

2007 Report

Responsible Investment in Focus:

How leading public pension funds are meeting the challenge

A report jointly prepared by:

**The United Nations Environment Programme Finance Initiative (UNEP FI)
Asset Management Working Group (AMWG)**

and

**The United Kingdom Social Investment Forum (UKSIF)
Sustainable Pensions Project (SPP)**

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UNEP Finance Initiative
Innovative financing for sustainability

The United Kingdom Social Investment Forum (UKSIF)
Sustainable Pensions Project (SPP)



**UK
Social
Investment
Forum**

UKSIF is grateful for financial support from Esmée Fairbairn Foundation for the Sustainable Pensions Project.



“ABP firmly believes that integrating environmental, social and governance (ESG) factors into its investment processes will help to improve risk-adjusted financial return. Engaging with companies to improve their management of ESG risks is an integral part of this. We have expanded our resources in this area recently and plan to do so further in the future.”

Rob Lake

Senior Portfolio Manager, Environmental, Social and Governance Issues, ABP Investments

“As a large investor with significant assets we believe responsible investment is aligned with our duty to beneficiaries, it is our understanding that an enlightened attitude to environmental and ethical issues can enhance a company’s value.”

Carl Rosén

Head of Corporate Governance and Communications, AP2

“As a public investor, acting in the interest of the community, Fonds de Réserve pour les Retraites is keen on assessing the extent to which companies manage the impacts of their activities on society, namely if and how they measure, limit or compensate their negative externalities.”

Nada Villermain-Lécolier

Head of responsible investment strategy, Fonds de Réserve pour les Retraites

“Caisse de dépôt et placement du Québec considers environmental, social and governance (ESG) issues in its activities mainly for two reasons: the risk they represent in investments and the essential factors they are in the pursuit of sustainable economic development, both reasons being intrinsically linked.”

Ginette Depelteau

Senior Vice-President, Policies and Compliance,
Caisse de dépôt et placement du Québec

“For MetallRente, responsible investment is not only an ethical issue but also part of efficiency: The more sustainability you put in, the more security and improvement of investment strategies you have. This ethic and efficiency is part of the social partnership in MetallRente.”

Heribert Karch
Managing Director, MetallRente

“At the CIA, we are conscious that the funds we manage belong to our members, the employees of the canton of Geneva. This means we invest with a sense of social responsibility, and give importance not only to financial results, but also to social and environmental criteria.”

Michel Ducommun
Vice-President, Employees' Representative, Caisse de Prévoyance du Personnel Enseignant de l'Instruction Publique et des Fonctionnaires du Canton de Genève (CIA)

“For PREVI, integrating environmental, social and governance (ESG) issues is a fundamental part of our strategy since our mission, beyond payment of benefits, is to assure a better standard of living for our participants in the long run. This vision puts “sustainable environment” and “social responsibility” concepts at the foremost of our investment perspective.”

José Reinaldo Magalhães
Chief Investment Officer, PREVI

“At the EAPF we believe that environmental issues like climate change have growing economic impact and will increasingly affect the financial performance and sustainability of companies. Our responsible investment strategy is grounded on fund managers' investment decision-making processes that include environmental issues for fundamental economic and financial reasons, rather than any moral or ethical reasons”

Howard Pearce
Head of Environmental Finance and Pension Fund Management

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Frequently used abbreviations

CSR	Corporate Social Responsibility
ESG	Environmental, Social and Governance (issues)
SRI	Socially Responsible Investment
UNPRI	United Nations Principles for Responsible Investment

Message from the Chairs

In the summer of 2006, the United Nations Principles for Responsible Investment (UNPRI) were launched. Leading up to and following this event, the United Nations Environment Programme Finance Initiative (UNEP FI) and the United Kingdom Social Investment Forum (UKSIF) noted a significant increase in the number of institutional investors and pension funds taking an interest in responsible investment – in particular, environmental, social and governance (ESG) issues. At the same time, there seemed to be a clear need on the part of the trustees, consultants, and managers of these institutions to understand better the why and how of integrating such considerations into the investment process.

Knowing the importance of this need, UNEP FI's Asset Management Working Group (AMWG) and the UKSIF Sustainable Pensions Project (SPP) decided to gather some examples of practical, concrete strategies being employed by some of the world's leading public pension funds and present this information in a joint publication. We believe that these examples will provide illumination to institutional asset owners and their affiliates as interest in ESG integration into asset management grows.

The UNEP FI AMWG is an alliance of 14 investment managers from Brazil, Canada, France, Italy, Japan, the US and the UK. Members collaborate to understand the multiple ways that ESG issues can affect investment value and the evolving techniques for their inclusion in portfolio investment decision-making and ownership practices.

The UKSIF SPP assists and encourages UK pension funds to adopt more sustainable and responsible investment strategies. It believes that this will protect and enhance long-term shareholder value and financial returns for beneficiaries. It focuses, in particular, on supporting UK local government pension funds and the pension schemes of those UK listed companies that are leading the way on corporate social responsibility (CSR) practice. As part of this, it seeks to raise awareness within the UK of international good practice in sustainable and responsible investment by occupational pension funds.

Over 25 public pension funds were initially surveyed, and 15 of these were selected for inclusion in this report. These range from the California Public Employees Retirement System (CalPERS) to the employees' pension fund of Banco do Brasil (PREVI) and the French Fonds de Réserve pour les Retraites (FRR). The diversity of approaches to responsible investment is wide, as is the degree of advancement in implementation. While some funds are still developing policies, others have introduced approaches to integration across their entire portfolios and multiple asset classes.

The 15 case studies offer a snapshot of the current state of play among leading public pension funds, highlighting a range of some of the most advanced and creative approaches to responsible investment from Brazil, Canada, France, Norway, Sweden, Switzerland, Thailand, the Netherlands, the USA and the UK.

We offer this document as a practical guide to the institutional investment community, particularly trustees of pension funds, foundations and life insurers, and their agents.

We thank in particular the participating funds that agreed to take part in this project, and the UNEP FI AMWG and UKSIF staff who were responsible for compiling the report.



Julie Fox Gorte
Co-Chair, UNEP FI
Asset Management
Working Group
Vice President and
Chief Social Investment Strategist
Calvert Group



Michael Deakin
Chair, UKSIF Sustainable
Pensions Advisory Board



Xavier Desmadril
Co-Chair, UNEP FI
Asset Management
Working Group
Global Head of SRI Research
HSBC Investments

Introduction and background

A wide range of issues that five years ago were considered “non-financial” such as climate change, human rights and board remuneration are now coming to the fore as factors that can have a significant impact on investment value.

The role of environmental, social and governance (ESG) issues in company valuations is increasingly being documented by analysts from leading firms¹ such as Goldman Sachs, UBS and Morgan Stanley. Internationally renowned experts such as former World Bank chief economist Sir Nicholas Stern are adding their voices. For example, his report for the UK government² in 2006 warned that global warming linked to climate change could shrink the global economy by 20%.

Institutional investors are becoming aware of the need to take into account ESG issues, particularly pension funds and others with a remit to take a long-term perspective. The question is - how?

Many investors are grappling with these issues, and there can be both hesitation and confusion as to how to reconcile the integration of ESG issues with the thorny question of fiduciary responsibility.

Research in this area has helped provide some answers. For example, the recent study by international law firm Freshfields³ suggested that, far from consideration of ESG issues being contrary to fiduciary duty, failure to assess these may well breach a trustee’s duty to act in the best interests of scheme beneficiaries.

Ironically, as one of the primary providers of the capital fuelling the international markets⁴, pension funds are in a unique position to influence market participants, principally their fund managers, to value ESG factors appropriately and integrate them into the investment process.

The purpose of this report is to remove some of the apprehension around responsible investment, and to provide some practical examples which, it is hoped, will inspire funds to devise strategies of their own. It is not intended to be a comprehensive study of best practice or a benchmarking exercise, but merely a starting point.

1 See UNEP FI materiality work here: <http://www.unepfi.org/investment> and Enhanced Analytics Initiative (EAI) extra financial work here: <http://www.enhancedanalytics.com>

2 “Stern Review: The Economics of Climate Change” HM Treasury, 2006

3 To view the report see here: <http://www.unepfi.org/investment>

4 In 2005 it was estimated that the 100 largest institutional investors in the US owned 50% of all publicly held equity

Methodology

This report takes the form of a series of case studies of public pension funds. Compiling these involved telephone discussions with the head of responsible investment or equivalent at each fund and a review of related documentation where available.

Prior to the interviews, a sample group of 25 of the largest public pension funds was identified and each was approached to participate in the study. The final 15 case studies included in this report were selected with the aim of highlighting the range and originality of approaches being followed around the globe.

Although common questions were asked of all funds the discussions were open-ended. As far as possible, despite the different approach taken by each fund, the case studies are presented in a common format for ease of reference. Each case study contains the following three sections: a description of the scheme, the scheme's rationale for pursuing responsible investment and its strategy in this area (i.e., what it actually does to implement responsible investment principles).

Please note that interviews took place during the third and fourth quarters of 2006. At the time of this report's publication – April 2007 – some of the rationales and strategies of pension funds may have been updated. Nonetheless, the case studies included offer illuminating examples of the approaches of leading funds that others can aspire to.

ABP

Stichting Pensioenfond

1. Scheme Description

Country:	Netherlands
Web:	http://www.abp.nl
Interviewee:	Rob Bauer, Head of Research
Description:	ABP is the pension fund for employers and employees in the service of the Dutch government and the education sector and the second largest pension fund in the world. It provides assurance of income security against disability, death and retirement, based on the principles of solidarity and non-profit.
Assets:	Approximately \$265 billion of which 55% is invested in equities and alternatives, 43% in fixed income and 2% in other investments. ABP manages 80% of its assets internally. The remaining 20% is managed by external investment managers.
Membership:	Approximately 2.5 million customers: 4,317 affiliated employers, 1,113,000 in active service, 761,000 former participants and 697,000 pensioners.

2. Responsible Investment Rationale

ABP views its first responsibility as a duty to deliver the highest possible return on investment to its participants. In addition, due to the large amount of capital it invests and its dominant position in the capital markets, the pension fund is aware of its investment footprint and responsibility to society. ABP's investment managers are encouraged to adopt a long time horizon. A focus is placed on long-term corporate objectives in the context of sustainable economic growth, and related environmental, social and governance information is included in its company analysis. By following this approach, ABP believes it is possible to identify opportunities and risks that are particularly relevant to long-term investors but are not properly valued on corporate balance sheets – these could relate to environmental risks, labour relations and the quality of research and development for example. Furthermore, ABP believes that sustainability and corporate governance are inextricably linked to prudent entrepreneurship and that company management must be able to account for these issues. ABP views such accountability as inherent to profitability and important to prevent a corporation from becoming alienated from the stakeholders of the society within which it operates. In this context the pension fund deems the interests of stakeholders such as employees, customers, suppliers and capital providers as paramount and believes that corporations must balance these interests while striving for profitability.

ABP's activities in the field of sustainability and corporate governance do not constitute an objective per se and the implementation of policy in these areas is constantly assessed, partly by means of a cost-benefit analysis, against a primary responsibility of generating an optimal return on investment.

3. Responsible Investment Strategy

ABP uses the term sustainable investment to describe its responsible investment strategy. At ABP, sustainable investing is a joint effort between the legal, equity investment, corporate social responsibility (CSR) and research departments. Currently the sustainable investment strategy is applied to domestic and global equities only but this is under review and may be extended to all asset classes.

Exercising shareholder rights

ABP views corporate governance and an ability to rely on sound structures for decision-making within the companies in which it invests, as key to safeguarding the long-term interests of beneficiaries. As a result, the fund has an active corporate governance policy and requires high standards of transparency, independent supervision, accountability and respect for shareholder rights from these companies. ABP exercises shareholder rights when it believes this can contribute to the risk-return profile of its investment portfolio.

ABP has established a corporate governance working group, which meets monthly to discuss current issues and further the development of the pension fund's corporate governance policy. The Working Group oversees ABP's corporate governance activities and employs three full-time staff for voting and engagement activities.

In light of the international nature of its equity portfolio, ABP assesses the quality of corporate governance on the basis of principles and codes drawn up by international authorities such as the International Corporate Governance Network (ICGN) statement on global corporate governance principles⁵, the ICGN statement on institutional shareholder responsibilities, the Organisation for Economic Co-operation and Development (OECD) principles of corporate governance⁶, and the United Nations Principles for Responsible Investment (UNPRI)⁷. In addition, ABP includes national principles and codes in its assessment where possible and relevant, such as the Tabaksblat corporate governance code⁸ in the Netherlands. ABP's policy with regard to corporate governance is set out in its Corporate Governance Code.

Voting for Dutch equity holdings

ABP votes all its Dutch holdings. It does this either by attending annual general meetings (AGMs) in-person or by entrusting proxies to a third party representative. ABP's third party representative for voting in the Netherlands is Eumedion⁹. Eumedion members have a policy of ensuring that at least one their members is present at AGMs and extraordinary general meetings (EGMs) of all Euronext Amsterdam (AEX) listed corporations. Members can choose to entrust their proxies to the attending representative to ask questions or vote. When ABP is Eumedion's designated representative, the Fund's legal and equity departments work together to analyse the strategy and corporate governance of the company in question, they also take voting decisions and prepare discussion points. Reports from all meetings are disclosed on ABP's website.

Voting for international equity holdings

ABP votes at the shareholder meetings of companies when it has at least \$13 million invested. This is the case for around 1,000 companies across Europe, the US, Canada and Australia. Proxy advice is obtained from Glass Lewis for Canadian and US equities, International Shareholder Services (ISS) for European equities, and

⁵ See Appendix for more information on ICGN

⁶ See Appendix for more information on the OECD principles of corporate governance

⁷ See Appendix for more information on the UNPRI

⁸ The Corporate Governance Committee (Tabaksblat Committee) published the Dutch Corporate Governance Code on the 9th of December 2003. On the 30th of December 2004, the Code was adopted as the code of conduct to which listed companies should refer when preparing their annual reports. For more information visit: <http://www.commissiecorporat-governance.nl>

⁹ Eumedion is a membership association of institutional investors with an interest in corporate governance in the Netherlands. It is a non-for profit organization which counts more than 50 Dutch and international institutional investors – pension funds, insurers, asset managers, etc. Eumedion operates as a representative of the interests of institutional investors in the field of corporate governance. For more information visit <http://www.eumedion.nl>

Corporate Governance International (CGI) for Australian equities. External asset managers are requested to follow ABP's voting guidelines. Once an AGM has taken place, ABP's voting decisions are disclosed on their website.

Engagement

ABP will contact company management outside an AGM in exceptional circumstances. When this occurs, engagement activities can include writing letters and communicating with management, clearly stating concerns and expected actions. In addition the fund may put additional pressure on management by voting or filing resolutions or resorting to class actions if deemed appropriate. Where satisfactory changes are not achieved, ABP can divest its holdings in a company. It participates in collaborative engagement activities through Eumedion and is currently reviewing its engagement strategy. As a part of this, the pension fund is deliberating the benefits of integrating extra-financial ESG issues into its discussions with company management. So far, ABP mainly engages on corporate governance issues, such as executive remuneration and anti-takeover devices.

Class actions

ABP will participate in class actions when, by a company's action or omission, it has suffered a loss in investment value and believes that it can retrieve a substantial part of its loss through legal recourse. Some recent examples include action against AOL Time Warner, with which ABP recently reached a settlement agreement, and Delphi Corporation. ABP will take the role of co-lead plaintiff in a class action against Delphi Corporation. It believes its role may positively influence the outcome of the proceedings and in particular the amount of damages awarded. ABP's full policy on class action participation can be found on its website.

Exclusion policy

ABP will not make investments that contravene international law. Its investment policy clearly states investments will be avoided if illegal or morally reprehensible behaviour is promoted, or the investment is directly related to a violation of human rights and fundamental freedoms

Sustainability research and integration of extra-financial factors

ABP believes that companies with strategies that encompass both financial and environmental, social and governance issues will deliver better long-term performance. As a result, the pension fund considers the integration of ESG information throughout its mainstream investment analysis to be essential and promotes the integration of material issues into its investment decision-making by both internal and external fund managers. Ultimately, ABP believes capital markets will appropriately value and reflect environmental, social, governance risks and opportunities in stock prices. However, while progress is being made, good quality data and research on extra-financial ESG issues is broadly lacking. In an effort to increase the availability of quality research ABP is pursuing various activities:

- ABP finances the European Center for Corporate Engagement (ECCE)¹⁰, a research center on ESG issues which employs approximately five full time staff.
- ABP joined the Enhanced Analytics Initiative (EAI)¹¹ to actively support better investment research.

Specialist mandates

- Investing in Sustainability: The Loyalis Global Sustainability Fund

¹⁰ ECCE helps practitioners and scholars understand how businesses and financial markets can promote sustainable development by considering ESG issues. For more information visit <http://www.corporate-engagement.com/>

¹¹ For more information see Appendix

ABP runs a portfolio in which investments are selected, managed and divested on the basis of ESG issues. The \$190 million international fund, managed by Loyalis Global, is invested in companies where potential financial value is enhanced by a clear emphasis on sustainable management practices. This best-in-class portfolio serves as an experiment for future activities in the area.

Loyalis portfolio managers have access to specialized ESG research as well as mainstream broker research and apply this ahead of traditional financial stock selection techniques. The screening and rating is undertaken by Innovest, an ESG investment research and advisory firm. It specializes in analysing company performance on environmental, social, and strategic governance issues, with a particular focus on their impact on competitiveness, profitability and share price performance. Innovest provides two types of data input: sector ratings and company ratings. Sectors are assessed based on their impact in terms of environmental and social factors. Companies are rated relative to sector peers according to their performance on environmental (e.g. emissions, product liabilities, energy efficiency), social (e.g. stakeholder relations, human rights, labour conditions) and strategic governance issues. Companies' corporate governance performance is measured by Governance Metrics International (GMI) on the basis of six criteria: board accountability, financial disclosure and internal controls, shareholder rights, remuneration, market for control and corporate behaviour. Traditional fund management techniques then assist in the final composition of the portfolio. The portfolio is balanced to maintain sector weightings corresponding to the MSCI world index. ABP is currently analysing how this ESG research knowledge can be communicated and shared with its mainstream asset managers in an organized and efficient way. It is considering various information sharing methods and groups to better facilitate the transfer of this knowledge. It also encourages other international pension funds to participate in the fund.

- Climate Change Fund

In autumn 2006, ABP invested \$363 million in Climate Change Capital's (CCC) Carbon II fund, a large private sector carbon fund run by Climate Change Capital, the UK investment banking group dedicated to investment in clean energy and a low carbon economy. The fund invests in projects, principally in developing countries, which will lead to reductions in greenhouse gas emissions.

Collaborative initiatives

ABP participates in bilateral or multilateral collaborative initiatives with other international pension funds and institutional investors such as CalPERS or Hermes when these are in alignment with its responsible investment rationale. In addition, ABP is a member of the following initiatives¹²: the UNPRI, Carbon Disclosure Project (CDP), Enhanced Analytics Initiative (EAI), Eurosif, Global Investor Governance Network (GIGN) and International Corporate Governance Network (ICGN). ABP is also a founding member of Eumedion and is active in its various committees.

Lobbying

In addition to the activities undertaken by Eumedion, ABP submits responses to consultation documents on ESG issues. For example, ABP was closely involved in the revision of the Tabaksblat Code, the Dutch corporate governance code. ABP also attends many conferences in and outside of the Netherlands and presents and publishes on its experience in corporate governance and sustainable investing.

12 For information on all initiatives mentioned below see Appendix

AP2

Swedish National Pension Fund AP Funds Family

1. Scheme Description

Country:	Sweden
Web:	http://www.ap2.se
Interviewee:	Carl Rosén, Head of Corporate Governance and Communications
Description:	Sweden's pension system is a publicly financed pay-as-you-go system. When the baby boomers of the 1940s and 1960s retire, the demands on the pension system will be considerable. Sweden expects pension disbursements to exceed contributions from 2010 onwards. To help smooth out periods of surplus and deficit five "buffer funds" have been set up. The investment regulations are identical for the First to Fourth funds (AP1 to AP4) however the funds are completely separate and have different sets of investment managers. The purpose of this is to encourage competition between the funds as well as to avoid excessive influence on the Swedish market.
Assets:	Approximately \$27 billion. Each of the four AP funds has similar AUM meaning AP funds aggregate AUM are approximately \$105 billion. AP2 has a global investment mandate. Most assets are invested in Swedish and European equities and are managed in-house, non-European and global investments are primarily managed externally. The portfolio of fixed-income assets consists mainly of nominal and inflation-linked Swedish bonds, global government securities and corporate bonds. The Fund also invests in foreign currencies, private equity and real estate.

2. Responsible Investment Rationale

The ministerial legislation that governs all AP funds states that consideration shall be given to ethics and the environment without compromising the overall goal of attaining high financial returns. The common thread for the Funds ethical and environmental policies is the set of international conventions on human rights, labour, the environment, bribery, corruption and the use of certain weapons that have been signed by the Swedish Government.

If a company is associated with infringement of any of the above-mentioned conventions, the AP funds will seek to influence it to improve its behaviour rather than divest. Each AP fund has its own ethical and environmental policy. AP2 policy focuses on governance issues. It aims to improve returns on its assets by using shareholder rights to inspire boards and executive managers to improve the way companies are run.

As a pension fund with significant assets, AP2 believes it has a responsibility to promote high ethical standards. Among other things, it actively encourages sound ethics and enlightened environmental management in listed companies, as well as promoting shareholder interests and paying attention to ethical and environmental issues in capital market regulation.

AP2 believes that an enlightened attitude to environmental and ethical issues enhances a company's value. Respect for regulations, conventions, and the formation of constructive relationships with society are essential to the solid long-term profitability of companies.

3. Responsible Investment Strategy

Following the launch of the Swedish corporate governance code in 2004, AP2's board of directors adopted a new corporate governance policy at the start of 2005. The Policy guides actions the Fund may take, and it is integrated into the Fund's day-to-day activities and subject to annual review.

AP2 encourages companies to observe the OECD's guidelines on corporate governance¹³ and the Fund's governance specific activities focus on value-generating issues such as:

- Structural issues: corporate structure, capital structure and ownership structure;
- Management issues: the board, the nomination process, executive management and executive remuneration;
- Transparency: information, dissemination of information, financial reports;
- Investment: corporate acquisitions, divestments and investments;
- Corporate culture, ethics, the environment and equality issues.

Environmental and ethical issues form an integral part of the AP2's corporate governance policy. The standards expected of companies on environmental and ethical issues are those outlined in the United Nations Global Compact Principles and the OECD's Guidelines for Multinational Companies¹⁴. Moreover, AP2's corporate governance policy stresses the importance of sound ethics which it defines as a respect for human rights, as defined by the UN Commission on Human Rights¹⁵, and rejection of corrupt business practices, prostitution, illegal drugs trafficking, the exploitation of child labour, discrimination and segregation. AP2 does not invest in companies that disregard these standards, or in countries that are subject to trade embargoes imposed by the United Nations or the European Union, and sanctioned by Sweden.

As part of its corporate governance policy AP2 values an ongoing dialogue with companies held in its portfolio on governance, environmental and ethical issues. Where the Fund sees the need for change, it seeks further contact with the company – this may be undertaken in collaboration with other shareholders.

In an effort to appropriately incorporate corporate governance in its investment process, AP2 maintains a record of specific corporate governance research supplied by investment managers and analysts. The records are updated every six months and form the basis for engagement cases. The process comprises an in-house analysis, sometimes collaboration with other investors, contact with the chairman of the board and other board members and, in certain cases, contact with the media. The Fund's in-house portfolio managers decide independently as to how governance issues should be addressed with a view to adding value.

AP2 has partnered with Sustainable Asset Management (SAM) to create a valuation model for ethical and environmental issues. This may be used by internal portfolio managers as a selection tool.

AP2 publishes information on its governance activities on an ongoing basis, on its website and in special governance reports. The information includes changes to the Corporate Governance Policy, the Fund's position on questions of principle, data on AGMs in which the Fund participated and voting decisions.

Engagement

If a suspicion arises that any company AP2 holds in its portfolio is violating sound ethics, ignoring important environmental concerns or in some other serious manner is deviating from desirable governance principles, the fund looks into the breach immediately. This may include direct contact with the company. Should the

¹³ For more information on the OECD's guidelines see Appendix

¹⁴ For more information on the UN Global Compact Principles and the OECD's guidelines see Appendix

¹⁵ The UN Commission on Human Rights is the main policy-making body dealing with human rights issues. Composed of 53 member Governments, it prepares studies, makes recommendations and drafts international human rights conventions and declarations. It also investigates allegations of human rights violations and handles communications relating to them. For more information visit <http://www.ohchr.org/>

suspicions be confirmed then the Fund will seek an explanations and a commitment to correct the problem. If the company's response is unsatisfactory, or if it fails to respond then AP2 may sell its holding in the company concerned.

In order to prepare for meetings with companies AP2 uses data from SAM, and research from NGOs as well as the company's public reports and information from the Fund's in-house investment managers and analysts. It has found companies have reacted highly positively to these meetings.

Together with the First, Third and Fourth AP funds, AP2 has established a Joint Ethical Council to monitor and maintain a dialogue with non-Swedish holdings. They believe that their joint assets under management provide more scope to influence individual companies. Through the Ethical Council, the funds coordinate their analysis of environmental and ethical compliance in foreign companies. The collaboration will involve a systematic screening of the Funds' portfolios to identify cases of violation of international conventions. The Council will review a total of 3,500 overseas companies globally. On an annual basis the AP funds wish to jointly conduct collaborative active dialogue with around ten companies that have infringed of international conventions on the environment, human rights and labour rights. The principal aim is to encourage companies to review their policies. Divestment is seen a last resort and the decision to exclude companies from portfolios will rest with individual funds. The Council consists of one representative from each of the funds and chairmanship will alternate between the funds.

Voting

AP2 votes at the AGMs of all Swedish companies and, in recent years, has voted by electronic proxy at the AGMs of companies representing its 50 largest foreign holdings. In 2005, the Fund voted against board proposals at the AGMs of 13 overseas companies. In several cases – Toyota Industries, Total, and BNP Paribas – the issue was remuneration based. In the case of Citigroup, Nestlé and Pfizer, the issue was the role of the chairman. At the Wal-Mart AGM, AP2 voted to implement a clearer system for reporting on executive and employee remuneration and on the company's sustainability programme. Voting for international holdings was put on hold in 2006.

Special mandates

In line with its commitment to integrate sustainability criteria into the asset allocation process, AP2 invested approximately \$83 million in a fund managed by SAM which takes into account a number of key sustainability issues. Companies that satisfy these criteria are selected for investment.

In addition to this portfolio, a programme has been initiated with SAM to promote a transfer of competence and ensure that AP2's investment managers adopt a consistent approach in addressing sustainability issues when making investment decisions.

Collaborative initiatives and public consultation

AP2 is a signatory to the UNPRI, participates in the CDP¹⁶ and participates in collaborative investor engagement activities with companies on an ad hoc basis. AP2 submits its opinion to ministerial consultations on social, environmental and corporate governance issues.

ARIA

Australian Reward Investment Alliance

1. Scheme Description

Country:	Australia
Web:	http://www.aria.gov.au
Interviewee:	Steve Gibbs, CEO
Description:	Aria provides superannuation services and products to employees of the Australian Government through three schemes – the Commonwealth Superannuation Scheme (CSS), the Public Sector Superannuation Scheme (PSS) and the PSS Accumulation Plan (PSSap).
Assets:	Approximately \$13.5 billion combined in the three funds. All assets are externally managed with 30% of the portfolio invested in Australian equities and 25% invested in global equities. Aria considers itself to be a long-term universal investor in the Australian market.
Membership:	Over 305,000 members

2. Responsible Investment Rationale

Aria's rationale for responsible investment is based on a risk management philosophy that involves monitoring the governance aspects of invested companies. This approach recognises that poor ESG practices can lead to financial risks as well as a decline in investment value. As a fiduciary with a duty to act in the best financial interests of its members, Aria believes that all risks, including these, must be minimised. This is consistent with its primary investment objective of maximising long-term returns for members. In addition, Aria believes that while environmental, social and governance risks often feature in the standard risk management practices of leading Australian businesses, investment managers generally do not adequately account for the damage to long-term shareholder value that mismanagement of these issues can incur. In response, Aria has developed a range of strategies to cover this gap and improve risk monitoring; these include voting and a monitoring and engagement strategy.

3. Responsible Investment Strategy

Voting

The purpose behind voting, in Aria's view, is to ensure companies in its portfolio follow best corporate governance practice. It believes this approach underscores its commitment to ensure long-term value for members and sends a clear signal to management that, as a shareholder, it is prepared to consider and vote upon every resolution in the best interests of members. Aria votes at the shareholder meetings of all companies in which it owns shares. Voting advice for Australian holdings is obtained from Corporate Governance International (CGI) and the Australian Council of Superannuation Investors. The final voting

decisions rest with Aria trustees however and all Australian equities are voted by the scheme itself. For international holdings, Aria takes advice from International Shareholder Services (ISS), and uses their electronic proxy voting service.

Monitoring ESG risks and engagement strategy

In 2001, Aria asked for advice from external investment service providers to develop a systematic approach for monitoring and mitigating ESG risks in its Australian portfolio. The resulting product, Governance Advisory Service (GAS), was developed with the objective of protecting and enhancing value by identifying risks that could impact investments both presently and in the future. BT Financial Services¹⁷, the group that developed GAS, was appointed to research corporate governance risks in Aria's Australian equity holdings, and make recommendations to its board on constructive means for diminishing or eliminating risks found. The ESG assessment is currently conducted in partnership between BT and Monash University¹⁸. BT undertakes corporate governance risk analysis, and environmental and social risk analysis is undertaken by Monash University.

Aria's action plans to mitigate risk range from State and Federal Government policy level submissions to dialogue with industry sectors or groups and direct contact with individual companies. Since its development, a number of other superannuation funds have joined GAS, including the Northern Territory Government and Public Authorities Superannuation Scheme, the Catholic Superannuation Fund, Vic Super and the Emergency Services Superannuation Fund. Aria considers the costs of developing and maintaining GAS to be low compared to the risks it assists in mitigating for investors with long time horizons. Many believe Aria's pioneering initiative in this area has assisted in raised the bar for standards across corporate Australia.

Governance Advisory Service (GAS) in detail

Aria's engagement strategy is mainly concerned with improving corporate governance. Aria has never divested due to poor governance but would not rule it out. In 2003, Aria's GAS programme was recognized by the United Nations with an award for responsible and sustainable investment¹⁹.

As Aria's investment governance advisor, BT's mandate is to work with the board to:

- Identify potential ESG risks: A formal review of potential ESG risks to long-term shareholder value is conducted on a yearly basis by BT in partnership with Monash University. Both international and domestic issues are examined. Consideration is given to current issues and those that might arise in the short to medium term. At the last review, a list of over 70 potential risks was identified.
- Assess the importance of ESG risks and prioritise them for consideration: The list of ESG risks is subjected to a rigorous analysis that identifies the potential impact on portfolio value. The analysis is quantitative in nature and the results allow risks to be ranked by potential severity. At the last analysis a priority list of 12 ESG issues was identified for further investigation
- Research the exposure of companies to the high priority ESG risks: BT and Monash University conduct research into companies listed on the S&P ASX200²⁰ to determine the level of exposure of each to the ESG risks. Exposure to the relevant risk factor is rigorously assessed. The output from the research is a risk score for each company. The higher the score, the greater the potential risk.

17 Formerly Westpac Investment Management

18 Monash Sustainability Enterprises (MSE) was established in July 2000 as a consulting, advocacy, and training arm of the Monash Centre for Environmental Management. MSE is involved in a number of research initiatives and commercial ventures to promote more sustainable practices in the investment and finance sectors. For more information see: <http://arts.monash.edu.au/ges/mse/>

19 The Royal Award for Responsible Investment, is a collaboration between UNEP FI and the Copenhagen based Royal Awards for Sustainable Development. For more information see: <http://www.royalawards.org/awards>

20 The S&P ASX200 is recognized as the investable benchmark in Australia. Index constituents are drawn from eligible companies listed on the Australian Stock Exchange. This index is designed to address investment managers' needs to benchmark against a portfolio characterized by sufficient size and liquidity.

- Assess the effectiveness of companies' responses to those risks and identify any gaps: BT and Monash conduct a second layer of research to determine steps taken to manage the high priority ESG risks present. The output from this research is a score. The higher the score, the more appropriate the companies' management of the risk. By comparing each company's exposure score with its management score, any gaps are identified. Where such gaps exist, this suggests a company may not be managing a particular ESG risk appropriately. The gap analysis is then reviewed to determine whether gaps exist in isolated cases, are confined to one or a number of industry sectors, or are generally found. Finally, in an effort to assess relative importance in the investment portfolio, each company's risk gap is weighted according to its market capitalisation.
- Work with the board to develop action plans to mitigate the risk gaps: This phase is characterised by the development of a Dialogue Action Plan. Possible strategies for Dialogue Action Plans include the use of media, position statement, policy request, industry comment, company letter, company meeting, company conversation or a combination of the above.
- Implement the action plans on behalf of Aria: When a Dialogue Action Plan is approved, BT is responsible for implementing the plan. Implementation of a Dialogue Action Plan will usually include the development of a position paper setting out the risk issue and explaining the reasons for the Boards' concerns.

Step 1

- For companies with low weighting in the index dialogue by written correspondence seeking clarification on issues of concern.
- For companies with high weighting in the index: Meeting with management and board members seeking clarifications on issues of concern.

Step 2

- BT will consider responses and enter into a dialogue as appropriate depending on the response received in step one.
- The company must demonstrate that concerns are being addressed otherwise BT will request behavioural change.
- The company is given a timeframe to resolve the problem and a requirement to report on improvement.

Step 3

Report back to Aria's board on the effectiveness of the implementation: BT reports quarterly, or more frequently if necessary, on engagement activities and results. Since inception, GAS has noted a number of improvements in corporate behaviour in the following areas:

- Audit and governance.
- Directors' share trading rules.
- Workplace health and safety practices.
- Environmental disclosure.
- Disclosure of energy use.

Specialist sustainability mandates

Aria invests 5% of its Australian equity in a sustainable portfolio managed by AMP Capital Sustainable. This fund's investment universe is limited to companies that follow sustainable strategies and practices. A standard financial model is then used to select from this pre-approved universe. Aria believes this strategy should produce good returns over the long-term.

To summarise AMP Capital's overall approach to sustainable investment it:

- Identifies ‘industry of the future’ companies – in sectors with the most socially and environmentally sustainable performance outcomes, including education and training, health care, renewable energy, waste management and mass transport
- Excludes industries judged to be the least sustainable as a result of their social, ethical and environmental performance such as those with material exposure to the production or manufacture of alcohol, armaments, gambling, nuclear, pornography and tobacco
- Encourages companies in less sustainable sectors such as forestry, oil and mining to meet higher CSR standards. Such companies are expected to take a proactive and leading approach to corporate social responsibility
- Undertakes standard financial analysis to identify suitable companies for investment from the approved universe.

If a company falls below the required standards for investment, shares in that company are sold within six months. Shares may also be sold at any time for financial reasons.

Collaborative initiatives and consultation

Aria is a signatory of the UNPRI and the CDP²¹. Aria responds to consultation papers and present policy level submissions on ESG issues to industry groups and to the State and Federal Australian Governments.

21 See Appendix for more information on UNPRI and CDP

Caisse de dépôt et placement du Québec

1. Scheme Description

Country:	Canada
Web:	http://www.lacaisse.com
Interviewee:	Marie-Claude Provost, Senior Director, Policies and Compliance
Description:	The Caisse de dépôt et placement du Québec was created in 1965 by an act of the Canadian national assembly to manage the funds contributed to a newly created universal pension plan, the Québec Pension Plan. In the decades that followed, many other public-sector organizations also became members.
Assets:	Approximately \$143.5 billion invested in domestic and international public and private equity, bonds, real estate, currencies and hedge funds. Of the total assets, 80% are internally managed and 20% are externally managed.
Membership:	Originally, the Caisse managed only the funds of the Régime de rentes du Québec (RRQ). Over the years, many depositors, most of them public bodies, have been added to the RRQ. As at December 31, 2006, the Caisse had 22 depositors – pension funds, insurance plans and various other types of funds. About 60% of the contributions from these bodies come from individuals. For example, the pension plan for governmental and public bodies' employees (RREGOP) is the largest depositor. It is a compulsory plan for Quebec's workforce, with contributions provided by employers and employees.

2. Responsible Investment Rationale

The law states that the mission of the Caisse is “to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return on capital within the framework of depositors' investment policies while at the same time contributing to Québec's economic development.” The Caisse believes that its contribution to economic development cannot be dissociated from the commitments it makes as a good corporate citizen. It encourages the companies in which it invests to conduct themselves as good corporate citizens in the communities in which they operate; in other words, to act responsibly and participate in the economic and social life of their communities.

In pursuing its SRI activities, the Caisse is guided by its fiduciary obligation to members. It therefore prefers a single comprehensive approach within a framework that is sufficiently flexible to suit all its depositors, namely achieving a workable balance between ethics and profitability. A company's social behaviour is one of several criteria used to determine whether or not to buy its shares but not the deciding factor.

The Caisse aims to maximize its influence in the area of SRI over time. For this reason it favours an active approach through exercising its voting rights and engaging in dialogue with the companies in which it invests. In the majority of cases, the Caisse adopts a medium- or long-term approach to investments, it therefore intends, within the limitations of the law, to monitor and to help contribute to the profitability of the companies in which it invests. Its contribution is intended to be constructive by targeting first and foremost a common objective - the success of the companies - and, consequently, the best possible financial returns.

Through its approach to SRI, the Caisse hopes to encourage like-minded institutions to adopt similar strategies

3. Responsible Investment Strategy

In 2005, on the recommendation of its human resources, ethics, and corporate governance committees, the Board of Directors of the Caisse adopted an SRI policy. Before adoption, the policy was submitted to the depositors of the Caisse for approval. On an ongoing basis, the Caisse informs depositors of SRI developments through an annual formal consultation, which also allows members to voice their expectations, views and concerns.

The SRI Policy is intended to define a clear but flexible framework within which the Caisse can make a credible and effective contribution to improving corporate social behaviour. Accordingly, the policy states that the Caisse expects the companies in which it invests:

- To conduct their activities with respect for rights and fundamental freedoms enshrined in legislation and to prohibit any form of discrimination;
- To respect workers rights, to take all measures necessary to ensure a healthy and safe work environment and to prohibit any form of abuse or coercive labour;
- To take all measures necessary to respect and protect the environment in which they operate;
- To respect the local communities in which they conduct their affairs and to promote community development.

Incorporating social, ethical and environmental criteria into portfolio management

In alignment with the SRI Policy, the Caisse expects its investment managers to take social, ethical and environmental criteria into account in their investment risk analysis. Managers are expected to keep abreast of the environmental practices and labour relation policies that companies pursue as well as their involvement and integration in their local communities. In addition, managers are expected to undertake in-depth research on agenda items at shareholder meetings and to make voting recommendations. They are responsible for obtaining policies, reports, ethical and environmental studies and assessments of companies as necessary. Managers are also expected to inform companies of the importance that the Caisse attaches to such reports, assessments and studies.

The Caisse intends to integrate social, ethical and environmental issues into investment decision making across all assets. To that effect, all investment managers receive annual training on SRI.

Equities

The Caisse uses specialist research firms to obtain ESG ratings for Canadian companies. These ratings are incorporated into a research platform provided by the Caisse to its investment managers. In addition the Caisse will provide specialist assistance to investment managers to aid with the integration of ESG issues into their investment decision-making. For all publicly listed equities, investment managers are provided with a list of ESG factors they are expected to take in account in their investment decision processes.

Bonds

The Caisse uses specialist research firms to obtain corporate governance ratings for corporate bonds. Again, these ratings are incorporated into a platform provided by the Caisse to its investment managers.

Engagement

Investment managers are required to make companies aware of the importance of developing and adopting policies and practices in line with best practice CSR. They are responsible for establishing a relationship with corporate CSR officers and for ensuring that requirements of the Caisse in this regard are properly communicated and understood. In addition, investment managers are expected to ensure the requests of the Caisse pertaining to improvements in behaviour are taken on board and that company management

seeks to make improvements where necessary. So far, engagement activities have been focused mainly on Canadian companies and have been triggered by the media, shareholder resolutions or concerns raised by portfolio managers. The Caisse maintains the right to sell its shares in a company should its behaviour prove unsatisfactory and dialogue be unproductive. .

Voting

The Caisse votes at the shareholder meetings of all companies held in internally managed portfolios in accordance with the voting guidelines in its policy. The policy provides a guide for the exercise of voting rights and sets out voting positions on issues such as the independence of board of directors, executive compensation, incentive plans, takeover protection mechanisms and shareholder rights. In addition to these issues, the policy specifies that the Caisse will always take into consideration the principles set out in its Policy on Socially Responsible Investment when addressing social, environmental and ethical issues.

Additionally, the Caisse has established a number of voting principles concerning the following specific ESG issues:

- Companies are encouraged to adopt policies on governance, workers' rights and conditions, standards of ethical conduct, outsourcing, political contributions and all other related elements.
- Shareholder proposals that seek disclosure of companies' environmental and social activities are supported.
- In a democracy, exercising the right to vote is proper to citizens not to companies and the latter must not financially influence the democratic process. The Caisse is opposed to contributions made by companies to political parties or similar movements. If a company makes such contributions, the Caisse favours reporting on the contributions made.

Investment managers are required to make voting recommendations before the Caisse casts its votes. The Caisse also takes an external third party firm's recommendations into account before voting. The Caisse believes that voting is a powerful tool. For example, in 2005 it voted in favour of a shareholder resolution requesting that Wal-Mart publish a sustainable development report. Although the resolution was defeated, the position of the Caisse was covered in the media. Wal-Mart subsequently contacted it to arrange a meeting to present the activities it planned to undertake in the field of sustainable development.

A statistical report is periodically submitted to the board of directors and to the members of the Caisse to advise them of voting decisions taken at AGMs and EGMs.

Collaborative initiatives

The Caisse participated in the committee which compiled the UNPRI and is a signatory²².

22 See Appendix for more information on UNPRI

CalPERS

California Public Employees Retirement System

1. Scheme Description

Country:	USA
Web:	http://www.calpers.ca.gov http://www.calpers-governance.org
Interviewee:	Dennis Johnson, Senior Portfolio Manager, Corporate Governance
Description:	CalPERS was established by state law in 1932 and is the largest public pension plan in the US and the third largest in the world in terms of asset under management. The Pension plan provides a variety of retirement and health benefits programs and services to the State of California's public employees, retirees, and their families. CalPERS is a defined benefit retirement plan.
Assets:	Approximately \$230 billion. Assets are managed internally and externally and the fund employs both active and passive investment strategies across four asset classes: Global equities, global fixed income, real estate, and alternative investments. CalPERS considers itself a long-term, universal owner.
Membership:	Approximately 1.5 million public employees, retirees, and their families and more than 2,500 public employers.

2. Responsible Investment Rationale

CalPERS is a leader in the area of corporate governance. Their approach is best described as the prudent exercise of ownership rights with the aim of increasing shareholder value while minimizing risk. The central rationale, that shareholders are equity owners in the company and must be active and prudent in the use of their rights in the management of their investments, is based on the concept that shareowners collectively have the power to direct the course of corporations. The Pension Plan believes economic wealth can be either created or destroyed through shareholder activism and hence must be done responsibly. Corporate governance is central to CalPERS' ownership practices and is used as a tool for both monitoring performance and enhancing value.

CalPERS' board has a fiduciary obligation to undertake its responsibilities in accordance with the twin duties of loyalty and care. Loyalty is understood as a necessity to act solely in the interest of members and beneficiaries. Care is understood as the necessity to manage assets as a prudent investor. Inherent in the concept of prudence is the duty to monitor investment performance.

In the US, the Employee Retirement Income and Security Act (ERISA)²³ was passed in 1974 and the US Department of Labour (DOL) administers title one of ERISA. CalPERS' standards of fiduciary duty are in alignment with the ERISA, which states that pension fiduciaries may be held accountable for screening the performance of holdings, including the performance of holdings in passive portfolios. In 1988 the DOL issued its so-called Avon Letter²⁴, putting private pension plan trustees on notice that proxy-voting rights must be

²³ The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for pension plans in private industry

²⁴ In 1988, the Department of Labor issued a set of guidelines, now known as the «Avon Letter,» directing Employee Retirement

diligently exercised as an aspect of fiduciary duty. In 1994 the DOL updated its Avon Letter in a bulletin that consolidates the voting requirements of ERISA fiduciaries. The DOL now advocates an activist role for pension plan trustees, to include activities intended to monitor or influence corporate management.

CalPERS expects the directors of public corporations to conduct themselves with propriety and a view toward responsible corporate conduct that is consistent with practices and policies outlined by the Global Sullivan Principles²⁵. The Global Sullivan Principles relate to CSR and have as their objective to assist companies in supporting economic, social and political justice where they undertake business. The underlying tenet for these principles is that the companies must have governance structures that enable them to be fully accountable to shareholders and that lead, over the long-term, to the best returns to shareholders. This is based on the understanding that sound corporate governance leads to improved long-term performance. While CalPERS recognizes the right of other investors to pursue a range of issues, the pension plan strictly limits its activities to issues that have a demonstrable impact on financial returns.

3. Responsible Investment Strategy

Exercise of shareholder rights

Voting

CalPERS' corporate governance department votes its domestic and international equity holdings, in accordance with the Pension Plan's Statement of Investment Policy for Global Proxy Voting and the Core Global Principles of Accountable Corporate Governance. CalPERS' Global Principles of Accountable Corporate Governance embrace those adopted by the ICGN²⁶. In addition to conducting its own analysis, CalPERS considers advice from proxy voting agencies such as Glass Lewis, ISS, Proxy Governance and Egan Jones when making voting decisions. CalPERS supports shareholder resolutions that are consistent with its Principles of Accountable Corporate Governance does not result in long-term harm to the company. Additionally, CalPERS submits its own resolutions and encourages other shareholders to support proposals on various corporate governance issues.

The corporate governance team provides the CalPERS board with detailed quarterly reports explaining voting decisions. In an effort to more effectively communicate with other shareowners and market participants, CalPERS' post voting decisions for its top 300 domestic companies as well as the focus list companies on its website approximately two weeks prior to the annual general meetings taking place.

Engagement

In addition to its voting activities, CalPERS undertakes systematic engagements, at companies where the equity is owned both internally and externally, which are pre-approved at board level by the CalPERS investment committee. CalPERS engages with companies on issues which may pose a risk to the value of its portfolio. Companies are given a timescale to implement behavioural changes and report on improvement. CalPERS prefers to engage with companies rather than to divest their holdings in them.

Current corporate governance initiatives

Executive compensation programmes

Compensation programs are one of the most powerful tools available to companies to attract, retain and motivate key employees, as well as align their interests with those of shareowners. Poorly designed compensation packages may have disastrous impacts on company and shareholder value by incentivising short-term oriented and self-interested behaviour. Conversely, well-designed compensation packages will help

Income Security Act (ERISA) fund managers to vote proxies with the same diligence as making other fiduciary decisions.

25 See Appendix for more information

to align management with owners and drive long-term superior performance. As a result, CalPERS believes shareholders should exercise a stronger oversight of executive compensation programs. It pursues pay-for-performance initiatives with regulators, stock exchanges, and companies. These include:

- Targeting a number of companies in key market sectors with the worst compensation practices
- Urging companies to submit executive compensation policies to shareowners for approval, including disclosure of pay-for-performance provisions and a non-binding shareowner vote on compensation packages
- Proposing that corporate boards seek shareowner ratification of any severance agreement that provides benefits that exceed 2.99 times the sum of an officer's base salary, plus target bonus
- A comprehensive proposal to the Securities and Exchange Commission (SEC) that calls for greater transparency of executive compensation packages.

Majority vote for corporate directors

CalPERS advocates majority voting for directors. Currently, a plurality system is used at most US companies in which directors can be elected onto the board by the vote of a single share unless they are opposed by a dissident candidate. Shareholders who object to a candidate can only withhold their votes, there is no option of voting against directors at US companies. As a result, CalPERS:

- Advocates majority voting for directors
- Seeks to implement majority voting at individual companies through company bylaw and charter amendments
- Seeks to implement majority voting via discussion with the SEC and major stock exchanges
- Pursues changes to state laws to implement majority voting where feasible.

Environmental corporate governance plan

CalPERS adopted a corporate governance environmental strategy to improve data transparency and timely disclosure of environmental impacts such as those associated with climate change. The Pension Plan expects timely and complete information on environmental risks to assist in making more complete investment decisions. In the long run, CalPERS believes companies must address environmental issues such as climate risks and opportunities in order to remain competitive and sustain long-term returns. Thus CalPERS has launched a number of initiatives aimed at improving environmental data transparency, some examples of these include:

- Signing the CDP²⁷
- Engaging companies in the utilities sector. In July 2005, CalPERS was one of 15 signatories representing more than \$550 billion in assets that signed a letter sent to 43 of the country's 50 largest publicly quoted greenhouse gas (GHG) emitters in the electric power and utilities industry. The letter requested that the companies report within a year on how future GHG limits will affect their financial bottom line and any steps they are taking to reduce those financial impacts and improve their competitive positioning.
- Working to support the Investor Network on Climate Risk's (INCR) call for action, a ten-point plan that calls on US companies²⁸, Wall Street firms and the SEC to intensify efforts to provide investors with comprehensive analysis and disclosure on the financial risks presented by climate change.
- Identifying companies held in its portfolio with shareholder resolutions on their AGM agenda requesting improved environmental risk disclosure and by voting in favour of these, supporting efforts to improve accurate, timely reporting of risks such as those associated with climate change.

²⁷ See Appendix for more information

²⁸ See Appendix for more information

- Engaging companies in the insurance sector, CalPERS and 19 other members of the INCR have asked the 30 largest U.S.-based companies to undertake a comprehensive analysis of the business implications of climate change and report the findings of that analysis to shareowners.

CalPERS investment staff are also in the process of targeting companies in the transportation, utilities and oil and gas sectors that fail to disclose environmental data.

CalPERS' focus list

The CalPERS' Corporate Governance Focus List program identifies poor performing companies within its domestic portfolio. Companies selected on an annual basis are targeted for engagement on corporate governance. The process is designed to identify and constructively work with undervalued companies in the portfolio that produce the lowest long-term value relative to peers and lack good governance practices. CalPERS begins the process by screening more than 1,200 US companies within its internally managed equity portfolio. It then narrows the list of candidates to 15 to 20 companies based on their long-term stock performance, corporate governance practices, and an economic value-added evaluation. CalPERS uses economic value-added evaluation and stock performance to identify companies where poor market performance is due to underlying company specific operating performance problems as opposed to industry or extraneous factors. Companies that perform poorly in the quantitative screen and qualitative review are then individually analysed to determine whether CalPERS, through engaging in discussions with the company's board and management, could potentially add value and improve performance. In its engagement process CalPERS makes a persistent effort to meet with company management and directors to discuss performance and governance issues. It focuses on reforming governance practices with an emphasis on accountability, transparency, independence, and discipline. The CalPERS' Corporate Governance Focus List program has led to positive results which include: director and managerial changes; formal governance policy improvements; increased transparency and communication, pay-for-performance; formal board self-evaluation processes; auditor independence; shareowner-approved proposal implementation and supermajority voting-right elimination. Research shows that the actions CalPERS takes to influence corporate governance change, can lead to performance improvements over time²⁹.

Screening strategies

Emerging markets exclusion list

CalPERS has a policy on emerging markets equity investment, which sets minimum acceptable standards for investment in an effort to control risk and enhance returns. Potential returns are weighed against associated risk in these countries and CalPERS permits investment managers to invest in companies listed in countries that meet prudent market standards and outweigh risk. The research is undertaken by Wiltshire Associates on an annual basis. For inclusion in the permissible investment universe, countries need a minimum score of two on the CalPERS' investment threshold. The threshold is a composite of scores ranging from one to three for country and market factors, which include: political stability, including civil liberties and an independent legal system; transparency, including press freedom and accounting standards; productive labour practices that prohibit abuse and offer legal recourse, including adherence to International Labour Organisation (ILO) conventions and principles³⁰; market liquidity and volatility, including the health of the country's stock market; market regulation, regulatory and legal protections for investors; openness to foreign investment; and the proficiency and cost of financial transactions.

The draft list of countries is placed on CalPERS' web site and a copy is sent to both the US embassy of every evaluated country and the head of the respective country's primary stock exchange. Countries and other interested parties have 30 days to review the report and provide feedback or additional information to be

²⁹ A Wiltshire Associates study of the «CalPERS Effect» of corporate governance found that the stock values of companies on the Focus List companies subsequently outperformed the Standard & Poor's 500 Index by 8.1% over five years. For more information see CalPERS corporate governance website: <http://www.calpers-governance.org>

³⁰ See more information in Appendix

considered before the list is reviewed and approved by CalPERS' Board. Once approved by the CalPERS Board, the list is circulated to both internal and external investment managers with instructions to only invest in public equity of permissible countries.

CalPERS expects portfolio emerging economy companies to conduct themselves with propriety and with a view toward responsible corporate conduct. However, CalPERS recognizes that adopting formal corporate governance principles, such as the ICGN Principles, may not be appropriate for every company in emerging capital markets due to differing developmental stages, ownership structure, regulatory structure, competitive environment, or a myriad of other distinctions. Nonetheless, CalPERS believes that with adequate, accurate, and timely disclosure of environmental, social, and governance practices, shareowners are able to more effectively make investment decisions by taking into account those practices. Therefore, CalPERS recommends companies in emerging markets formalize a reporting mechanism by which sustainable development practices can be disclosed to stakeholders, including shareowners, such as the Global Reporting Initiative (GRI) Sustainability Reporting Guidelines .

Sudan position statement: screening and engagement

Concerned by potential risks to its portfolio, CalPERS adopted a position statement on Sudan in 2006. The position reiterates the Pension Plan's view that companies undertaking business in Sudan may be unwittingly furthering the human rights violations occurring there. A company associated with the violations taking place in Sudan poses a serious risk to long-term value. As part of its position statement, CalPERS passed a motion to ban investment in nine companies identified as providing monetary or military support to the Sudan government, while showing little or no interest in the violence in Darfur or willingness to improve the welfare of the Sudanese people. The list of excluded companies was transmitted to both internal and external asset managers. For additional companies held in their portfolio and identified as conducting business in Sudan, CalPERS undertakes constructive engagement to ensure that those companies are not contributing to genocide. In a review of its global equity portfolio, CalPERS identified 94 companies with a presence in Sudan which were selected for systematic engagement. CalPERS contacted each company, requesting that they describe in detail the impact of their business on human rights and respond to related concerns. Companies are encouraged to explore all options to understand and limit the impact of their operations on human rights violations and complicity including: developing specific policies as well as working with pertinent entities such as the United Nations Global Compact³¹, the Business Leaders Initiative on Human Rights (BLIHR)³² and the Collaborative for Development Action Collaborative Learning Projects³³. CalPERS staff reports on the Sudan engagement strategy on a regular basis to its Investment Committee.

On September 25, 2006, the Governor of California signed Assembly Bill 2941 and its effective date was January 1, 2007. AB 2941 prohibits CalPERS from having investments in a company engaged in active business operations in Sudan that fails to take substantial action as defined in the bill. It also requires CalPERS to sell or transfer any investments in a company that fails to take substantial action within 18 months subject to CalPERS' fiduciary duty. CalPERS must report to the California Legislature on an annual basis beginning January 1, 2008 any investments in a company with business operations in Sudan.

Lobbying

Where deemed appropriate, in addition to engaging with individual companies or industry sectors, CalPERS may make representations at a broad policy level to promote shareholder rights. The Pension Plan often advocates corporate governance best practices to the US SEC, major stock exchanges and the California legislature. CalPERS also articulates its opinion to investors inside and outside of the US through speaking at conferences.

31 See more information in Appendix

32 See more information in Appendix

33 CDA Collaborative Learning Projects is a non-profit organization, based in USA, committed to improving the effectiveness of international actors who provide humanitarian assistance, engage in peace practice, and are involved in sustainable development. For more information see <http://www.cdainc.com/>

Legal action

Where its rights as a shareholder have been violated, CalPERS may resort to legal and class actions in order to recover of lost assets. CalPERS is currently suing companies including Enron, Time Warner, WorldCom and the New York Stock Exchange on allegations ranging from fraud and deception to excessive stock-option grants. CalPERS' General Counsel provides quarterly updates on all CalPERS' litigation activities to the full Board and litigation information is posted on the pension plan's website.

Specialist mandates

Environmental investment initiative

CalPERS has a strong track record of mobilizing financial capital in new and innovative ways, consistent with the highest fiduciary standards and is starting to explore ways in which it can marry capital market investment with public purpose. By investing in three different asset classes with environmental considerations, CalPERS' goals are to achieve positive financial returns while fostering energy savings, sustainable growth and sound environmental practices.

CalPERS' invests \$200 million in environmental technology solutions that are more efficient and less polluting than existing technologies. Areas of particular interest include alternative and renewable energy, water technologies, advanced materials or nanotechnology, air purification technologies, and transitional infrastructure opportunities. CalPERS is building a diversified portfolio of clean technology-focused investments by investing across stages, strategies, geographies and structures through private equity and venture capital firms. The primary objective of the programme is to achieve attractive investment returns over the long-term and catalyse the adoption of environmentally sustainable and clean technologies in the broader marketplace.

CalPERS has earmarked \$500 million for investment in stock portfolios that use environmental screens. Six asset managers are investing assets using environmental strategies:

- AXA Rosenberg manages a domestic product including undervalued companies selected from an environmentally-friendly universe.
- Brandywine Asset Management uses environmental research to select a portfolio of undervalued international stocks.
- New Amsterdam Partners examines environmental, social and sustainability factors as part of the decisions it makes to invest in domestic growth companies.
- Piper Jaffray obtains environmental research and analysis from KLD Research & Analytics which it uses to screen companies and make investment decisions
- State Street Global Advisors manages domestic and international products. Innovest rates each investment prospect based on eco-efficiency.

CalPERS invested \$75 million in the iShares KLD Select Social Index Fund managed by Barclays Global Investors. The fund seeks to maximize exposure to large cap companies that have positive social and environmental characteristics while maintaining acceptable risk and return characteristics.

Real estate environmental strategies

Through its real estate environmental strategy CalPERS' focus is to generate attractive investment returns while adopting environmental and green building technologies in areas such as energy efficiency, water conservation, waste stream management and indoor air quality within the Pension Plan's overall real estate portfolio. CalPERS board has set an energy reduction goal of 20% in its core real estate portfolio over the next five years. To achieve this goal, CalPERS works with its real estate partners who report on energy savings methods such as adjusting or reprogramming of temperature control systems, installing sensor-operated flushers and faucets, and sorting scrap metal and other materials for recycling. The pension fund owns

approximately \$5 billion in core real estate that includes office, retail, industrial, and apartment properties. The real estate environmental strategy also supports green building initiatives and continues to explore investments that fit within the Leadership in Energy & Environmental Design (LEED) Energy Star requirements³⁴.

Economically targeted investment programme

Economically targeted investment has collateral intent to assist in the improvement of both national and regional economies and the economic well-being of the State of California, its localities and residents. Economic stimulation includes job creation, business creation, increases or improvement in affordable housing and improvement of the infrastructure. Over the course of several years, CalPERS has developed a number of unique investment strategies designed to target economically underserved segments of the State of California. In May 2001 it established the California Initiative Program under which \$475 million of commitments were allocated to ten private equity funds for investment in underserved markets in California and other areas. The initiative aims to provide jobs and economic stimulus to underserved geographies and populations.

CalPERS corporate governance investment program

In addition to its engagement activities, CalPERS has created a Corporate Governance Investment Program for which it has earmarked \$5 billion. The strategic objective of the program is to achieve returns not available in traditional public markets. CalPERS' Corporate Governance team manages an active investment program by partnering with external corporate governance fund managers. A Corporate Governance Fund is broadly defined as a highly concentrated portfolio where the portfolio managers of the fund actively engage with the portfolio companies to unlock value through governance operational strategic and/or management changes.

Collaborative initiatives

In addition to collaborating with other investors on various initiatives on a case by case basis – joint company engagements, joint lobbying activities, class actions, etc – CalPERS is a signatory of the following initiatives: UNPRI, CDP, Investors Network in Climate Risk (INCR), EITI, ICGN, Global Investors Governance Network (GIGN), Council of Institutional Investors (CII), Asian Corporate Governance Association (ACGA)³⁵

34 Every year, the U.S. Environmental Protection Agency recognizes top partners in its voluntary Energy Star program that have made outstanding contributions to energy efficiency and environmental protection.

35 For further information on all mentioned initiatives see Appendix

CIA

Caisse de Prévoyance du Personnel Enseignant de l'Instruction Publique et des Fonctionnaires du Canton de Genève

1. Scheme Description

Country:	Switzerland
Web:	http://www.cia.ch
Interviewee:	Michel Ducommun, Vice-President, Employees' Representative.
Description:	CIA is the largest contingency fund (pension and insurance) of the canton of Geneva, Switzerland. It covers all public education and civil servants of the central administration of the State
Assets:	Approximately \$5 billion split almost equally between equities, bonds and real estate. Assets are externally managed with the exception of the real estate portfolio.
Membership:	35,000 active members and pensioners.

2. Responsible Investment Rationale

The CIA has considered sustainable development in its investment strategies and policies for over 20 years.

The CIA has a democratic management structure in which there is extensive involvement by cantonal pension fund members and takes a strong interest in the social aspects of its investments. The CIA's supreme governing body, the assembly of delegates, is composed of 180 representatives elected by pension fund members. The assembly of delegates votes on statutes and main policies, such as investment strategies and asset allocation guidelines. In 1996, the CIA set out its responsible investment policy in its statement of investment principles, which is publicly available. The policy was discussed, debated and approved by pension fund members via the assembly of delegates.

As a public pension fund with a long-term horizon and significant assets under management, the CIA believes it has a responsibility towards members and society as a whole. As an institutional investor, it has a social responsibility to reflect on its role as an economic agent. Conscious of its investment footprint, the CIA monitors how funds are invested as well as the potential impact of its investments .

The Pension Fund aims to invest assets in a manner consistent with promoting sustainable development. The strategy takes account of economic, environmental and social dimensions and is based on the necessity to meet the needs of the present generation without compromising the needs of future generations. Accordingly, the CIA requires its asset managers to integrate sustainable criteria into their investment decision-making.

3. Responsible Investment Strategy

The CIA's responsible investment strategy is applied across its entire portfolio. All investment mandates integrate sustainable development criteria including a social, environmental and economic evaluation of corporations.

Equity exclusion policy

The CIA does not invest in companies where more than 5% of revenues come from weapons, tobacco, gambling or nuclear production or agrochemical companies where more than 5% of revenues come from genetically modified products.

Investment manager selection process

In all its requests for proposals (RFPs), the Fund states that it requires investment managers to take account of its exclusion policy and integrate sustainable criteria into portfolio construction and management. The CIA also seeks investment managers that can take account of environmental and social issues of particular interest to the Fund such as corporate environmental policy, recycling, supply chain management, collective bargaining and human rights. Provided these requests are taken into account, investment managers are free to pursue the investment strategy they deem most appropriate. At the selection interview, investment managers are questioned on their responsible investment strategy and are often accompanied by a partner ESG research service provider.

The CIA favours investment in companies which operate best practice management of the environmental and social contexts in which they operate as well as having sound financial prospects. The CIA tends to favour active mandates and best-in-class proactive approaches, investing in corporations that have the most responsible ESG management. The CIA believes this is the most appropriate manner in which to encourage improvements in corporate behaviour.

Some examples of the CIA's mandates include:

- An active strategy that includes companies on the basis of a sustainability evaluation undertaken by an independent ESG research provider. Companies are analysed from an environmental and social perspective in order to rate their contribution to sustainable development. Those managing ESG issues best are rated highest and are over-weighted in the portfolio. Poor ESG performers are under-weighted.
- An active mandate that uses a best-in-class sustainability strategy to determine a permissible investment universe before using a financial screen to complete the selection.
- A passive mandate that reproduces the Dow Jones Sustainability Index (DJSI), a sustainable development passive index based on a best-in-class strategy.

While investment managers are not remunerated on the basis of returns to society, the CIA accepts that there may be a need for higher management fees linked to the responsible investment mandates. Investment managers are evaluated on a basis of their compliance with the CIA's responsible investment strategy and the sustainability of their portfolio is assessed and compared to the sustainability of the benchmark. The CIA expects its portfolios to outperform benchmarks in sustainability terms and ideally financial terms.

Sovereign bonds

For sovereign bonds Centre Info, an ESG research provider, rates countries according to sustainability criteria such as economic stability, corruption, free speech, and human rights. Any given country will need to obtain a minimum score in order to be included in the CIA's permissible investment universe. The list of excluded countries is communicated to investment managers who must not invest in these countries.

Real estate

The CIA's real estate portfolio is managed internally. Its real estate policy strategy is to produce optimum financial returns while providing affordable, good-quality housing to the residents of the canton of Geneva. Accordingly, 90% of the portfolio is located in Geneva and 40% is invested in low-rent housing with a strong commitment to good maintenance and renovation. The CIA follows a responsible real estate investment policy by funding affordable housing that follows best-practice architectural and energy saving qualities and provides sound returns to pension fund members.

Exercise of shareholder rights; creation of and participation in Ethos Foundation

In 1997 the CIA co-founded Ethos³⁶ Swiss Foundation for Sustainable Development with the Caisse Paritaire de Prévoyance du Bâtiment pension fund. Its purpose is to manage assets that include environmental and social criteria and promote the consideration of sustainable development principles and corporate governance best practice in investment activities. Ethos provides engagement services for investors on these issues. The organisation is member driven and has around 85 institutional investor members. Ethos also offers third party proxy voting services, it analyses resolutions and submits recommendations allowing pension funds to combine their voting rights in order to ensure maximum impact.

Voting

The CIA exercises its voting rights by instructing investment managers to vote in accordance with advice obtained from Ethos for both Swiss and international holdings, but maintains the right to override Ethos's recommendations in special cases. The pension fund also attends Swiss company AGMs where it largely limits its interventions to matters related to the promotion of sustainable development.

Engagement

The CIA's engagement activities are normally undertaken by Ethos. Each year, the members of Ethos discuss and select four to five topics for engagement with Swiss companies such as corporate governance and outsourcing. The members then agree to finance the engagement strategy, which is undertaken by the ownership service provider. Examples of successful engagement strategies include obtaining an agreement from UBS to publish an annual social report.

Example of successful exercise of shareholder rights

In 2005 Ethos, with the voting rights of six member funds including CIA, filed three resolutions at the Nestlé AGM, requesting:

- The separation of powers between the CEO and Chairman
- Modification of the company by-laws.
- Lowering of the minimum threshold required to submit a resolution.

Although the resolutions were defeated, Nestlé listened and took notice. Shortly after the AGM, it undertook a shareholder consultation, asking shareholders what they thought of the statutes and requesting a mandate to modify them.

Collaborative initiatives

CIA has signed the UNPRI³⁷ and favours collaborative initiatives between pension funds to improve efficiency and negotiation power.

36 For more information see <http://www.ethosfund.ch/>

37 See Appendix

Environment Agency Pension Fund

1. Scheme Description

Country:	United Kingdom
Web:	http://www.environment-agency.gov.uk
Interviewee:	Howard Pearce, Head of Environmental Finance and Pension Fund Management
Description:	The Environment Agency is the environmental regulator for England and Wales. It has major responsibilities for controlling pollution control and water management, and is dedicated to protecting and improving the environment so that tomorrow's generations inherit a cleaner and healthier world. The Environment Agency Pension Fund (EAPF) is the 20 th largest member of the UK's Local Government Pension Schemes (LGPS) ³⁸ and one of the largest 100 pension funds in the UK.
Assets:	Approximately \$2.7 billion all externally managed.
Membership:	18,000 members

2. Responsible Investment Rationale

The Environment Agency is a leading public sector body dedicated to protecting and improving the environment so that tomorrow's generations inherit a cleaner and healthier world. The Agency considers it important to align its values with the investment principles of its pension fund and as such the Environment Agency Pension Fund (EAPF) seeks to manage its investments in a manner, which is both financially robust and environmentally responsible.

In 2004, following several years of poor stock market returns and media criticism, including claims that the Fund was invested in highly polluting industries, EAPF reviewed its investment policy, including its view on the exercise of shareholder rights. In 2005 it launched its responsible investment policy to ensure that investment managers take account of environmental issues and other long-term risks and opportunities that can affect financial returns. Consistent with this view, the EAPF believes financially material issues like climate change are increasingly important and will increasingly affect the performance of companies. As a result its strategy is grounded on investment decision-making that includes material environmental issues for financial reasons, rather than ethical reasons. The Pension Fund deems this strategy to be entirely consistent with its fiduciary duty, which requires it to manage all assets in a manner consistent with maximising financial returns for beneficiaries. It will assess and account for existing and future financial risks such as climate change and potential costs related to environmentally damage, as well as opportunities that arise from innovative approaches to environmental issues such as renewable energy and technology. Furthermore, EAPF believes that organizations that best manage environmental risks, impacts, and opportunities are more financially sustainable in the long-term and organizations that take such an approach are good for the environment and the economy, as well as their owners.

³⁸ With 3.5 million members, the Local Government Pension Scheme is one of the largest public sector pension schemes in the UK. It is a nationwide pension scheme for people working in local government or working for other types of employer participating in the Scheme. Employers in the Scheme include local authorities and public service organisations as well as other employers that provide the LGPS for their employees by becoming admitted bodies. The Scheme is administered for participating employers locally through 99 pension funds. For more information visit: <http://www.lgps.org.uk>

3. Responsible Investment Strategy

The EAPF's responsible investment strategy seeks to exploit the relationship between good environmental management and long-term sustainable businesses. The Pension Fund believes its main areas of influence are through its strategic asset allocation, investment portfolio structure, investment manager stock selection, performance targets, monitoring, and reporting – and not by getting involved in the day-to-day investment decisions, which is the role of its investment managers. It encourages investment managers to undertake and use research on environmental issues to avoid financial risks attributable to environmental issues impacting negatively on investment returns. The Pension Fund monitors investment manager performance and asks managers to explain and justify investment decisions. EAPF favours investing on a positive best-in-class selection basis, takes an active approach to the exercise of its shareholder rights and encourages the use of engagement rather than negative screening.

Environmental overlay strategy

EAPF has deployed an environmental overlay strategy across 100% of its pension fund, all asset classes and investment activities that its investment managers must adopt and comply with. The strategy includes specific requirements for each asset classes. Using the strategy, the Pension Fund selects investment managers that integrate environmental risk assessment into their investment decision-making and monitors both financial and environmental performance.

Investment manager selection

Investment managers are evaluated on their ESG competencies during the selection process and have to detail in their response to RFPs how they integrate financially material environmental risks and opportunities as well as other sustainability criteria into their investment process. This includes stock selection, portfolio management, research, engagement, voting and performance reporting. Managers must also detail how they use thematic and best in class styles to identify financially robust companies that contribute to sustainable development. The manager's responsible investment specialists are invited to attend selection interviews and the manager is questioned on its ESG competences.

With the exception of property and private equity managers who report annually, investment managers are expected to report quarterly on both their investment performance and on their engagement with, and voting record at, companies. Decisions to abstain or vote against shareholder resolutions must be justified.

Investment managers are also evaluated on the basis of their ability to deliver the EAPF's environmental overlay strategy. This includes the integration of environmental issues into investment decision-making, engagement, voting and referral of any environmental resolutions to the Agency. Their relative performance will also be benchmarked using financial and corporate governance and socially responsible investment indices. Under the UK Local Government Pension Schemes (LGPS) investment regulations³⁹, the Agency can terminate contracts if performance is below that required.

The EAPF selects investment managers via the European Union procurement process⁴⁰ and uses a standardized investment management agreement for all mandates. These include its investment, corporate governance and environmental policies and disclosure and reporting requirements.

Responsible investment across asset classes

The EAPF's environmental overlay strategy applies to all its investment managers and features specific requirements for each asset classes.

³⁹ The LGPS rules are contained in regulations made by Parliament after consultation with both employee representatives (Trade Unions) and employer representatives. The rules comply with the relevant provisions of the UK Pension Schemes Act 1993, the UK Pensions Act 1995 and the UK Pensions Act 2004. For more information visit: <http://www.lgps.org.uk>

⁴⁰ EU Procurement process requires at least 52 days between advertisement and tenders being received. For more complex procurements longer is needed, sometimes up to about 80 days.

Public equity

The EAPF has several mandates with different investment strategies. Equity fund managers are required to use specialist ESG research providers or, if they have the capacity, in-house ESG research. Around 7% of the EAPF's assets are invested with a manager that explicitly integrates sustainability and environmental considerations into a selection of best-in-class companies (both large and small to medium sized) within best-in-class-sectors. Sustainability is the first criterion for stock selection, economic criteria the second. The Pension Fund also has an active emerging markets equity portfolio.

Bonds

The EAPF's investment manager does not hold bonds issued by companies where it perceives there to be a liability, such as a litigation risk, based on ESG issues. For example, companies with a large exposure to elements that can damage human health, such as asbestos, tobacco, and genetically modified organisms, are excluded.

Private equity

The EAPF invests in a specialist sustainable private equity fund-of-funds, which includes a variety of funds in Europe and the US with a bias towards energy, water, waste, food and health sectors. Approximately 30% of the mandate is allocated to environmental technology funds. The EAPF's private equity investment manager will only invest in funds where the funds and the underlying companies have pledged to act in a responsible manner.

Property

The EAPF invests in a segregated fund-of-funds that was specifically designed for them. Investments include around 12 UK based property funds, giving the Pension Fund a broad exposure to the UK property market. The investment manager carries out environmental risk assessments across all 12 funds before investing. The EAPF's property portfolio also includes a sustainability and regeneration property fund that invests in disused brown fields sites and works in conjunction with the public sector to develop and provide well designed, mixed use, sustainable urban communities in the UK.

Voting

Investment managers are required to vote, when feasible, for all equity holdings on behalf of the Pension Fund and in the UK are encouraged to vote in line with the general principles of the UK Combined Code⁴¹, the Association of British Insurers (ABI) guidelines and the Institutional Shareholders Committee (ISC) principles. The Pension Fund also provides investment managers with details of its corporate governance and environmental policies and preferred voting positions. Managers are required to refer environmental-related resolutions to the EAPF, the Pension Fund decides how to vote these itself. In 2006, the EAPF voted on 49 US company environmental shareholder resolutions – an 80% increase on 2005.

Engagement

The EAPF defines environmental governance as a company's management of environmental impacts, risks, performance and opportunities. In line with its responsible investment strategy the Pension Fund encourages invested companies to report on environmental issues and disclose the environmental risks they face and performance against these.

41 The Combined Code on Corporate Governance sets out standards of good practice in relation to issues such as board composition and development, remuneration, accountability and audit and relations with shareholders. All companies incorporated in the UK and listed on the Main Market of the London Stock Exchange are required under the Listing Rules to report on how they have applied the Combined Code in their annual report and accounts. The Combined Code contains broad principles and more specific provisions. Listed companies are required to report on how they have applied the principles of the Code, and either to confirm that they have complied with the Code's provisions or - where they have not - to provide an explanation. For more information visit: <http://www.frc.org.uk/>

The EAPF complies with the principles of activism laid out in the Myners' report⁴² and aims to become more engaged as an active investor, especially with companies whose environmental behaviour and performance are currently impacting negatively on investment returns – or could do so in the future. The Pension Fund mainly delegates engagement activities to its investment managers. Managers are expected to engage on behalf of the Pension Fund with companies on the following issues:

- Climate change
- Emissions and other environmental externalities
- Contaminated land and related clean-up issues
- Natural habitats and wildlife issues

Investment managers report their engagement activities on a quarterly basis. The reporting details issues discussed, the outcomes of discussions, actions agreed and timelines for these.

ESG research

Resources permitting, the EAPF undertakes responsible investment research in-house and will support joint studies with other pension funds and organizations that have interests in responsible investment, especially research related to environmental performance and financial returns. Where appropriate this research may be used to inform the Pension Fund's own investment policies. In the past EAPF has carried out research on corporate reporting and carbon management and green investment funds. Examples include a study on the extent and nature of environmental disclosure of FTSE All-Share companies and a study on the carbon management and carbon intensity of the FTSE All-Share index. All research that the EAPF commissions is publicly available on its website.

Collaborative initiatives

The EAPF favours partnerships and alliances with other pension funds to increase the impact of its engagement with companies.

The Pension Fund will collaborate with investors with similar responsible investment objectives and environmental goals. Such organizations include the UK Social Investment Forum (UKSIF), the CDP, the Local Authority Pension Fund Forum (LAPFF) campaign on environmental reporting, and the Institutional Investors Group on Climate Change (IIGCC). The Agency has also signed the UNPRI and encourages its fund manager to participate in the EAI⁴³.

Performance

The EAPF launched its responsible investment policy in 2005. It believes the results have been positive so far, in particular for specialist sustainability mandates and alternative energy related investments. The Pension Fund's overall return in 2006 was 22.8% (0.8% above its benchmark). Seven managers exceeded their performance benchmarks and four beat their performance targets. Sarasin Chiswell, the Agency's specialist SRI fund manager, which manages 7% or \$195 million of the actively managed assets and mainly invests in EU based companies, produced the best performance (9% above their benchmark) this year.

42 In March 2000, the Chancellor of the Exchequer commissioned Paul Myners to conduct a review of institutional investment in the UK. Myners concluded that there were a number of areas where change would result in improved investment decision-making. In his report, which was published in March 2001, he recommended that pension fund trustees voluntarily adopt, on a 'comply or explain' basis, a series of principles codifying best practice for investment decision-making. Under Myners' activism principles trustees are recommended to ensure that managers have an explicit strategy, elucidating the circumstances in which they will intervene in a company; the approach they will use in doing so; and how they measure the effectiveness of this strategy. For more information see: <http://www.hm-treasury.gov.uk>

43 For details on all above mentioned collaborations and initiatives see Appendix

The merits of the new investment strategy have also been recognised externally. The EAPF has won several awards including– the LGC Corporate Governance Award⁴⁴, the IPE SRI Fund of the Year Award⁴⁵, the Global Money Management Public Pension Fund of the Year Award⁴⁶ and the 2006 Professional Pensions Best Use of SRI Award⁴⁷.

44 This award is give to the UK council pension fund, which has done the most to promote good governance over the preceding 12 months. Evidence of achievement can take a variety of forms. It may involve dealings with an individual company affecting behavioural change among a cluster of firms, or a general review of policy regarding corporate governance. For more information see here: <http://www.lgcnet.com/>

45 For more information see <http://www.ipe-awards.com/>

46 For more information see <http://www.globalmoneymangement.com/>

47 For more information see <http://professionalpensions.com>

ERAFP

Etablissement de Retraite Additionnelle de la Fonction Publique

1. Scheme Description

Country:	France
Web:	http://www.rafp.fr
Interviewees:	Philippe Caila – Managing Director Remy Lamont – Risk Manager
Description:	Etablissement de Retraite Additionnelle de la Fonction Publique (ERAFP) was created in 2004 as the compulsory supplementary French civil service employees pension scheme. Members include hospital workers and military service personnel. The scheme supplements the state pay-as-you-go pension. Contributions are collected from state employees' ad-hoc compensations – bonuses, overtime, benefits-in-kind – that were not previously taken into consideration for pension purposes. French law requires the scheme to be fully funded and overseen by a board of directors composed of employers and union representatives.
Assets:	Approximately \$4 billion with an annual growth of \$2 billion. Expected AUM in 2010 is \$12 billion. The asset allocation policy allows for a maximum of 25% invested in equities, with a limit of 10% invested in non-euro currencies, all managed externally. The remaining 75% is invested in bonds and managed internally.
Membership:	4.6 million public service workers and future pensioners and 48,500 employers.

2. Responsible Investment Rationale

In 2005, the Pension Scheme's board of directors adopted an investment policy that takes broad societal and stakeholder interests into account. SRI is a fundamental pillar of the policy and all assets are invested according to this approach. The ERAFP's investment decisions are made using financial risk and return objectives and are based on the understanding that SRI and financial performance can be aligned. As a long-term investor, the ERAFP believes assessing ESG issues is a key element in properly valuing the risks and opportunities associated with companies held in its portfolio. The ERAFP believes investment strategies that seek only to maximise financial returns can be harmful in the long-term.

In an effort to forward their work in SRI, the ERAFP's board of directors adopted an SRI charter in March 2006. The six-page charter outlines the Pension Scheme's beliefs, values and broader social vision. The ERAFP scheme members were represented on the board when the charter was adopted and participated in its drafting and finalization.

The policy concerns all issuers: states, territorial collectives, public organizations, supranational organizations, financial institutions and corporations.

By investing according to its SRI charter, the Pension Scheme intends to favour activities, companies and states that promote broader societal and stakeholder interests. Aside from being a sound long-term investment strategy, the ERAFP believes its SRI rationale is aligned with the societal goals and values of its members. The scheme's aim is to combine investment performance with SRI and to strive to combine private sector best practices with public sector values.

3. Responsible Investment Strategy

The ERAFP's SRI charter is currently being implemented and when deemed necessary by the board may be subject to revisions. . As a first step towards implementation, the board has identified several guiding values that it considers to be of primary importance. These guiding values will be added as an appendix to the ERAFP's SRI charter and will be used as the criteria for assessing issuers. The appendix states how the values should be reflected in investment decision-making, portfolio construction, engagement strategy, voting, submission of resolutions, questions at AGMs and participations in collaborative actions with other investors. The guiding values are:

- **Law and human rights:** when making investment decisions, the ERAFP includes an evaluation of an issuer's compliance with local and international laws, as well as their respect and promotion of human rights. Where applicable, the ERAFP will make an assessment in order to understand any potential impacts of their investments on: discrimination of any form, freedom of speech, labour conditions, corruption and money laundering. When specifically evaluating sovereign nations, in addition to considering the ratification and implementation of international standards and conventions, the ERAFP will also consider issues such as use of torture and the death penalty and the presence of children in the military. Based on these assessments, the ERAFP may choose to refrain from investing in certain companies, nations or states. One example is the ERAFP's decision not to invest in American states where the death penalty is still in use.
- **Social advances:** the ERAFP favours employers and companies that follow best practice in labour management. Accordingly the Pension Scheme will assess states and companies on the basis of their respect for labour laws, including the number of working hours per week and statutory or contractual benefits. In addition, the fund will assess how the underlying investment contributes to the improvement and development of employment practices in areas such as training and equal gender representation in the workplace.
- **Social democracy:** the ERAFP favours investment vehicles and investment issuers that respect employee rights. The Pension Scheme will favour investments in companies and states that respect the right of freedom of association including unionisation and employee health and safety.
- **Environment:** the ERAFP aspires to contribute to sustainable development and promote environmental preservation. Accordingly, the scheme assesses issuers, companies and states on environmental issues and includes any environmental impacts that result from commercial activities and production processes in its investment decisions. In its assessments the ERAFP will consider carbon emissions, biodiversity, pollution risks and eco-efficiency. In addition, the Pension Scheme will assess the adoption and implementation of environmental policies and environmental reporting and certification.
- **Governance and transparency:** When making investment decisions, the ERAFP includes an evaluation of an issuer's governance and level of transparency. The evaluation includes an assessment of governance practices, respect of legal and fiscal laws, ethical policy (relative to tax havens, money laundering, codes of ethics), relationship with stakeholders and operational and financial transparency. Generally, the Pension Scheme will consider these issues on a global basis. For example, a multinational's global supply chain is to be considered. For state issuers, public policies are also considered.

Sovereign bonds

The ERAFP holds more than \$3.3 billion in Euro-zone sovereign bonds that have been selected according to SRI criteria. When composing the portfolio, the ERAFP weighted the bonds according to the percentage Gross Domestic Product (GDP) of each of the 25 European Union member states. Then, it over-weighted bonds from countries that had adopted and implemented international conventions and under-weighted those from countries that had not. The Pension Scheme rates countries using lists of signatories to international conventions as well as lists compiled by Transparency International⁴⁸. When making decisions to invest in sovereign bond, the ERAFP believes it is essential to assess debt quality by considering countries' laws and regulations as well as their track records on ESG issues such as climate change. Nonetheless, the Pension Scheme adopts a relatively flexible approach that includes consideration of a country's overall situation as well as its efforts to improve.

Investment service providers

The ERAFP has selected investment service providers Vigeo and Oekom to assist in developing and implementing its SRI charter. The service providers will assist the Pension Scheme to implement its policy in line with the guiding values listed above. In particular service providers will:

- Define ESG indicators and methods for their integration in investment decision making
- Develop a method to assess issuers' compliance with the SRI policy.
- Monitor the ERAFP's portfolios and flag issues where necessary.
- Take a consultative and a non-directive role in the selection and construction of mandates.
- Develop the ERAFP's annual SRI reporting system.
- Propose other actions for inclusion in the ERAFP's SRI policy.

Equities

In June 2006, the ERAFP launched a tender for a Euro-zone SRI equity portfolio. The objective was to award four mandates of \$60m - \$530 million each. Successful investment managers had to demonstrate how their strategies are compatible with the ERAFP's SRI charter and how they combine transparency with performance and compliance with SRI principles. The ERAFP has opted for an active management strategy in order to optimise investment opportunities and favours a best-in-class approach. Investment managers will have to report at least annually on how they have applied the SRI charter in their investments.

Collaborative initiatives

The ERAFP is a signatory of the UNPRI⁴⁹ and is considering joining other initiatives.

48 Transparency International (TI) is a leading international non-governmental organization addressing corruption. This includes, but is not limited to, political corruption. It is widely known for producing its annual Corruptions Perceptions Index (see below), a comparative listing of corruption worldwide. For more information see: <http://www.transparency.org/>

49 See Appendix

Fonds de Réserve pour les Retraites

1. Scheme Description

Country:	France
Web:	http://www.fondsdereserve.fr
Interviewee:	Nada Villerman-Lecollier, Head of Responsible Investment Strategy
Description:	The French retirement system is built on the related notions of pay-as-you go and inter-generational solidarity. In common with those in other industrialised nations, the French pension system currently faces a number of challenges. Predicted impacts of changing demographics on public retirement systems have led to the creation of reserve funds to pre-finance all, or a portion of, future public liabilities. France established the Fond de Réserve pour les Retraites (FRR) in 1999. The aim of the Fund is to supplement pay-as-you-go pension schemes where needed from 2020 onwards. The FRR is a publicly owned, state-funded agency governed by an executive board of three and steered by a supervisory board of 20 people.
Assets:	Approximately \$42 billion. Approximately 32 investment managers worldwide externally manage all assets.

2. Responsible Investment Rationale

When established, the FRR was legally required to disclose how social and environmental issues are taken into consideration. Its board decided to build on this and take an even stronger stance on sustainability issues and so put into place a responsible investment policy. The Board regularly reaffirms that the principal aim of the fund investment policy is to maximise returns subject to a given level of risk. It states that it is attached to its commitment to responsible investment as embodied in the Principles for Responsible Investment elaborated under the auspices of the UN by an international group of investors, including FRR.

As a public investor with a broad-based public service mission, the FRR strives to manage assets in accordance with values that promote balanced economic, social and environmental development. When compiling their responsible investment policy the FRR decided this should be consistent with the principles of sustainable development, benefits to the community and long-term investor and universal owner practices.

The FRR's aim is to optimise investment returns by 2020. The fund was created to benefit future retirees in France and so believes it also has a role in promoting general societal and community interests. For this reason, FRR decided to adhere to investment policies that are consistent with community values. It therefore takes account of corporate practices and behaviour insofar as these could have positive or negative impacts on the general public. Due to its size, mission and the nature of its beneficiaries, the FRR views itself as a long-term investor and universal owner.

3. Responsible Investment Strategy

The FRR's Responsible Investment strategy comprises the following basic elements:

- Voting at shareholder meetings via proxies and external asset managers consistent with the FRR's voting guidelines
- Encouraging mainstream investment managers to adopt responsible investment practices

- SRI mandates that integrate ESG issues into investment decision-making and portfolio management.

The FRR has decided to concentrate on implementing its responsible investment policy within all European equity mandates and global large-cap mandates. The fund aims to extend the universe of assets to which the policy applies but with relatively few investment managers offering suitable products it considers that there is a need for greater maturity in the marketplace before it can advance further. In addition, responsible investment is dependent on quality sources of relevant information on companies' social and environmental policies and performance. For certain geographical regions and asset classes, these sources are currently too limited to support the development of a viable market for investment management services.

Voting

The FRR delegates the exercise of its shareholder rights to its external investment managers, who use the fund's voting guidelines as a framework. The guidelines were compiled using various standards issued by investors, industry associations and international organisations. Investment managers report on their voting activities on a quarterly basis and the FRR also has access to electronic voting platforms that permit the fund to follow voting decisions taken on its behalf. Most of the FRR's investment managers have developed a policy of approaching company management to explain reasons for their voting decisions. In the case of French companies, this contact takes place prior to the shareholder meeting. For overseas companies, the manager must set out the explanation for the voting decision in a letter after the meeting.

Promoting responsible investment

A significant percentage of the FRR's European equity is not managed according to a responsible investment approach. Nevertheless, for these portfolios and in an effort to increase mainstream investment manager sensitivity to responsible investment, FRR has requested all investment managers to commit to the following at a minimum:

- Undertake basic research and analysis of the social and environmental behaviour of companies considered for investment, including a framework assessment based on the UN Global Compact principles⁵⁰. This aims to broaden and deepen investment manager knowledge of companies to enable more informed investment decision-making and also to identify the most appropriate extra-financial performance indicators.
- Make an effort to integrate the findings of this research gradually into the investment decision-making processes
- Report transparently on the way in which extra-financial criteria have been integrated into portfolios and any problems encountered in doing this
- Exchange information with the FRR on research methodologies, so the fund can eventually build its own benchmark and methodology.

Examples of some of the innovative approaches adopted by investment managers as a result of these basic commitments include:

- A portfolio limited to the FTSE Large Cap Europe index that screens out worst in class companies, including those in breach of the UN Global Compact principles, before applying traditional financial stock selection techniques.
- A portfolio with no exclusion policy or screening filter but strong engagement activities with worst in class companies.
- The construction of a shadow portfolio that incorporates an analysis of material ESG risks and opportunities into investment decision-making. If and when the pilot portfolio shows positive financial results, the investment strategy will be modified accordingly.

Mainstream investment managers have agreed to report to the FRR on their efforts every six months.

⁵⁰ See Appendix

SRI Mandates

In 2005, the FRR put out an RFP that included several mandates for investment managers with expertise in SRI. The five-year mandates are for European equities and to an aggregate sum of \$800 million. The mandates required the integration of ESG issues into investment decision-making on a best in class basis. To assist investment managers, the FRR drew up a set of responsible investment principles. The principles describe the FRR's expectations of companies held in their portfolios including management practices and relationships between companies and their stakeholders and the environment in which they operate. The principles cover five major themes:

- Respect for international law and basic human rights
- Job development through better management of human resources
- Corporate environmental responsibility
- Respect for consumers and fair trade practices in local markets
- Promotion of best corporate governance principles and practice

Around 40 European investment management firms expressed interest. A shortlist of 20 managers was asked to submit final proposals. In April 2006, the FRR's Executive Board chose the five following investment management firms: AGF Asset Management, Dexia Asset Management, Morley Fund Management, Pictet Asset Management and Sarasin Expertise Asset Management. The selection criteria used to award these mandates were, in descending order of importance:

- Quality of SRI management processes provided, particularly the dedicated human and technical resources allocated, capability in extra-financial analysis and its suitability to FRR's needs, as well as the SRI management process
- Quality of the organization in operational terms particularly in the areas of risk management, SRI reporting and voting
- Total management costs

The objective of the RFP was to select the most coherent investment processes, in particular with respect to portfolio building techniques and the inclusion of both financial and extra-financial criteria. These processes are diverse, and this diversity is naturally reflected in the proposals that were selected. Some of these are described below:

- Best-in-class strategies: Starting with the MSCI Europe Benchmark, the investment manager applies an ESG screen to determine the permissible investment universe. Companies are given a sustainability rating based on the FRR's five responsible investment principles. Best performers get included in the investment universe and companies rated below a minimum acceptable standard are screened out. The asset manager then applies a classic financial stock selection model to create the final portfolio.
- ESG matrix strategy: Using an ESG rating provider, as well as internal research, the investment manager plots sectors in terms of their sustainability rating. The manager then assesses the ESG behaviour and performance of companies within each sector. Sectors that have a higher sustainability rating are selected and the behaviour and performance of companies within those sectors is assessed. The investment manager combines these assessments within a matrix to establish the investment universe. In a less sustainable sector, the investment manager will apply a more stringent analysis and select the best performing companies from an ESG perspective. In a more sustainable sector, the asset manager can apply less stringent selection rules. The asset manager then applies a classic financial stock selection model to create the final portfolio.
- ESG financial weighting strategy: The investment manager analyses companies' financial and extra-financial performance in parallel. Companies are awarded a financial rating and an ESG rating. The investment manager then conducts arbitrage between the two to complete the stock selection process.

- Engagement strategy in parallel with the SRI strategy: In addition to an active stock selection strategy, some investment managers include an active engagement strategy with the companies included in the portfolio.

All investment managers report quarterly to the FRR on financial performance and on SRI activities including voting.

ESG research providers

The FRR has selected three ESG research providers in order to help it to achieve the following objectives:

- Measure the environmental, social and governance quality of its portfolio;
- Assess the extent to which its investment approach contributes to sustainable development
- Identify financial threats and opportunities to which the Fund may be exposed.

Vigeo analyses the FRR's European equity portfolio – approximately \$18 billion – on the basis of the fund's responsible investment principles. Both EIRIS and Trucost assess the FRR's global equity portfolio – approximately \$ 23 billion. EIRIS assesses portfolios for compliance with international standards, in particular those linked to the FRR's first principle of respect for basic human and worker rights. Trucost assesses portfolios for environmental imprint, threats and opportunities. In addition all of the service providers supply the FRR with screening and extra-financial research services. This is aligned with the Principles for Responsible Investment (PRI), which the FRR signed in April 2006.

Collaborative initiatives

The FRR played an active role in 2005 in developing the UNPRI. The FRR also supports other initiatives, such as the CDP⁵¹ as well as academic research in the area of SRI by co-financing a professorship on the subject.

51 See more information on UNPRI and CDP in the Appendix

Government Pension Fund Global (Norway)

1. Scheme Description

Country:	Norway
Web:	Government Pension Fund Global: http://www.regjeringen.no/en/dep/fin Council of Ethics: http://www.etikkradet.no Norges Bank Investment Management: http://www.nbim.no
Interviewee:	Dr. Henrik Syse, Head of Corporate Governance, Norges Bank Investment Management.
Description:	Currently the largest pension fund in Europe, the Government Pension Fund Global was established in 2006 as a continuation of the Petroleum Fund which itself was set up in 1990 as a fiscal policy tool to support long-term management of the petroleum revenues. Renaming the Fund in 2006 was part of a broader reform, giving the Fund a central role in facilitating the government savings necessary to meet the expected rapid rise in public pension expenditure. The Norwegian Ministry of Finance is responsible for the Fund and has delegated the day-to-day management of the assets to Norges Bank, the Central Bank of Norway. Norges Bank Investment Management (NBIM) invests the Fund's capital in overseas bonds and equities in accordance with guidelines issued by the Ministry. Capital inflow to the Fund consists of net state petroleum revenues less the sum needed to cover the non-oil budget deficit.
Assets:	Approximately \$280 billion of which 60% is invested in bonds and 40% in equities, all assets are invested outside of Norway and the majority are managed by NBIM.

2. Responsible Investment Rationale

Following several instances where the Fund attracted attention for holding controversial companies for example those with activities in arms or tobacco production, the Norwegian government devised ethical guidelines and a council of ethics to oversee their implementation of these. Established by royal decree in November 2004, the guidelines are based on the understanding that the purpose of the Fund is to ensure that a portion of the country's petroleum wealth benefits future generations and that its assets are managed in a manner that generates a sound financial return, which is seen as contingent sustainable development. In addition, the guidelines make clear the fund should not make investments which constitute an unacceptable risk of contributing to unethical acts or omissions – such as violations of fundamental humanitarian principles, serious violations of human rights, gross corruption or severe environmental damage.

3. Responsible Investment Strategy

Exercising ownership rights: voting and engagement

Norges Bank Investment Management (NBIM), a division of the Central Bank of Norway, is responsible for exercising the Pension Fund's ownership rights. NBIM's primary objective is safeguarding the Fund's financial interests and views company boards as ultimately responsible for ensuring that business is conducted in a manner that protects shareholders' long-term interests. Following several well-known cases in recent years where management has destroyed value, NBIM is a keen proponent of good corporate governance practices. To ensure shareholders' long-term interests are protected, firms must effectively manage relationships with

employees, suppliers and customers, follow a code of ethics and take into account the impact of their activities on their surroundings and society in general. NBIM views the willingness to obey national and international laws and conventions and to respect fundamental ethical and environmental principles as part of good corporate governance. A lack of ability or willingness in this respect may put a company's reputation at risk and jeopardise its business. NBIM encourages companies to refer to the UN Global Compact principles as well as the OECD Guidelines for Multinational Enterprises and the OECD Guidelines for Corporate Governance⁵² for guidance on how they can incorporate ethical and environmental considerations into their business activities. NBIM aspires to contribute to promoting human rights, environmental protection, and political stability. It reports annually on how ownership rights are exercised and how the aspirations of good corporate governance and sustainability are advanced on behalf on the Government Pension Fund.

Voting

In order to ensure companies and other investors have confidence in their activities, NBIM ensures that its voting activities are undertaken in a rational and predictable manner. It therefore votes at all shareholder meetings itself. In 2005, it voted on 20,307 resolutions at 2,705 general meetings. Where necessary, it takes voting recommendations from proxy voting service providers.

NBIM's voting decisions are guided by a set of principles which were developed as part of the Fund's Ethical guidelines and are based on internationally recognised codes such as the OECD Principles of Corporate Governance⁵³. One of NBIM's fundamental voting principles is that companies should act in accordance with the UN Global Compact principles and the OECD Guidelines for Multinational Enterprises. The full voting guidelines are available on the NBIM website. Its voting decisions shall be made public from 2007.

In 2005, shareholder proposals accounted for more than 3% of the resolutions on which NBIM voted. NBIM has voted in favour of shareholder proposals on the following subjects:

- Equal voting rights for all shares
- Splitting the roles of CEO and chairman
- Anti-takeover mechanisms, golden parachutes and severance agreements
- The ability of shareholders to propose board candidates
- Expensing stock options
- Executive compensation
- Policies on human rights
- Social and environmental impact reports
- Reports on equal rights for all employees
- Reports on compliance with the Kyoto Protocol⁵⁴

Engagement

As an owner, NBIM expects companies to provide an account of how well they comply with principles or codes of corporate governance. In addition to corporate governance, NBIM engages and discusses other issues with companies which it views as being potentially damaging to long-term financial value, contradictory to the Fund's principles, or of key concern in relation to OECD and UN guidelines. Where deemed an appropriate and effective means of achieving a desired result, NBIM participates in, or initiates, cooperation between institutional investors and individual companies.

52 See Appendix for more information on the UN Global Compact principles and both the OECD Guidelines for Multinational Enterprises and the OECD Guidelines for Corporate Governance

53 See Appendix for more information

54 Established in 1997, the Kyoto Protocol to the United Nations Framework Convention on Climate Change is an amendment to the international treaty on climate change, assigning mandatory emission limitations for the reduction of greenhouse gas emissions to signatory nations.

Class Action Suits

On behalf of the Pension Fund, NBIM will join class action suits where deemed appropriate.

Lobbying and participation in international networks and organizations.

NBIM participates in international networks that promote good corporate governance. NBIM may provide input into consultative meetings to help ensure that government agencies, stock exchanges and other authorities develop and monitor regulations that protect ownership rights in accordance with NBIM's principles. Both NBIM has participated in the development of and signed the UNPRI, and are members of the ICGN⁵⁵.

Negative screening and exclusion

In addition to exercising its ownership rights, the Government Pension Fund Global's Ethical Guidelines set out measures for negative screening and the exclusion of companies from the Fund's investment universe.

The Norwegian Ministry of Finance is responsible for this and the government appointed a Council of Ethics to assist the Ministry with this task. The Council is an independent body with a mandate to assess and recommend whether companies should be excluded as a result of behaviour inconsistent with criteria set out in the Government Pension Fund Global's Ethical Guidelines. The Ministry makes final decisions on the exclusion of companies based on the Council's recommendations.

The Council meets once a month and discusses issues about companies on its own initiative or at the request of the Ministry of Finance. When requested to do so by the Ministry of Finance, the Council issues recommendations on whether an investment may constitute a violation of Norway's obligations under international law. The Council relies on a number of different sources in making its recommendations. These include non-governmental organizations (NGOs), government institutions, research institutes, commercial screening companies, companies and other international organisations. If the Council is considering recommending the exclusion of a company, the company in question receives the draft recommendation for comment. The Council regularly reviews whether the reasons for any exclusion still apply and may, if new information comes to light, recommend that the Ministry of Finance revoke a decision to exclude a company.

Once the Ministry has accepted a recommendation from the Council, it transmits that information to NBIM which is given a two month window to divest its holding in the company in question before the decision on exclusion is made public. Since the creation of the Council, the Government Pension Fund Global has divested its holdings in 18 companies. The list of excluded companies is publicly available.

Negative screening and exclusion policy

- Negative screening of companies that are directly or indirectly implicated in the production of weapons that through normal use may violate fundamental humanitarian principles. Companies may be indirectly implicated through entities they control.
- Exclusion of companies where an unacceptable risk contributing to the following is present:
- Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other child exploitation
- Serious violations of individuals' rights in situations of war or conflict
- Severe environmental damages
- Gross corruption
- Other particularly serious violations of fundamental ethical norms

⁵⁵ For more information on UNPRI, ICGN see Appendix

Example of exclusion and divestment: Wal-Mart

In June 2006, the Norwegian Ministry of Finance announced its divestment of Wal-Mart from the Government Pension Fund Global's portfolio citing serious and systematic violations of human rights and labour rights.

According to the Council of Ethics on 15 November 2005 "An extensive body of material indicates that Wal-Mart consistently and systematically employs minors in contravention of international rules, that working conditions at many of its suppliers are dangerous or health-hazardous, that workers are pressured into working overtime without compensation, that the company systematically discriminates against women in pay, that all attempts to unionise by the company's employees are stopped, that employees are in a number of cases unreasonably punished and locked in, along with a number of other circumstances...".

NBIM recommended shareowner engagement with Wal-Mart to try to encourage positive change. The Council, through NBIM, wrote to Wal-Mart on 14 September 2005 inviting them to comment on the allegations. Wal-Mart did not respond to this letter. While the Ministry strongly supports the use of shareowner dialogue to encourage companies to move on social and environmental problems, it considered that the approach would not be effective in this case. "In light of the Council's recommendation, the Ministry of Finance finds it unlikely that exercising the Fund's ownership rights vis-à-vis Wal-Mart will sufficiently reduce the risk of the Fund contributing to ethically unacceptable conduct, as this is defined in the Ethical Guidelines," stated Minister of Finance Kristin Halvorsen.

The Ministry of Finance therefore decided to act on the Council's recommendation to exclude Wal-Mart from the Fund based on the view that maintaining its investments in the company would incur an unacceptable risk of contributing to serious or systematic violations of human rights. After this decision was taken in March 2006, NBIM sold approximately \$416 million of Wal-Mart shares.

Government Pension Fund (Thailand)

1. Scheme Description

Country:	Thailand
Web:	http://www.gpf.or.th
Interviewee:	Chanchai Supasagee, Corporate Governance Director
Description:	One of the largest institutional investors in Thailand, the Government Pension Fund (GPF) was established in 1997 as a first step towards building a fully-funded pension system. The GPF is a defined contribution pension fund which supplements the defined benefit pay-as-you-go system that is designed for officials of the Royal Thai Government. The GPF operates as a privately managed entity, autonomous of the Ministry of Finance. Employees contribute 3% of their salary to the Fund and the Thai Government makes matching contributions.
Assets:	Approximately \$9billion invested in fixed income (68% Thai, 9% global), public equities (13% Thai, 1% global), property (3%) and alternative investments, as well as mainly Thai private equity (6%). The fund began to invest overseas in 2005 and is in the process of amending its policy to allow more exposure to equity and overseas investments. Assets are both internally and externally managed.
Membership:	1.1 million government officials including teachers, civil, military, judiciary, police and parliamentary officials.

2. Responsible Investment Rationale

In addition to maximizing financial returns for its beneficiaries, as one of Thailand's largest funds and a long-term investor, the GPF is expected to play a major role in the development of the Thai economy. One of the GPF's primary aim is therefore to introduce and promote good investment practices in Thailand. The GPF believes that the development of a sustainable pension system will allow for prudent fiscal management and the strengthening of the Thai financial markets. Its investment decisions have an impact not only on share prices but also on corporate and market practices.

The GPF understands that in order to ensure organizational credibility, member confidence and international respect, it needs to ensure that its own operations are governed by high standards of corporate governance. As such, the GPF regards corporate governance as a two-dimensional exercise: firstly for itself, as a trustee accountable to its members and secondly, as a responsible investor that takes account of invested companies' corporate governance practices.

The GPF believes that, through best practice corporate governance, invested companies will be better able to define an optimal structure for management duties and live up to their responsibilities to shareholders. The Fund views corporate governance as fundamental to long-term corporate growth and to the creation of healthy capital markets and hence the development of the Thai economy and society.

By being transparent about the corporate governance standards it sets itself, the companies in which it invests and the financial service providers that it hires, the GPF hopes to encourage other Thai and Asian institutional and private investors to follow suit and focus on the importance of good corporate governance.

The GPF's investment policy is based on a series of guidelines designed to ensure that the Fund's activities yield benefits to its members as well as to the Thai nation. In order to strengthen the mutual confidence between the GPF and society GPF's Board has decided to develop a set of CSR guidelines. The guidelines will cover a broad range of actions, including:

- Respect for the human rights of those impacted by the fund's activities.
- Support for the effective abolition of child labour and all forms of forced labour.
- The observation of standards of employment not less than those observed by comparable employers in the country.
- The establishment and maintenance of a system of environmental management appropriate to the fund.
- The promotion of higher levels of environmental awareness among business partners
- Abstention from any improper involvement in political activities.
- Encouraging business partners to apply CSR principles.
- The development and effective application of self-regulation
- The timely and regular disclosure of reliable and relevant information regarding the fund's activities, structure, financial situation and performance.

In line with its CSR Guidelines and the Pension Fund's commitment to the UNPRI⁵⁶, GPF will also incorporate companies' environmental and social performances within the realm of corporate governance.

3. Responsible Investment Strategy

Exclusion

The GPF invests in activities that yield benefits to its members as well as to the Thai nation. Selected investments must reflect this notion, and the Pension Fund screens investments to understand if any of the following non-beneficial activities are promoted:

- Pollution and environmental problems
- Breaches of intellectual property law
- Impediments to good morals and customs.
- Social problems and the endangerment of public security.
- Questionable accountability

An example of the GPF's exclusion policy is that it does not invest in the alcoholic beverages sector because alcohol consumption tends to be against the values of most Thai people and Fund wishes to avoid offending its beneficiaries when making investment decisions.

Corporate governance assessment

Six years ago, the GPF developed a corporate governance rating system inspired by the OECD Principles for Corporate Governance⁵⁷. The rating system applies to the GPF's internally managed active Thai equity portfolio. According to this system, the GPF rates Thai companies according to corporate governance criteria such as shareholder rights, board quality, accountability, disclosure and transparency. The target prices of

⁵⁶ See Appendix for more information

⁵⁷ See Appendix for more information

companies that are positively rated are increased by 10-20% whereas the target prices of companies that perform poorly are discounted. Although companies' ratings are not publicly available, the rating methodology is available on the GPF's website. Companies' ratings are reviewed annually.

For corporate bonds, the GPF also looks at the corporate governance quality of the issuer when considering an investment.

In addition to taking into account corporate governance standards for its bond and public equity portfolio, the GPF also assesses the corporate governance practices of its investment managers and custodial banks by looking at their ethical standards, fiduciary conduct, treatment of customers and segregation of duty and practice in the case of conflicts of interest.

Social and environmental issues

In line with its CSR Guidelines and following its decision to sign the UNPRI, the GPF has extended its focus beyond governance to environmental and social performance. It is currently in the process of drafting corporate, social and environmental governance guidelines for its Thai and global equity investments. The Guidelines will follow the OECD Guidelines for Multinational Corporations⁵⁸ and will cover issues such as environmental disclosure, bribery and consumer rights. The GPF's investment managers will be informed of the Fund's new ESG policy and will be asked to abide by it.

Voting

The GPF votes at the general meetings of Thai companies held in internally and externally managed portfolios in accordance with its corporate governance and voting guidelines. The Guidelines are inspired by US corporate governance best practice and the OECD Principles of Corporate Governance. They include issues such as the appointment of boards of directors and auditors, executive compensation, employee stock option plans, related party transactions, and capital structure. The Guidelines are publicly available on the GPF's website.

The GPF informs companies in advance by telephone when it votes against management recommendations, raising its concerns and listening to their explanations. The GPF publishes the number of votes cast and details of votes against management on its website and informs the general public about its voting decisions through the media. In 2005, the GPF voted at 84 company meetings, at five of which it voted against employee stock options plans that the Pension Fund deemed not to align employee interests with those of shareholders.

As it believes that voting is one of the few legal means at the disposal of shareholders to effectively protect their interests, the GPF encourages other investors to exercise their voting rights at AGMs.

Company and public policy engagement

The GPF tries to improve the corporate governance practices of the companies in which it invests by asking questions at companies' AGMs and requesting behavioural change when needed. The GPF also contributes to improving best practice at a market level by participating in seminars, brainstorming sessions and sitting on various working-group committees with the Thai financial authorities. Occasionally, the Pension Fund will also participate in shaping corporate governance best practice outside of Thailand.

Collaborative initiatives

From time to time, the GPF will work with other investors such as insurance companies to encourage improvements at the level of both individual companies and markets. The GPF believes that cooperation between investors can help to strengthen market standards.

The GPF was a member of the investor group that created the UNPRI and it signed up to the Principles when they were launched.

Metallrente

1. Scheme Description

Country:	Germany
Web:	http://www.metallrente.de
Interviewee:	Heribert Karch, Managing Director
Description:	MetallRente was created in 2001 by the German employers' association for the metalworking and electrical industry – Gesamtmetall – and the German Metalworkers' Union – IG Metall. It is the largest superannuation scheme in Germany and is best described as a distribution platform for three major corporate pension products – MetallDirektversicherung (direct insurance policies), the MetallPensionskasse and the MetallPensionsfonds. This case study focuses on the third investment vehicle, the voluntary defined contribution pension fund.
Assets:	More than \$780 million in aggregate in the three investment vehicles with an average annual growth of \$240 million. All assets are externally managed and invested in bonds and mainly European equities. The Pension Fund is the smallest investment vehicle in terms of assets with approximately \$33 million under management but has delivered the best financial performance to date.
Membership:	210,000 beneficiaries. Such has been the success of the fund that its membership has extended beyond workers in the metal and electrical industry to include those in the wood and synthetic materials, textiles and clothing and steel industries.

2. Responsible Investment Rationale

In 2001, Germany introduced transparency regulations for pension funds and required them to disclose whether or not they take SRI into consideration.

When employers and unions negotiated the creation of MetallRente in 2001, the parties discussed how to manage the assets pursuant to their legal obligations. Taking the new transparency regulations into consideration, the parties agreed to incorporate, where possible, an ethical investment component into their investment process. As a result, MetallRente requires all its equity fund managers to invest the Fund's assets according to SRI criteria.

MetallRente believes that investing in a sustainable manner makes sense for investors such as pension funds which need long-term sustainable growth to meet their future liabilities

3. Responsible Investment Strategy

SRI overlay exclusion strategy

MetallRente adopts an SRI approach to all its equity assets and has implemented an investment process that incorporates social, ethical and ecological criteria into stock selection. The strategy favoured by MetallRente is an SRI overlay and exclusion strategy whereby certain companies are excluded from portfolios due to poor

performance on social, ethycal or environmental (SEE) issues. As a public pension fund with thousands of beneficiaries, MetallRente gives special consideration to social and human rights issues, especially core labour standards.

As the fund is the result of a cooperation between employees and employers, as part of the agreement MetallRente has undertaken not to vote at the general meetings of, engage with or exert any influence on the companies in which it invests. This decision follows from the German system of co-determination whereby up to half of German company supervisory boards are composed of employee representatives. The founding parties agreed that additional intervention from the fund via engagement activities would result in an excessive influence by employees as their views were already represented at board level. It was also agreed between the employers and the employees not to publicise which companies were excluded from the portfolio due to poor social, ethical or environmental performance.

To help implement its SRI policy, MetallRente partners with Dresdner RCM Global Investors.

Dresdner RCM's SRI process originates from a partnership with the United Nations Association Trust, the charitable and educational arm of the UN. RCM approaches sustainability investing from a global perspective, believing that social, economical and environmental criteria derived from internationally agreed UN and International Labour Organisation (ILO) principles⁵⁹ provide the most comprehensive global benchmark against which to judge a company's environmental and social performance. The SRI process not only applies the core principles laid out by the UN and the ILO but it also requires a balance between economic, environmental and social management.

To create MetallRente's equity portfolio the investment manager first determine the target asset allocation. The manager then selects stocks based solely on fundamental research and financial performance, creating a short-list of possible investments. Companies are then rated according to their SEE performance on the basis of environmental issues (25%), societal issues (25%) and human rights issues (50%), which are of special interest to MetallRente. Dresdner uses these sustainability ratings to assign companies to one of the four categories described below.

Companies recommended for investment:

- Easy In: Corporate CSR leaders, exemplary behaviour with regards to the SEE criteria selected by MetallRente.
- Permissible: Have had problems with the management of SEE issues, but have taken action and put processes in place to resolve issues and improve behaviour.

Companies excluded from investment:

- Rejected: Difficulty managing SEE issues and no remedies taken or processes put in place to improve or resolve issues.
- Easy out: More than 5% of revenues or profits are derived from pornography, tobacco, alcohol or weapons.

Finally, RCM submits the draft exclusion list to MetallRente's Investment Committee for aproval. The list is discussed once a year, and both employees' and employers' representatives have to unanimously agree to the list. Unanimity guarantees both employer's and employee's agreement and support. The unanimity condition is seen as a main principle of MetallRente's social partnership and has been very much easier to achieve than expected. Once an agreement is reached, the confidential list is communicated to external investment managers. Investment managers have to divest from the negative stocks and replace them with permissible alternatives in order to avoid disrupting the investment process. Investment managers have to report on divestment and on their compliance with MetallRente's SRI policy.

⁵⁹ See Appendix for details of the ILO principles

Collaborative initiatives

MetallRente is an associate member of the EAI. Although the Fund has not signed the UNPRI⁶⁰ it endeavours to follow the principles and aspires to their aims.

60 See Appendix for information on the EAI and UNPRI

PGGM

1. Scheme Description

Country:	The Netherlands
Web:	http://www.pggm.nl
Interviewee:	Marcel Jeucken, Head of Responsible Investment
Description:	PGGM is the second largest pension fund in the Netherlands and one of the five largest in Europe and in the top-25 globally. It provides a compulsory, collective defined-benefit pension scheme to former and current employees in the healthcare and social work sectors based on the principle of solidarity. PGGM invests employer and employee contributions so that the investments generate optimum returns at acceptable levels of risk. PGGM's capital comprises pension contributions and investment returns.
Assets:	PGGM has total assets under management of around \$97 billion. The fund invests in equities, bonds, real estate, private equity and commodities on an international basis and uses both internal and external asset managers.
Membership:	PGGM is responsible for providing the pensions of over 2 million people in the healthcare and social work sectors.

2. Responsible Investment Rationale

PGGM defines responsible investment as any investment activity that takes account of the impact of ESG factors. The Pension Fund believes that its responsibility is to operate, over the long run, a superior pension scheme at a low cost.

When it signed the UNPRI in April 2006, PGGM reviewed its responsible investment policy and a new policy framework was adopted in November 2006 by its Board of Governors.

Within the new policy framework responsible investment is seen as a necessity that is first and foremost part of the Fund's fiduciary duty. As a pension fund, PGGM has a statutory responsibility to invest the assets entrusted to it in a manner that preserves the security, quality and liquidity of the fund as a whole. This requires it to assess and manage all foreseeable risk factors as effectively as possible. If ESG factors have a demonstrable impact on the financial performance of investments, they have to be analysed and taken into account in investment decisions.

PGGM views transparency and accountability as crucial aspects of a company's relationship with its stakeholders as they enable investors to make an informed judgment about the company's values and risk exposure. It takes the view that the exercise of shareholder rights by investors can generate higher investment results because companies that are aware that they are being closely monitored by investors will make greater efforts to perform well than those that are not subject to such scrutiny.

PGGM increasingly assesses investment opportunities not only in terms of the expected financial return, but also from a social and environmental perspective. The fund takes the view that superior shareholder value can only be achieved if the interests of all stakeholders in an organisation are taken into account. Businesses that acknowledge their responsibilities in relation to human rights, the environment and social policy are generally managed by people who are quick to recognise and respond to changes in society. Evidence indicates that the best-performing businesses are those that promote sustainable development, for example through environmental innovation.

As a universal investor, PGGM has an interest in the quality and continuity of the global investment universe and monitoring these parameters is therefore part of its fiduciary duty. At the same time, it sees responsible investment as an important expression of its identity.

3. Responsible Investment Strategy

PGGM's activities in the field of responsible investment until Q3 2006 comprised an active voting policy, engagement on corporate governance issues, as well as sustainable investment. From Q4 2006 onwards PGGM will implement a new responsible investment policy that integrates these activity areas as well as complementing them with new activities and a revised strategy.

Corporate governance and voting

PGGM votes at the shareholder meetings of domestic and international companies according to its Corporate Governance Code, the guidelines set out in the Tabaksblat code⁶¹ and the 2004 SCGOP Corporate Governance Handbook⁶². Moreover, the Fund has a high regard for the guidelines published by the OECD and the International ICGN⁶³. In the Netherlands, PGGM either attends AGMs in person or appoints another pension fund to cast votes on its behalf. Overseas, PGGM casts its votes remotely by means of electronic proxy voting. For certain portfolios, the exercise of voting rights may be delegated to an external portfolio manager, who will be instructed in such cases to comply with the PGGM Corporate Governance Code. The electronic voting system used by the external manager enables PGGM to monitor, and if necessary overrule, the external manager's voting behaviour. In special cases PGGM may decide to submit shareholder resolutions itself.

Information on how PGGM has exercised its voting rights is published at least four times a year on its website.

Exclusion strategy: exclusion of investments in countries or companies that are involved in human rights violations, or in arms production and trading

The exclusion strategy applies to all asset classes: stocks, bonds, private equity, hedge funds and property. PGGM will not invest directly in a country if it systematically violates fundamental human rights including freedom of association, freedom of speech and freedom of the press. In addition the Fund will not invest in countries upon which human rights related economic sanctions have been imposed by the international community, the UN, the International Labour Organization (ILO) or the EU. Dutch Sustainability Research (DSR) establishes a shortlist of embargoed countries for PGGM every year. The list is conveyed to internal and external asset managers who are required to refrain from investing in excluded countries' sovereign bonds or companies either listed on the identified countries' stock exchanges or receiving significant revenues from sales and trade in excluded countries. In addition, PGGM will not invest in companies that generate over half of their turnover from arms production or trading. The Pension Fund has taken the decision to divest from companies on this basis in the past.

Best-in-class strategy: companies rated as 'best-in-class' are over-weighted within specific portfolios

Companies are ranked on the basis of positive criteria relating to sustainability. Those rated as best-in-class are over-weighted in a pilot portfolio. PGGM has appointed two fund managers to manage pilot portfolios of sustainable European and US equities using a best-in-class strategy in terms of compliance with various sustainability-related criteria.

61 Dutch Corporate Governance Code, for more information see footnote 7

62 SCGOP is the Foundation for Corporate Governance Research for Pension Funds abbreviated in Dutch to SCGOP and renamed Eumedion on January 1st, 2006, see footnote 8 for more information on Eumedion

63 See Appendix for more information on OECD and ICGN

Engagement strategy: entering into active dialogue with companies with the aim of encouraging sustainable business practices.

Engagement, the third pillar underlying PGGM's sustainable investment policy, is deployed at different levels:

- Engagement with Dutch companies

Each year, Eumedion⁶⁴, a member-driven corporate governance platform of which PGGM is a founder and a member recommends a number of priority issues for pension fund members to rise with Dutch companies. The issues are communicated to company management and, where deemed appropriate, PGGM will engage with companies. Issues range from remuneration policies to the implementation of corporate governance codes.

- Engagement with European and US companies

UK asset manager F&C engages with companies on environmental and social issues on behalf of PGGM that is a client of its Responsible Engagement Overlay (REO) service. The engagement strategy is tailored to PGGM's needs. PGGM was involved in customizing F&C's product and periodically suggests engagement themes to F&C.

Collaboration with investors and others

- PGGM leverages its engagement activities through collaborative investor initiatives.
- PGGM is a founder of the EAI⁶⁵. It joined the initiative because it closely reflects its sustainable investment policy
- PGGM is a founding signatory to the UNPRI and has joined the Institutional Investors Group on Climate Change (IIGCC), Carbon Disclosure Project (CDP), the Institutional Investor Group on Myanmar and is an important member of Eumedion⁶⁶.
- In partnership with Triodos, PGGM launched and partly owns Dutch Sustainability Research (DSR), a sustainability research and proxy-voting provider that is part of the worldwide Sustainable Investment Research International (SiRi) Company and the European Corporate Governance Service (ECGS) Network.

Lobbying

PGGM takes part in consultations on corporate governance and ESG issues. For example, it participated in drafting the Dutch corporate governance Tabaksblat code. Moreover, through its membership of Eumedion, it also participates in collective initiatives aimed at improving corporate governance standards in the Netherlands.

New responsible investment policy

When it signed the UNPRI in April 2006, PGGM undertook a review of its investment policy and adopted a new responsible investment policy framework in November 2006. The new policy forms an integral part of its investment policy and provides a clear framework for planning, executing, evaluating and reporting on responsible investment activities. The policy will build on PGGM's existing sustainable and corporate governance policy described above. PGGM accepts that it will take several years to fully implement and expects responsible investment to be fully rolled out across all of its activities by 2009. The policy will be evaluated each year and new practical actions will be set out in the Pension Fund's annual plan.

Responsible investment principles:

- Responsible investment is an integral part of PGGM's policy and activities.

64 See footnote 63

65 For more information on the EAI see Appendix

66 See Appendix for more on all mentioned initiatives

- PGGM's fiduciary duty is paramount. Activities relating to responsible investment will not be undertaken at the expense of the fund's fiduciary duty. PGGM has a long-term fiduciary assignment.
- PGGM seeks to relate its investment policy to the fund's identity, and the norms and values of its participants.
- Responsible investment will develop over time. The implementation of responsible investment within PGGM will also be evolutionary.
- PGGM accepts that the results accruing from responsible investment are difficult to measure and allocate, but it shall attempt to do so.
- The focus is on activities that are expected to have the greatest impact.
- Cooperation with other players in the market will create synergy and increase impact. By working effectively with other pension funds, securities houses and asset managers, PGGM can deploy its resources more effectively and increase its influence
- PGGM will report transparently on its objectives, operations and results.

Responsible investment key policy areas:

- PGGM will actively practice its belief that financial return is compatible with social return.
- PGGM will seek to use sources of returns where ESG factors play an important role.
- As an active owner, PGGM will contribute to the quality and continuity of invested companies, to the benefit of the financial markets.
- The limits of its investment policy will be consistent with PGGM's identity and specific areas will be selected on the basis of that identity.
- PGGM will encourage its partners in the financial sector to adopt responsible investment principles.
- PGGM will render account for its objectives, activities and results in the field of responsible investment.

Activities

- Integration of responsible investment principles in strategy documents. This includes the review of all internal strategy documents to ensure they all reflect the responsible investment policy, as well as the further development of PGGM's monitoring framework.
- Integration of ESG into long-term equity portfolios. PGGM will develop an investment approach in which the assessment of the opportunities and risks presented by ESG factors will form an integral part of company analysis, this will be implemented across the Fund's Long-term Equity Portfolio in order to enhance alpha returns.

ESG themed investments

PGGM will select suitably themed investments that generate a social return. In this case social return is defined as the positive effect on ESG issues flowing from PGGM's responsible investment policy. Investment decisions or engagement activities may, for example, bring about a change in the behaviour of companies in which PGGM invests or the development of new and less environmentally harmful technologies. Social return investments can include investments in commercial microfinance, clean technologies or social housing initiatives.

Accordingly, PGGM will maintain its investment in Hermes' Focus Funds that aim to generate alpha by engaging with poorly performing companies on corporate governance, environmental and social issues. Additionally, in September 2006, PGGM announced it had taken a stake in the world's largest private sector carbon fund, Climate Change Capital (CCC)'s Carbon II fund. The fund will invest in projects in developing countries aiming to reduce greenhouse gas emissions.

Dialogue on corporate governance themes.

PGGM will enter into dialogue on a structural, systematic and visible basis, with market regulators and individual companies in which the Fund invests with the aim of raising corporate governance standards. A collaborative model will be developed with other pension funds to implement this policy beyond Europe.

Dialogue on environmental and social themes

PGGM will enter into a dialogue with market regulators and individual companies in which the Fund invests, with the aim of stimulating progress on environmental and social issues relating to PGGM's identity. PGGM will be an active participant in existing collaborative engagement initiatives such as IIGCC and Eumedion. It also plans to launch its own collaborative engagement initiative in 2007.

PGGM has selected the following specific issues for attention in 2007:

- Arms and defence industry
- Human rights
- Health care and pharmaceuticals
- Climate change

Note that PGGM has split corporate governance and environmental and social engagement activities to give them equal importance.

Informed voting policy

PGGM's role as an active investor will be supported by a well-informed voting policy. Specifically, PGGM intends to develop a differentiated voting policy, whereby priorities will be carefully set with reference to PGGM's best interests, impact and feasibility.

Specific exclusion policy

A specific exclusion policy will be developed, under which decisions will be made on the exclusion of certain companies on the basis of generic ethical standards. The policy will explicitly take account of the financial consequences of exclusion.

Dialogue on responsible investment with external investment managers

PGGM will seek to communicate to external investment managers the importance the Fund attaches to responsible investment and will assess their performance in this area. Initially this dialogue will take the form of specific ESG questions that will be included in the investment manager assessment and selection processes.

Encourage the development of responsible investment best practice in emerging markets

Responsible investment in emerging markets presents both challenges and opportunities. Accordingly, PGGM will organize a research initiative for emerging market investment managers with a view to formulating a practical investment strategy in which ESG issues play a distinct and significant role in the investment process.

External reporting

PGGM is developing a clear, integrated, external reporting process on its responsible investment activities. Existing reports will be combined and extended in 2007. PGGM is looking at developing a standalone responsible investment report which will include a comprehensive summary explaining its responsible investment activities to beneficiaries, peers, asset managers and stakeholders and which will show a clear link between PGGM's image and identity.

Challenges lying ahead

PGGM recognizes that it will face some substantive and practical issues while implementing its new responsible investment policy. Accordingly, it has tried to identify some of the most likely challenges it will encounter as well as the appropriate actions to counter them, some of which are listed below.

Issue: Investment staff is not equipped to make ethical choices in relation to the target return.

Action: The Investment Committee of the Board of Governors will formulate ethical standards and decide on the balance between ethical standards and target returns.

Issue: The contribution that responsible investment makes to returns has not been demonstrated.

Action: PGGM is playing a pioneering role in encouraging research, for example by developing a valuation model which explicitly incorporates ESG factors and engaging in dialogue with companies on CG and environmental and social themes.

Issue: The policy being pursued is inconsistent with the participants' expectations of responsible investment.

Action: The policy and action plan will be agreed with the PGGM's Participants Council – representative body for employers, employees, beneficiaries and unions. The participants' expectations will be addressed in the next Client Satisfaction Survey. PGGM will report clearly on its policies and activities.

Issue: The effect of responsible investment is difficult to measure.

Action: Valuation methods will be developed for factors such as dialogue on corporate governance and environmental and social themes.

Issue: The quality of analysis by external manager in relation to ESG is still unsatisfactory.

Action: PGGM shall encourage its financial partners to improve quality.

PREVI

1. Scheme Description

Country:	Brazil
Web site:	http://www.previ.com.br
Interviewee:	Jose Reinaldo Magalhães, Chief Investment Officer
Description:	PREVI is the employees' pension fund of the state-owned Banco do Brasil. Created 102 years ago, it is the largest pension fund in Latin America. The institution administers three different plans: a closed defined benefit plan, a defined contribution plan and an annuity benefit plan (invalidity, special or death annuity). PREVI controls the management process of its three benefit plans. This involves handling all aspects of liability management and investment management.
Assets:	Approximately \$50 billion split between equities (60%), fixed income (37%) and real estate (3%). The majority (97%) of PREVI's assets are managed internally, with the remainder managed externally. PREVI is only allowed to invest in Brazil
Membership:	Approximately 162,000 participants.

2. Responsible Investment Rationale

As a large investor with significant assets distributed across the Brazilian economy, PREVI is conscious of its investment footprint and potential to create value.

PREVI views companies as potential agents of change through which social and environmental issues can be positively addressed and contributions made to the development and sustainable growth of Brazil.

PREVI considers corporate governance to be a set of practices which are designed to optimise company performance; protect investors, employees, creditors and other interested parties; facilitate the company's access to the capital markets and offer it a framework that clearly defines corporate goals, the manner to achieve them and the oversight of performance, thus leading the company towards sustainable growth and socially responsible behaviour.

Through its code of corporate governance practices, PREVI tries to balance corporate and public interests, minimising the divergences between private and social returns, thus protecting all of those with an interest in companies. It is also part of PREVI's role to help fashion an investment climate in Brazil conducive to enhancing the confidence of overseas investors where respect of shareholder rights and strong corporate governance standards are the norm

Following its signing the UNPRI in 2006, PREVI is in the process of developing a socio-environmental responsibility policy that, alongside its corporate governance policy, will apply to all investment activities. PREVI uses the following rationale when considering environmental and social aspects of its investments:

- PREVI is a long-term investor and as such, must be concerned with the sustainability of its investments. Consistent returns over a long period are more important than short-term returns. Therefore, PREVI favours the establishment of an environment that is conducive to sustainable development.
- PREVI's main objective is to assure the financial security of its members at the end of their working life. PREVI believes that it is in the interest of its members to retire into a world that is characterized by a healthy environment and a healthy society.

- PREVI is the largest institutional investor in Brazil. Because of its size, positioning and history, its decisions significantly influence other pension funds, companies and the Brazilian financial market. PREVI recognizes its leadership role in the Brazilian economy and accepts the responsibility that comes with it.
- PREVI must be attuned to the concerns and demands of the society in which it operates. This society tends to be increasingly demanding in terms of the responsible performance it expects from organizations and companies.
- PREVI believes that ESG issues are important to determine the capacity of a company to generate and to preserve value over the long term. Inversely, companies that do not properly manage social and environmental issues are more exposed to risk and may potentially face value destroying consequences.
- PREVI believes that it is not only possible but also necessary to combine the pursuit of sound financial returns with social and environmental responsibility.
- PREVI believes that the adoption of a social and environmental policy for all its activities will not only help PREVI improve as an institution, but also achieve its objectives.
- PREVI's management is preoccupied with the positive sustainable development of the Brazilian society and as such, believes that proper consideration needs to be given to ESG issues.

3. Responsible Investment Strategy

PREVI's responsible investment strategy focuses mainly on corporate governance in publicly listed companies. As mentioned above it is in the process of reviewing its strategy in accordance with the UNPRI in order to broaden its focus to environmental and social issues.

Voting

PREVI votes shareholder resolutions in accordance with its corporate governance code. It views the code as a crucial instrument in guiding the relationships among agents operating in the companies in which it has interests. The code states the behaviours and practices that PREVI expects from invested companies. It includes the following main areas:

Transparency, disclosure and accountability

A company's corporate governance framework must promote the timely and accurate disclosure of financial and non-financial information to allow the interested parties to obtain a fully integrated understanding of a company's performance. Disclosure should be in accordance with the directives presented in the Global Reporting Initiative (GRI)⁶⁷, and Brazilian CSR groups Instituto Ethos de Empresas e Responsabilidade Social and Instituto Brasileiro de Análises Econômicas e Sociais.

In addition to financial statements, PREVI encourages companies to submit annually:

- A statement indicating adopted corporate governance practices.
- The policies applied to the management of insurance agreements and the result of systematic risk management including, but not limited to, equity, environmental, technological and regulatory risks.
- Performance indicators for corporate social responsibility.
- Policy on and the global amount of compensation paid to directors and executive officers, including variable compensation and stock option plans.
- Shareholder rights.

A company's corporate governance framework must guarantee the rights and interests of all shareholders and be aligned with the rights of clients, employees, suppliers, the government and community in general.

Corporate ethics and social responsibility

PREVI invests in profitable and socially responsible companies that, in addition to fulfilling their legal obligations, promote actions to the benefit of the communities in which they operate, offer their workers adequate safety, health and development conditions and care for environmental preservation and social and economic development.

PREVI expects the boards of invested companies to engage with stakeholders to establish corporate ethics and standards of behaviour that must be then approved and implemented

Engagement

PREVI will frequently assign a representative to attend the board meetings of companies in which it has significant holdings. This practice is driven by issues relating to performance, business strategy, returns and dividends, long-term value, corporate governance and, most recently, the management of ESG issues. PREVI will meet with board representatives to raise any concerns it might have with a company and discuss possible risks and areas for improvement. The representative's role is to transmit PREVI's view to the board and accordingly seek improvements in the company's behaviour. PREVI has a process in place to assess the performance of its board representatives, and currently employs 28 people to undertake this activity internally. Employees monitor and assess the performance of 177 representatives in 90 companies. All PREVI representatives meet on an annual basis, and a training process has been put in place to better align them with ESG issues.

Divestment

In instances where PREVI is concerned about the impact of a company's activities on society, it may take the decision to disassociate itself from that company, adopting a negative screening approach.

External investment manager requirements

PREVI is in the process of selecting five new external private equity investment managers. The consideration of ESG issues is a mandatory part of the RFP. PREVI will monitor its external investment managers on the basis of their implementation of a responsible investment strategy and it intends to participate in the investment decision-making process by sitting on its fund managers' investment committees.

Socio-environmental responsibility policy

PREVI is currently developing a socio-environmental responsibility policy that will apply to all its activities. The Pension Fund intends to implement the policy in 2007.

The policy will include the consideration of environmental and social issues in investment decision-making, including engagement and corporate governance activities. PREVI's goal is for ESG issues to be fully integrated into its stock selection process. In addition, the Pension Fund is developing methodologies and tools to measure the social and environment impact of its investments.

Furthermore, PREVI will review its investment policy in an attempt to further align it with each of the Principles of the UNPRI.

Changes to PREVI's approaches will be detailed the 8th annual edition of its Social Responsibility Report, due for launch in Q2 2007.

Collaborative initiatives

PREVI is a member of the following initiatives: The Brazilian Association for Pension Funds (Abrapp)⁶⁸, the Brazilian Institute for Corporate Governance (IBGC)⁶⁹, the ICGN, the CDP and the UNPRI⁷⁰.

PREVI has decided to use its position as a leading institutional investor in Brazil to promote responsible investment and the UNPRI. As such, it has asked Abrapp for institutional support to help publicize and encourage the adoption of the UNPRI. To this effect, PREVI has presented on the UNPRI at one of Abrapp's monthly meetings and is encouraging Brazilian pension funds to adopt Principles. In March 2007, a signing ceremony took place at BOVESPA, in São Paulo, where 14 Funds formally signed and adopted the UNPRI. Including PREVI, the 15 Brazilian pension funds that have endorsed the UNPRI represent 54% of total pension fund assets in the country.

68 For more information visit <http://www.abrapp.org.br/>

69 For more information go to <http://www.ibgc.org.br/>

70 See Appendix for more information on ICGN, CDP and PRI

TIAA-CREF

Teachers Insurance and Annuity Association, College Retirement Equities Fund

1. Scheme Description

Country:	USA
Web:	http://www.tiaa-cref.org
Interviewees:	Amy O'Brien, Director, Social Investing John Wilcox, Senior Vice President, Head of Corporate Governance Sonal Mahida, Senior Corporate Governance Analyst
Description:	TIAA-CREF is one of the world's largest financial services organizations, and leading provider of retirement savings products for the academic, research, medical and cultural fields, serving the long-term financial goals of those who serve others. The Carnegie Foundation formed TIAA-CREF in New York City in 1918 as the Teachers Insurance and Annuity Association of America after Andrew Carnegie, the legendary philanthropist, recognized that colleges needed to offer adequate pensions in order to attract talented teachers. The company's mission was to provide life insurance and a fully funded system of pensions to professors and employees of colleges and universities. Funding was provided by a combination of grants from the foundation and Carnegie Corporation of New York - including an initial gift of \$1 million - and ongoing contributions from participating institutions and individuals.
Assets:	More than \$406 billion, all internally managed in both actively managed and passively managed (indexed) funds. TIAA-CREF also offers funds from other companies. TIAA-CREF considers itself a long-term, universal investor.
Membership:	3.2 million retirement system participants and 15,000 participating institutions.

2. Responsible Investment Rationale

TIAA-CREF is a long-term investor and recognizes that the advancement, vitality and integrity of public corporations is good for investment returns as well as overall economic and social well-being. TIAA-CREF believes that sound corporate governance contributes significantly to long-term corporate performance and that companies that follow good corporate governance practices and are responsive to shareholder concerns are more likely to produce better returns. Accordingly, the Fund exercises shareholder rights to protect the long-term economic interests of its participants.

TIAA-CREF has addressed social issues as an active investor for nearly three decades. In the 1970s, it was one of the first institutional investors to engage in dialogue with corporate boards and management to encourage them to take positive steps for change on issues of South African apartheid and US automotive safety. Since then, it has maintained a deep commitment to responsible investment and corporate citizenship.

TIAA-CREF's investment decisions are guided solely by its fiduciary responsibility. The Fund's trustees and management are dedicated to securing the financial future of the nearly three million participants. At the same time, TIAA-CREF recognizes that it operates in a society not simply a marketplace and that its fiduciary

responsibility is necessarily linked to its social responsibility. TIAA-CREF therefore takes positions on social issues that it believes will positively impact shareholder value. The Fund encourages companies to adopt policies that promote corporate citizenship. In recent years, TIAA-CREF has voted to support greater disclosure of corporate activities in the areas of environmental practices, human rights, anti-discrimination policies and labour practices. With the help of third-party advisors and ongoing communication with participants, TIAA-CREF continues to monitor closely these and other issues that may affect investment value.

Moreover, TIAA-CREF recognizes that some of its participants have strong views on particular social issues. It believes that its participants should have an opportunity to invest in a fund that takes social considerations into account in making investment choices. Accordingly, in 1990, TIAA-CREF introduced the CREF Social Choice Account to provide an investment vehicle that gives special consideration to social criteria. The CREF Social Choice Account, with over 430,000 investors and over \$9 billion in assets is the largest, comprehensive socially screened fund.

3. Responsible Investment Strategy

Exercise of shareholder rights

TIAA-CREF established a Trustee Committee on Corporate Governance and Social Responsibility to oversee its corporate governance and social responsibility activities. The committee develops and recommends policy positions on selected corporate governance and social responsibility issues for consideration by the full board of trustees. The committee has the responsibility for establishing policies and guidelines for voting as well as the submission of shareholder resolutions and engagement with companies. A team of eight people work in the corporate governance department, executing the strategy put into place by the committee.

TIAA-CREF encourages boards of both US and international companies to exercise diligence in their consideration of environmental and social issues, analyse the strategic and economic questions they raise and disclose their environmental and social policies and practices. In particular, TIAA-CREF believes that the following concerns should be among the issues that companies address:

- Environment: the short-term and long-term impact of the company's operations and products on the local and global environment.
- Human Rights: the company's labour and human rights policies and practices and their applicability through the supply and distribution chains.
- Diversity: the company's efforts to promote equal employment opportunities and fair treatment for all segments of the populations it serves.
- Product Responsibility: the company's attention to the safety and potential impact of its products and services.
- Society: the company's diligence in reviewing all its activities to ensure they do not negatively affect the common good of the communities in which it operates.

Voting

TIAA-CREF votes at shareholder meetings whenever possible. The Fund is familiar with the voting procedures of every country in which it invests and has custodial arrangements that enable voting around the world. TIAA-CREF tries to identify, address and improve mechanisms in other markets that have impediments to effective foreign shareholder voting. A team of professionals is responsible for reviewing and voting each resolution in accordance with the guidelines established by the Trustee Committee on Corporate Governance and Social Responsibility. The guidelines are articulated in the TIAA-CREF Policy Statement on Corporate

Governance which sets out the Fund's views on good corporate governance and major proxy issues such as: election of directors, executive remuneration, shareholder rights, independent advisors, governance outside the US, social responsibility, shareholder proposals and company dialogue.

Aside from corporate governance issues, TIAA-CREF's approach to proxy voting is applied to a wide range of environmental and social issues. As such, TIAA-CREF will generally support reasonable shareholder resolution seeking:

- Disclosure of greenhouse gas emissions and the impact of climate change on a company's business activities.
- Disclosure or reports relating to a company's use of natural resources, the impact on its business of declining resources and its plans to improve energy efficiency or to develop renewable energy alternatives.
- Disclosure or reports relating to a company's initiatives to reduce any harmful community impacts or other hazards that result from its operations or activities.
- A review of a company's internal labour standards, the establishment of global labour standards or the adoption of codes of conduct relating to human rights.
- Disclosure or reports relating to the potential impact of HIV, AIDS, Avian Flu and other pandemics and global health risks on a company's operations and long-term growth.
- Disclosure or reports relating to a company's lobbying efforts and contributions to political parties or political action committees.
- Disclosure or reports relating to a company's non-discrimination policies and practices, or to implement such policies, including equal employment opportunity standards.
- Disclosure or reports relating to a company's workforce diversity.
- Disclosure or reports relating to the safety and impact of a company's products on the customers and communities it serves.
- Disclosure or reports relating to risks associated with tobacco use and efforts by a company to reduce youth exposure to tobacco products.

When analysing a voting proposal, TIAA-CREF professionals utilize various sources of information such as proxy voting advisory firms and corporate governance related publications. A report of votes is transmitted quarterly to the Fund's Board and an annual record of all votes cast during the year is available on the TIAA-CREF and on the SEC websites.

Engagement

TIAA-CREF's Policy Statement on Corporate Governance, updated in March 2007, serves as a basis for dialogue with boards of directors and senior managers, with the objective of improving corporate governance practices and increasing long-term shareholder value. To that effect, TIAA-CREF provides a copy of its Policy to all companies in which it invests.

TIAA-CREF also communicates directly with companies where it perceives there to be shortcomings in governance structure or policies. TIAA-CREF has a policy of "quiet diplomacy," and engages in confidential discussions with board members and senior executives to explain its concerns and gain insights into companies. Its aim is to resolve privately any differences it may have. TIAA-CREF's engagement style is non-adversarial and non-confrontational. It believes companies are more willing to listen and negotiate under those terms. TIAA-CREF will not publicise its engagement activities, even when it agrees to collaborative engagement campaigns with more aggressive investors.

Every year, TIAA-CREF selects one to two topics of importance for systematic engagement with companies in its portfolio. In cooperation with asset managers, it screens its entire portfolio for poor financial performers and companies with low standards of behaviour in particular areas. Once it has devised a list of target companies,

TIAA-CREF writes to the companies to raise its concerns and request clarification. If it is not reassured by the company's response, it will enter into discussions with the company's board and senior executives to agree on a timeframe for change and improvement. If discussions fail to persuade TIAA-CREF that management is responsive to shareholder interests, it may file shareholder proposals. TIAA-CREF is not in favour of divestment as this entails losing the possibility of influencing companies and is not felt to be appropriate for the Fund's many passive mandates.

Engagement activities have been mainly concentrated on corporate governance issues such as majority voting in board elections, takeover devices, executive remuneration and accounting rules for share options. In addition, TIAA-CREF is working to influence positive change by means of a dialogue with companies whose activities in Sudan suggest a cause for concern. Topics for engagement with foreign companies include various issues such as shareholder resolutions, voting caps or share blocking requirements. For example, in France, TIAA-CREF was able to get a resolution onto the agenda on the subject of voting right caps.

Lobbying

TIAA-CREF is an active participant in dialogue on corporate governance matters, meeting regularly with governments, shareholders, managers, regulators and exchange officials. The Fund promotes regulatory changes and focuses its efforts on increasing the accountability of the board. TIAA-CREF comments on the proposals of Congress, the SEC and other organizations that may affect its business, operations and interests. In addition, given its international investment portfolio and footprint, TIAA-CREF has played a significant role in efforts to improve global standards of corporate governance.

The Social Choice Account

TIAA-CREF believes that its participants should have an opportunity to invest in a fund that reflects their values and takes social considerations into account in making investment choices. Accordingly, in the 1990's, TIAA-CREF introduced the CREF Social Choice Account. This has grown into the world's largest socially screened investment fund, with just over \$9 billion in assets under management.

The Account is managed by a partnership between TIAA-CREF's internal investment managers and KLD Research Analytics in Boston that provides social research. For equities and corporate bonds, the Account invests only in companies that are suitable from a financial perspective and whose activities are consistent with the Account's social criteria. The equity portion of the Account attempts to track the return of the US stock market as represented by the Russell 3000 Index. It excludes companies with substantial revenues from alcohol, tobacco, gambling, weapons production or nuclear power. In addition, remaining companies are evaluated on their record in certain qualitative areas. A company's social performance is assessed in relation to its industry peers and the general social and environmental impact of the sector to which it belongs. The following are some of the principal social criteria that are currently considered when selecting companies:

- Product safety records, marketing practices,
- Employee relations, labour matters, workplace safety, employee benefit programs and meaningful participation in company profits either through share purchase or profit sharing plans;
- Human rights and relations with indigenous peoples, non-US labour relations and operations in countries where there are widespread and well-documented labour rights abuses;
- Corporate citizenship records, philanthropic activities, community relations and the impact of operations on communities;
- Corporate Governance, including executive compensation, tax disputes and accounting practices;
- Environmental performance, including a company's record with respect to fines or penalties, waste disposal, toxic emissions, efforts in waste reduction and emissions reduction, recycling and environmentally beneficial fuels, products and services;

- Diversity, including a company's record with respect to promotion of women and minorities, equal employment opportunities, family friendly employee benefits and contracts with women and minority suppliers.

Social & community investing

In 2006, TIAA-CREF surveyed its participants on Socially Responsible Investing. The survey results found that after financial returns social factors were the next most important to beneficiaries and that there was a significant interest in proactive social investing and a desire to promote human rights and economic development. In response, on July 1st, 2006, TIAA-CREF created a new Social and Community Investing Department within its asset management area, reporting directly to the Chief Investment Officer.

In addition to developing new products, the department oversees the investment process used for TIAA-CREF's socially screened fund. It seeks investment opportunities that are competitively priced and offer a broad social appeal. Commitments include:

- \$100 million to social housing investments, allocated to joint ventures or funds financing ownership housing for low-income civil servants.
- \$100 million Global Microfinance Investment Program (GMIP) to invest in selected microfinance institutions worldwide. The capital provided will assist expansion in Africa, Latin America and Eastern Europe, providing responsible banking services to many low income families and small businesses and enabling small scale entrepreneurs to build viable enterprises and create employment in low-income countries. TIAA-CREF subscribes to the view that microfinance can contribute to both financial and social returns.

Collaborative initiatives

In addition to participating to private collaborative engagement initiatives with other investors, TIAA-CREF as joined the following initiatives: Asian Corporate Governance Association (ACGA), Council of Institutional Investors (CII), European Corporate Governance Institute (ECGI), International Corporate Governance Network (ICGN), Carbon Disclosure Project (CDP), Boston College Center for Corporate Citizenship (BCCCC), Interfaith Center on Corporate Responsibility (ICCR) and Social Investment Forum⁷¹.

71 See Appendix for more information on all listed initiatives

About the UNEP FI Asset Management Working Group (AMWG)

The United Nations Environment Programme Finance Initiative (UNEP FI) is a global partnership between UNEP and the private financial sector. UNEP FI works closely with the 165 financial institutions that are signatories to the UNEP FI Statements, and a range of partner organisations, to develop and promote linkages between the environment, sustainability and financial performance.

Through regional activities, a comprehensive work programme, training programmes and research, UNEP FI carries out its mission to identify, promote, and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.

Further information visit: <http://www.unepfi.org/>

The asset management working group is an alliance of 14 investment managers from Brazil, France, Italy, Japan, North America, and the UK. Members collaborate to understand the ways that environmental, social and governance (ESG) issues can affect investment value, and the evolving techniques for their inclusion in portfolio investment decision-making and ownership practices.

Member institutions include:

ABN AMRO Banco Real Brasil

Acuity Investment Management

BNP Paribas Asset Management

Calvert Group

Clearbridge Advisors, SAI

Eurizon Capital

Groupama Asset Management

Hermes Pensions Management

Henderson Global Investors

HSBC Investments

Insight Investment Management

Mitsubishi UFJ Trust and Banking Corp

Morley Fund Management

RCM (UK) (Allianz Global Investors)

For further information, visit: http://www.unepfi.org/work_streams/investment/amwg

About the UKSIF Sustainable Pensions Project (SPP)

The UK Social Investment Forum (UKSIF) is the membership network for sustainable and responsible financial services. It promotes finance that supports sustainable economic development, enhances quality of life and safeguards the environment. It also seeks to ensure that individual and institutional investors can reflect their values in their investments.

The Forum was launched in 1991 to bring together the different strands of sustainable and responsible financial services within the UK and to act as a focus and voice for the industry. UKSIF's 200+ members and affiliates include pension funds, investment consultants, institutional and retail fund managers, investment banks, retail banks and building societies, financial advisers, socially responsible investment (SRI) research providers, trade unions, community development finance institutions, non-governmental organizations and interested individuals.

The UKSIF Sustainable Pensions Project was launched in 2006 to assist UK occupational pension funds to adopt more sustainable and responsible investment strategies. It seeks to encourage the pension schemes of companies which are leading the way on corporate responsibility (CR) practices and local government pension funds to consider environmental and social issues also in their pension fund investment decisions. It believes that this should help to protect and enhance long-term shareholder value and financial returns for the scheme beneficiaries.

The project is overseen by an independent Sustainable Pensions Advisory Board, whose membership includes:

Michael Deakin (ChaiMichael Deakin Consultancy Ltd

Tim Currell CFA	Hewitt Associates
Reg Hinkley	BP Pension Trustees Limited
Emma Hunt	Mercer Investment Consulting
Will Oulton	FTSE Group
Shaun McCarthy	Action Sustainability
Paul Moody	Morley Fund Management
Peter Montagnon	Association of British Insurers
Larry Stone	BT Pension Scheme
Mike Taylor	Local Authority Pension Fund Forum
Alex Van der Velden	FairPensions

All members serve in a personal capacity.

For further information, visit <http://www.uksif.org>

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UKSIF

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Appendix: Initiatives mentioned in the report

Asian Corporate Governance Association

The Asian Corporate Governance Association (ACGA) is an independent, non-profit membership organisation dedicated to working with investors, companies and regulators in the implementation of effective corporate governance practices throughout Asia. ACGA was founded in 1999 from a belief that corporate governance is fundamental to the long-term development of Asian economies and capital markets.

For more information see <http://www.acga-asia.org/>

Boston College Center for Corporate Citizenship

A membership based research organization, that works with global corporations to help them define, plan and operationalise their corporate citizenship. Their goal is to help business leverage its social, economic and human assets to ensure both its success and a more just and sustainable world.

For more information see <http://www.bcccc.net>

Business Leaders Initiative on Human Rights

The Business Leaders Initiative on Human Rights (BLIHR) is a programme to help lead and develop the corporate response to human rights. It is a business-led programme with 13 corporate members. Since the initiative was created in May 2003 it has worked to break down some of the barriers and uncertainties that have kept many responsible companies from realising their role in supporting universal human rights.

For more information see <http://www.blihr.org/>

Carbon Disclosure Project

The Carbon Disclosure Project (CDP) provides a secretariat for the world's largest institutional investor collaboration on the business implications of climate change. CDP represents an efficient process whereby many institutional investors collectively sign a single global request for disclosure of information on Greenhouse Gas Emissions. More than 1,000 large corporations report on their emissions through this web site. On 1st February 2007 this request was sent to over 2400 companies.

For more information see <http://www.cdproject.net/>

Council of Institutional Investors

The Council of Institutional Investors (CII) is the premier U.S. shareowner-rights organization. It is a not-for-profit association of 130 public, labour, and corporate pension funds with assets exceeding \$3 trillion. The Council works to educate members and the public about corporate governance, and to advocate for strong governance standards on issues ranging from executive compensation to the election of corporate directors.

Member funds are major long-term shareowners with a duty to protect the retirement assets of millions of American workers. CII believes that by pooling their resources, institutional investors can and should use their proxy power to hold the companies in which they invest accountable. Since it was founded in 1985, the Council has encouraged member funds to use their proxy votes, shareowner resolutions, pressure on regulators, discussions with companies, and, when necessary, litigation to protect plan assets.

For more information see <http://www.cii.org>

Enhanced Analytics Initiative

The Enhanced Analytics Initiative (EAI) is an international collaboration between asset owners and asset managers aimed at encouraging better investment research, in particular research that take account of the impact of extra-financial issues on long-term investment. EAI seeks to address the absence of quality, long-term research which considers material extra-financial issues. The Initiative incentives research providers to compile better and more detailed analysis of extra financial and intangible issues such as corporate governance, human capital management, value creation and destruction as a result of mergers and acquisitions or the risks presented by climate change within mainstream research.

For more information visit <http://www.enhancedanalytics.com>

Eurosif

The European Social Investment Forum is a pan-European group whose mission is to Address Sustainability through Financial Markets. Current member affiliates of Eurosif include pension funds, financial service providers, academic institutes, research associations and NGO's. The association is a not-for-profit entity that represents assets totalling over \$700 billion through its affiliate membership.

For more information visit <http://www.eurosif.org>

European Corporate Governance Institute

The ECGI is an international scientific non-profit association. We provide a forum for debate and dialogue between academics, legislators and practitioners, focusing on major corporate governance issues and thereby promoting best practice.

ECGI's primary role is to undertake, commission and disseminate research on corporate governance. Based upon impartial and objective research and the collective knowledge and wisdom of members, ECGI can advise on the formulation of corporate governance policy and development of best practice and undertake any other activity that will improve understanding and exercise of corporate governance.

For more information visit <http://www.ecgi.org>

Extractive Industries Transparency Initiative

The Extractive Industries Transparency Initiative (EITI) supports improved governance in resource-rich countries through the verification and full publication of company payments and government revenues from oil, gas, and mining. The Initiative works to build multi-stakeholder partnerships in developing countries in order to increase the accountability of governments.

For more information visit <http://www.eitransparency.org/>

Global Investors Governance Network

The Global Investors Governance Network (GIGN) is an informal network of international institutional investors who share a common interest in good corporate governance and improving long-term shareholder value.

Global Reporting Initiative

The Global Reporting Initiative (GRI) aims to make reporting on economic, environmental, and social performance – sustainability reporting – by all organizations as routine and comparable as financial reporting.

To achieve this, the GRI, continuously improves and builds capacity around the use of the GRI's Sustainability Reporting Framework, the core of which being the Sustainability Reporting Guidelines. Other components in the Reporting Framework are Sector Supplements and Protocols. This reporting guidance - in the form of principles and indicators - is provided as a free public good and is intended for voluntary use by organizations of all sizes, across all sectors, all around the world.

The GRI Reporting Framework is increasingly recognized as the de facto global standard in sustainability reporting. Nearly 1,000 organizations from over 60 countries, from business, civil society, labour, accounting, investors, academics, governments, and others, disclose their sustainability performance with reference to the GRI Guidelines.

The GRI was formed by the Coalition for Environmentally Responsible Economies (CERES) and UNEP in 1997. In 2002, at the World Summit on Sustainable Development, the GRI became a permanent institution, with headquarters in Amsterdam, the Netherlands. The GRI is a collaborating centre of UNEP and works in cooperation with UN Secretary-General Kofi Annan's Global Compact.

For more information see <http://www.globalreporting.org>

Global Sullivan Principles

A global framework for social responsibility for companies. Endorsers of the Global Sullivan Principles are expected to maintain a continuous commitment to each of the eight Principles, within the laws and customs of each country where they hold operations, including the implementation of internal policies, procedures, training and reporting structures.

The Principles

As a company which endorses the Global Sullivan Principles we will respect the law, and as a responsible member of society we will apply these Principles with integrity consistent with the legitimate role of business. We will develop and implement company policies, procedures, training and internal reporting structures to ensure commitment to these Principles throughout our organization. We believe the application of these Principles will achieve greater tolerance and better understanding among peoples, and advance the culture of peace.

Accordingly, we will:

Express our support for universal human rights and, particularly, those of our employees, the communities within which we operate and parties with whom we do business.

Promote equal opportunity for our employees at all levels of the company with respect to issues such as colour, race, gender, age, ethnicity or religious beliefs, and operate without unacceptable worker treatment such as the exploitation of children, physical punishment, female abuse, involuntary servitude or other forms of abuse.

Respect our employees' voluntary freedom of association.

Compensate our employees to enable them to meet at least their basic needs and provide the opportunity to improve their skill and capability in order to raise their social and economic opportunities.

Provide a safe and healthy workplace; protect human health and the environment; and promote sustainable development.

Promote fair competition including respect for intellectual and other property rights, and not offer, pay or accept bribes.

Work with governments and communities in which we do business to improve the quality of life in those communities — their educational, cultural, economic and social well-being — and seek to provide training and opportunities for workers from disadvantaged backgrounds.

Promote the application of these Principles by those with whom we do business.

For more information visit <http://www.globalsullivanprinciples.org>

Institutional Investors Group on Climate Change

The Institutional Investors Group on Climate Change (IIGCC) is a forum for collaboration between pension funds and other institutional investors on issues related to climate change.

IIGCC seeks to:

Promote better understanding of the implications of climate change amongst our members and other institutional investors.

Encourage companies and markets in which IIGCC members invest to address any material risks and opportunities to their businesses associated with climate change and a shift to a lower carbon economy.

For more information visit <http://www.iigcc.org/>

International Labour Organisation

Since 1919, the International Labour Organization (ILO) has maintained and developed a system of international labour standards aimed at promoting opportunities for women and men to obtain decent and productive work, in conditions of freedom, equity, security and dignity. In today's globalised economy, international labour standards are an essential component in the international framework for ensuring that the growth of the global economy provides benefits to all.

International Labour Organisation (ILO) Conventions and Recommendations cover a broad range of subjects concerning work, employment, social security, social policy and related human rights.

For more information visit <http://www.ilo.org>

Interfaith Center on Corporate Responsibility

For thirty-five years the Interfaith Center on Corporate Responsibility (ICCR) has been a leader of the corporate social responsibility movement. ICCR's membership is an association of 275 faith-based institutional investors, including national denominations, religious communities, pension funds, foundations, hospital corporations, economic development funds, asset management companies, colleges, and unions. ICCR and its members press companies to be socially and environmentally responsible. Each year ICCR-member religious institutional investors sponsor over 200 shareholder resolutions on major social and environmental issues.

For more information visit <http://www.iccr.org/>

International Corporate Governance Network

The International Corporate Governance Network (ICGN) is a not-for-profit association under with four primary purposes:

To provide an investor-led network for the exchange of views and information about corporate governance issues internationally;

To examine corporate governance principles and practices; and

To develop and encourage adherence to corporate governance standards and guidelines;

To generally promote good corporate governance.

Membership of ICGN is open to those who are committed to the development of good corporate governance. ICGN members are estimated to hold assets exceeding \$10 trillion

Policy-related committees include:

Accounting and Auditing Practices Committee

Corporate Governance Principles Review Committee

Cross Border Voting Practices Committee

Executive Remuneration Committee

Non-Financial Business Reporting Committee

Securities Lending Committee

Shareholder Responsibilities Committee

Shareholder Rights Committee

For more information see <http://www.icgn.org>

Investors Network on Climate Risk

The Investor Network on Climate Risk is a network of institutional investors and financial institutions dedicated to promoting better understanding of the financial risks and investment opportunities posed by climate change.

INCR was launched at the first Institutional Investor Summit on Climate Risk at the United Nations in November 2003, and now includes more than 50 institutional investors that collectively manage over \$3 trillion in assets. Members engage companies and policy makers through educational forums, shareholder resolutions, and other actions to ensure the long-term health of their investments.

For more information visit: <http://www.incr.com>

Institutional Investor Group on Myanmar (Burma)

In 2001, a group of financial institutions; Morley Fund Management, Co-operative Insurance Services, Ethos Investment Foundation, Friends Ivory & Sime, Henderson Global Investors, PGGM and the Universities Superannuation Scheme joined forces to launch 'Business involvement in Myanmar (Burma) - A statement from institutional investors.' Collectively the Group represented almost \$780 billion in funds under management. The statement outlines the concerns raised by the presence of a military dictatorship in Myanmar and highlights the risks to shareholders in investing in companies that have interests in the country. The Group suggests that companies operating in unstable political climates can be exposed to loss of shareholder confidence, negative press and publicity campaigns, safety risks, and corruption. In the case of Burma, there is also the possibility of a democratically elected government returning to power and penalising companies that supported the military regime.

The statement does not call for divestment, but urges companies to be aware of the risks and to establish effective policies and procedures for managing them. The statement calls upon those companies choosing to continue their business involvement there to adopt responsible business practices so as not to contribute to, or further perpetuate human rights abuses committed in the country.

Local Authority Pension Fund Forum

The Local Authority Pension Fund Forum (LAPFF) exists to promote the investment interests of UK local authority pension funds, and to maximise their influence as shareholders whilst promoting corporate social responsibility and high standards of corporate governance amongst the companies in which they invest.

Formed in 1990, the LAPFF Forum brings together a diverse range of local authority pension funds with combined assets of over \$130 billion.

For more information visit <http://www.lapffforum.org/>

MacBride Principles

The MacBride Principles--consisting of nine fair employment, affirmative action principles--are a corporate code of conduct for US companies doing business in Northern Ireland. Initiated proposed, and launched by the Irish National Caucus in November, 1984.

The Principles include:

Increasing the representation of individuals from under-represented religious groups in the work force including managerial, supervisory, administrative, clerical and technical jobs.

Adequate security for the protection of minority employees both at the work place and while travelling to and from work.

Banning of provocative religious or political emblems from the work place.

All job openings should be advertised publicly and special recruitment efforts made to attract applicants from under-represented religious groups. Layoff, recall and termination procedures should not in practice favour a particular religious group.

The abolition of job reservations, apprenticeship restrictions and differential employment criteria which discriminate on the basis of religion.

The development of training programs that will prepare substantial numbers of current minority employees for skilled jobs, including the expansion of existing programs and the creation of new programs to train, upgrade and improve the skills of minority employees.

The establishment of procedures to assess, identify and actively recruit minority employees with potential for further advancement.

The appointment of a senior management staff member to oversee the company's affirmative action efforts and the setting up of timetables to carry out affirmative action principles.

For more information visit <http://www.irishnationalcaucus.org>

OECD Guidelines for Corporate Governance

The Organisation for Economic Corporation and Development (OECD) Principles of Corporate Governance were endorsed by

OECD Ministers in 1999 and have since become an international benchmark for policy makers, investors, corporations and other stakeholders worldwide.

The Principles were last revised in 2004 and are intended to assist OECD and non-OECD governments in their efforts to evaluate and improve the legal, institutional and regulatory framework for corporate governance in their countries, and to provide guidance and suggestions for stock exchanges, investors, corporations, and other parties that have a role in the process of developing good corporate governance. The Principles focus on publicly traded companies, both financial and non-financial.

The Principles outline good corporate governance practices as:

The promotion of transparent and efficient markets.

The protection and facilitation of the exercise of shareholders' rights.

Equitable treatment of all shareholders, including minority and foreign shareholders.

The recognition of the rights of stakeholders established by law or through mutual agreements and active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

The timely and accurate disclosure of all material matters regarding corporations, including the financial situation, performance, ownership, and governance of companies.

Ensuring strategic guidance of the companies, the effective monitoring of management by company boards, and the board's accountability to the company and the shareholders.

For more information see <http://www.oecd.org>

OECD Guidelines for Multinational Enterprises

The OECD Guidelines for Multinational Enterprises are annexed to the OECD Declaration on International Investment and Multinational Enterprises. They are recommendations providing voluntary principles and standards for responsible business conduct for multinational enterprises operating in or from countries adhered to the Declaration. The Guidelines are legally non-binding. Originally the Declaration and the Guidelines were adopted by the OECD in 1976 and were last revised in 2000.

The Guidelines cover business ethics on:

Employment, human rights, environment, information disclosure, combating bribery, consumer interests, science and technology, competition, taxation

For more information see <http://www.oecd.org>

Social Investment Forum (SIF)

The (US) Social Investment Forum (SIF) is a US non-profit membership association dedicated to promoting the concept, practice and growth of socially responsible investing (SRI). Administered by Co-op America, SIF is comprised of investment practitioners and institutions from across all fields who seek to use their investment dollars to encourage positive social and environmental change in society.

For more information see <http://www.socialinvest.org/>

United Nations Principles for Responsible Investment

In early 2005 the United Nations Secretary-General invited a group of the world's largest institutional investors to join a process to develop the United Nations Principles for Responsible Investment (UNPRI). Individuals representing 20 institutional investors from 12 countries agreed to participate in the Investor Group. The Group accepted ownership of the Principles, and had the freedom to develop them as they saw fit. The Group was supported by a 70-person multi-stakeholder group of experts from the investment industry, intergovernmental and governmental organizations, civil society and academia.

The United Nations Principles for Responsible Investment were launched at the New York Stock Exchange in April 2006. The process was coordinated by the United Nations Environment Programme Finance Initiative (UNEP FI) and the UN Global Compact.

As of March 2007 the UNPRI had more than 171 asset owner and asset manager signatories, collectively representing more than \$8 trillion in assets.

The PRI reflects the core values of the group of large investors whose investment horizon is generally long, and whose portfolios are often highly diversified. However, the Principles are open to all institutional investors, investment managers and professional service partners to support.

The Principles

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

We will incorporate ESG issues into investment analysis and decision-making processes.

We will be active owners and incorporate ESG issues into our ownership policies and practices.

We will seek appropriate disclosure on ESG issues by the entities in which we invest.

We will promote acceptance and implementation of the Principles within the investment industry.

We will work together to enhance our effectiveness in implementing the Principles.

We will each report on our activities and progress towards implementing the Principles.

For more information visit: <http://www.unpri.org>

United Nations Global Compact Principles

The United Nations Global Compact is an initiative to encourage businesses worldwide to adopt sustainable and socially responsible policies, and to report on them. As of 2006, it includes more than 3,300 companies from all regions of the world who work to advance 10 universal principles.

The Principles concern:

Human Rights

Businesses should:

Principle 1: support and respect the protection of internationally proclaimed human rights; and

Principle 2: make sure that they are not complicit in human rights abuses.

Labour Standards

Businesses should uphold:

Principle 3: the freedom of association and the effective recognition of the right to collective bargaining;

Principle 4: the elimination of all forms of forced and compulsory labour;

Principle 5: the effective abolition of child labour; and

Principle 6: the elimination of discrimination in employment and occupation.

Environment

Businesses should:

Principle 7: support a precautionary approach to environmental challenges;

Principle 8: undertake initiatives to promote environmental responsibility; and

Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption

Principle 10: businesses should work against corruption in all its forms, including extortion and bribery.

For more information visit <http://www.unglobalcompact.org>

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