the retirement investments it deploys on behalf of a vital constituency, its own employees
  • The overwhelming majority of Institutions as well as companies have not yet aligned their retirement plans with their sustainability commitments
  • University employees are likely to want to have opportunities to invest in accordance with their values

• We believe this is a sizable sustainability gap for IEN members, as well as a market opportunity for the asset management and investment advisory community.

Size of the opportunity and potential for impact

• The 4,000 colleges + universities in North America represent in excess of $1 Trillion pool of retirement assets
  • 150+ IEN members
  • Potential for International Institutions to participate
Model: WBCSD’s “Aligning Retirement Assets” (ARA)  
Launched in June 2018

Help companies better align retirement assets, including defined benefit and defined contribution plans, with their overall sustainability goals by integrating Environmental, Social and Governance (ESG) considerations
IEN: Integrating ESG into Retirement Plans

Help IEN members to better align retirement assets, including defined benefit and defined contribution plans, with their overall sustainability goals by integrating Environmental, Social and Governance (ESG) considerations.

Core Collaboration Partners

IEN Members requested to sign up

Seeking 10-20 Institutions to form the core of the working group

Associate Collaboration Partner

Responsible Retirement Plans

* Healthy Pension System

* Positive ESG Impact
Top Benefits

Institutions as retirement plan sponsors could meet a growing demand from their employees for responsible investments and increase plan engagement, participation and savings rates. This aligns well with the University and student body ethos.

75% generally interested in sustainable investment
69% want to see an option of responsible retirement plan
60% ready to shift own money

Source: WBCSD meta-study of 9 market surveys on 5000+ individual investors’ attitudes about sustainable investment in retirement plans
Top Benefits

In 2018 the U.S. Government Accountability Office (GAO) conducted a detailed study of ESG investment trends in retirement plans, and conducted its own meta-study of ESG investment research articles. In looking at studies conducted between 2012 and 2017, the GAO found that 88% of scenarios evaluated in those studies found a neutral or positive relationship between the consideration of ESG data and financial returns when compared to otherwise comparable investments.

Thoughtfully considering ESG factors in investment processes can result in improved risk-adjusted returns for participants and beneficiaries over the longer term.
Finding the **Change Agents** in Retirement Plan Governance

The project aims to arm Champions/sustainability professionals to be catalysts to assist those with direct oversight of their plans to be better positioned to integrate ESG.

Ultimately, we want to help engage the plan administrators and decision makers to assist them to incorporate ESG into their plans.
Not Violating **Fiduciary Responsibility**

Considerations of fiduciary duty lie at the heart of how retirement plans are governed, and must be considered in any course of action a retirement plan might take. It is useful to consider how sustainable retirement approaches might impact fiduciary duty.

**Fiduciary duty in the United States**

In the United States, private sector retirement plans are governed by the Employee Retirement Income Security Act (ERISA) of 1974. Under ERISA, fiduciaries’ responsibilities span multiple duties.

- **Duty of Loyalty**
  - ESG integration practices generally seek to consider material risk and return considerations rather than purely focus on policy or ethical matters, therefore can be considered to be operating the plan “solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses.”

- **Duty of Prudence**
  - ESG integration extends the range of material data points taken into account in investment decision making processes, fiduciaries would be acting “prudently” in ensuring that ESG risks are taken into account in the retirement plan they govern.

- **Duty to Diversify**
  - Active investment managers may choose to invest towards “best in class” companies in terms of ESG performance, and those companies may not be included in more traditional investment strategies, thus offering some potential diversification benefits in line with fiduciary duty.
How can we help more entities join the journey?

Key Takeaways from ARA Company Interviews

The sustainability professionals often feel they are not equipped with the right amount of understanding of retirement plans and would like to learn more about the following key retirement topics:

- Evidence that ESG considerations are not violating fiduciary responsibility
- The portfolio of methods that define 'sustainable'
- Fund selection, governance, regulation
- Costs of sustainability investing
- Overcoming fear of “concessions”

Source: Mercer; WBCSD
Toolkits to Support the Journey

Similar to the approached we used for the ARA: We will work with Mercer and others to develop “toolkits” to assist in deciding how to approach the opportunity in 403b plans.

The ARA toolkits consisted of:

1. What is a Sustainable Retirement plan and Why would we consider doing so
   - The purpose of this toolkit is to answer the question “what is a responsible retirement plan?” starting with the basics of how retirement plans are governed and operated.

2. How to develop a sustainable retirement plan
   - A more “tactical” approach to responsible retirement plans, with a strong emphasis on helping interested individuals start to have conversations with the right people internally, as well as a series of typical objections that individuals might encounter and ways to respond effectively to them. This toolkit features case studies highlighting what others have achieved.
For ARA first-mover companies

ARA Member companies added ESG-themed Defined Contribution options

Defined Benefit plans of member companies have joined PRI to showcase ESG integration

Source: WBCSD, PRI
A Few Guidelines for Champions to consider

1. Speak with the RETIREMENT PLAN COUNSEL for an opinion on ESG integration and fiduciary responsibilities from their perspective.

2. Link the company’s PRIORITY ESG FACTORS/THEMES with retirement assets investments to support communication and engagement with stakeholders.

3. Define KEY CRITERIA to assess ESG and potentially measure the impact.

4. Different approaches for DEFINED CONTRIBUTION and DEFINED BENEFIT Pension Schemes through dialogues with employees and trustees respectively.

5. SHARING best practices with other Institutions.
Asset Manager Perspective: Schroders
Sustainable investing is not simple

Confusion over definitions
Range of different investment products under the broad umbrella

Performance concerns
Many products in this space have not met performance expectations

Lack of transparency
Leading to confusion over what the intended approach is

Questions over members’ views
What do they want?
Majority find sustainable investment a challenge

Schroders Institutional Investor Study 2018, conducted between 1–30 June 2018. This study was commissioned by Schroders and undertaken by an independent research agency, CoreData Research, to study institutional investors across North America, Europe, Latin America and Asia to analyse their attitudes towards sustainable investments, investment objectives and risk. Respondents represent a variety of institutions, including pension funds, foundations, endowments and sovereign wealth funds. The 650 institutional respondents were sourced from 15 different countries and were split as follows: 175 in North America, 250 in Europe, 175 in Asia and 50 in Latin America.
Sustainability growing in importance
Over 2/3 believe it will become more important

How do you expect the role of sustainable investing to change in the next five years?

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Barriers to investing more sustainably

Which, if any, of the following specific factors do you consider a challenge of investing in sustainable investments?

- Performance concerns: 53%
- Lack of transparency and reported data: 50%
- Difficulty measuring and managing risk: 33%
- Cost: 28%
- Investment committee is not comfortable making sustainable investments: 17%
- I do not believe in sustainable investments: 16%
- I do not consider there to be any challenges to investing in sustainable...: 12%
- Other: 3%

How ESG matters

Three cases ESG can enhance investment performance

1. **Pick up Sustainable Growth**
   - High quality companies tend to have less ESG issues and Management can execute business strategy to achieve sustainable growth

2. **Avoid high risk companies**
   - Corporate scandal and fraud can destruct corporate value severely and therefore we cannot ignore ESG issues of invested companies

3. **Turnaround by engagement**
   - Engagement can lead to resolution or improvement of ESG issues and that leads to turnaround of companies business as well as stock price

For illustration purpose only
Source: Schroders.
Multi-faceted area of investment

Leading Asset Owners are taking action in a variety of ways

- Clear ESG policy consistent with their beliefs, objectives and circumstances
- Multi-faceted approach
- Signed up to local stewardship code, governance principles and/or UN Principles for Responsible Investment (PRI)
- Active participant in industry organisations and initiatives
- Transparency and reporting on stewardship activities

Source: Schroders.
Asset Manager Perspective: Mirova / Natixis
Over the past several years there has been growing interest in investments that align with investor’s values:

- 75% of investors would like their investments to reflect their personal values
- 84% believe it is important to be invested in companies that are ethically run
- 68% believe it is important to make a positive social impact through their investments
- 74% would like to see more socially responsible investments in their retirement plan

Source: Natixis Investment Managers, Global Survey of Individual Investors conducted by CoreData Research, February-March 2017. Survey included 8,300 investors from 26 countries, of whom 750 were in the US.

*Source: Defined Contribution Plan Participants Survey conducted by CoreData Research, August 2016. Survey included 951 US workers, 651 being plan participants and 300 being non-participants.
The Millennial movement

75% of the workforce will be Millennials by the year 2025

71% of Millennials would likely increase their retirement plan contributions if they knew their investments were doing social good*

*Source: Defined Contribution Plan Participants Survey conducted by CoreData Research, August 2016. Survey included 951 US workers, 651 being plan participants and 300 being non-participants.
Investor motivations

**POSITIVE/NEGATIVE SCREENING**
Screening securities on ESG or values-based criteria

“I want my investments to be consistent with my world view.”

**ESG INTEGRATION**
Incorporates ESG factors into fundamental analysis to pursue alpha and mitigate risk

“The world is changing; I believe ESG can help me identify more resilient investments.”

**IMPACT/THEMATIC**
Investment selection guided by ESG themes and positive impact

“I want my investments to contribute to a better world in addition to identifying more resilient investments.”
RESPONSIBLE INVESTING

Using ESG to identify more sustainable businesses

Assess management quality and limit surprises and event risks
- Accidents
- Shutdowns
- Fraud
- Inefficient use of resources
- Litigation

Understand exposure to long-term systematic risk factors
- Weather patterns
- Water scarcity
- Data security
- Skill shortages
- Changes in commodity prices

Align with values
Invest to create positive impact
Enhance long-term risk/return
**RESPONSIBLE INVESTING**

### Department of Labor guidance as a reference

**ERISA requires fiduciaries to:**
- act with the care, skill, prudence, and diligence a prudent person would use
- act “solely” in interest of a plan’s beneficiaries and for “exclusive purpose” of providing benefits and paying reasonable administrative expenses

**Collateral Benefits (CBs):**
- economic benefits created apart from investment return to the plan (CBs created by “Economically Targeted Investments” or “ETIs”)
- DOL’s longstanding position: fiduciaries may not sacrifice investment returns or assume greater investment risks as a means of promoting collateral social policy goals
- Interpretative Bulletins issued on ETIs:

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<td>“Everything being equal test” risk/return must be at least in line with alternative available investments Encouraged consideration of ESG</td>
<td>More rigorous view of “Everything being equal test” Discouraged consideration of ESG</td>
<td>Rescinded 2008 guidance ESG “issues may have a direct relationship to the economic value of the plan’s investment” Encouraged consideration of ESG</td>
<td>Must “not too readily treat ESG factors as economically relevant” Doesn’t necessarily discourage consideration of ESG</td>
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Source: US Department of Labor
Disclosure

This material is provided for informational purposes only and should not be construed as investment advice. The views and opinions expressed may change based on market and other conditions. There can be no assurance that developments will transpire as forecasted. Actual results may vary.

Investing involves risk, including the risk of loss. Investment risk exists with equity, fixed-income, and alternative investments. There is no assurance that any investment will meet its performance objectives or that losses will be avoided. Sustainable investing focuses on investments in companies that relate to certain sustainable development themes and demonstrate adherence to environmental, social and governance (ESG) practices, therefore the universe of investments may be reduced. This could have a negative impact on performance depending on whether such investments are in or out of favor.

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Next Steps
Priorities for this initiative over next 18 months
IEN working group will develop industry-leading contents

Reports & Thought Leadership

**Toolkit #1 – Why**

**Toolkit #2 – How to feature** A more “tactical” approach to responsible retirement plans – featuring case studies and resources for practitioners start to have conversations with the right people internally.

Articles and stories published on thought leadership Potential to explore issues related to implementation, using Default options, attracting employee participation etc.

Webinars

Periodic Webinars on Important developments/regulatory changes (US or Internationally) or case examples of ESG Integration by peers

Strengthen and grow the working group – extend reach beyond IEN members to the 3-4,000 non-IEN member universities (US and Internationally)
Project Rollout

- July 2019 - Webinar – Soft launch to invite IEN members to participate

- August 2019—Internal survey to identify common barriers

- September 2019 – Potential event during UNGA/Climate Week in NYC

- Fall 2019 – Interviews of project participants for toolkits and Release of Survey results

- January 2020 – Roll out of first Toolkit and Communications to support visibility

- February/March 2020  – Presentation of Toolkit at Greenbiz/Higher Education Summit

- September 2020 – Roll out of second toolkit and Communications to support

- December 2020  - Review of project; develop 2021 scalable engagement strategy
Questions?

Please use the Q&A window on your Zoom control panel to ask questions.
Thank you!
For more information, visit us at www.intentionalendowments.org