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# ESG & Fiduciary Duty of Asset Owners: An Illustration

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# Responsible Investment at AXA IM

## Our Mission

### Transform investing

“ We believe that RI can help deliver superior risk-adjusted returns for our clients over the long term. That is why we embed global ESG research across all asset classes and provide investors the opportunity to select the level of ESG integration that best fits their needs and objectives. It’s how we redefine investment solutions.”



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## Our Team

The RI team is composed of **10 professionals with 14 years average experience** in both ESG and traditional financial analysis.

**RI Search®**, our unique ESG platform, is used by the team to integrate fundamental and quantitative ESG research into investment decisions.

[www.axa-im.com/ri](http://www.axa-im.com/ri)

## Our Differentiation

### Pure RI funds

- › Thematic strategies driven by proprietary ESG research
- › Third-party label awarded to all our RI funds
- › Quality assurance through external audit

### ESG Embedded into AXA IM's mainstream funds

- › ESG scoring at portfolio and security level
- › Portfolio management with the integration of ESG research
- › Active stewardship through engagement and voting over all client shareholdings

### Tailored RI solutions

- › Customised mandates specific to client ESG factors
- › Engagement overlay services
- › Reporting and control, including carbon and ESG footprint analysis

RI Search® - our unique ESG research platform



# Agenda: A Practical Example of ESG & Fiduciary Duty

- **Context: Growing Pressure to Integrate ESG**
- **Strategic Discussion with Investment Committee**
- **Sample RI Framework**

## Context (1): Principles for Responsible Investment (PRI)

■ “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 recognize 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 :”

1. We will incorporate ESG issues into investment analysis and decision-making processes.
1. We will be active owners and incorporate ESG issues into our ownership policies and practices.
1. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
1. We will promote acceptance and implementation of the Principles within the investment industry.
1. We will work together to enhance our effectiveness in implementing the Principles.
1. We will each report on our activities and progress towards implementing the Principles

## Context (2): United Nations Global Compact Principles

Corporate Pension funds increasingly have to connect their investment policies with the commitments signed by their corporate parents

### *Global Compact Principles:*

- **Human rights**
  1. Support and respect the protection of internationally proclaimed human rights
  2. Make sure that they (businesses) are not complicit in human rights abuses
  
- **Labour**
  3. Uphold the freedom of association and the effective recognition of the right to collective bargaining
  4. Elimination of all forms of forced and compulsory labour
  5. Effective abolition of child labour
  6. Elimination of discrimination in respect of employment and occupation
  
- **Environment**
  7. Support a precautionary approach to environmental challenges
  8. Undertake initiatives to promote greater environmental responsibility
  9. Encourage the development and diffusion of environmentally friendly technologies
  
- **Anti-Corruption**
  10. Work against corruption in all its forms, including extortion and bribery

## Context (3): Pressure groups start to monitor the ESG quality of pension funds – *example from 2011 VBDO survey in Dutch market*

Criteria of VBDO Survey	VBDO Market Analysis	VBDO Comments about x pension fund
<b>RI policy (25%)</b> Content Volume Communication with Participants	<b>Pension funds should improve their policy by:</b>	
	1) Explaining how the principles of the UN Global Compact are dealt within the investment practice and by setting measurable targets to improve the adherence to these principles.	
	2) Adopting more asset classes in the responsible investment policy (60% have less than 75% of their portfolios in SRI)	
	3) Involving their participants in adapting and formulation of the RI policy	◀
<b>Implementation of the RI Policy (50%)</b> Public equity Corp/Gov bonds Real estate Alternatives	<b>Pension funds are encouraged to further implement the RI across all assets classes:</b>	
	1) Make the policy clearer and more systematic (positive selection as an instrument has become less prevalent among the researched pension funds)	
	2) Engagement in a systematic manner	
<b>Accountability (25%)</b> Investment policy Implementation	<b>Pension funds should disclose their RI policy and provide clarity on implementation of policy</b>	

# ESG Tool to Assess Priorities

- AXA IM utilises a diagnostic that helps to quickly better understand and focus on key ESG areas for investors
- The diagnostic helps to determine the sensitive areas that where the RI policy framework should be focused
- Example: **ESG** Framework

Governance	Questions	Scoring (1 = low / 10= high)
<b>Risk</b>	How important is it that <b>governance</b> risks are taken into account by top management?	
- Board	What is the importance of board independence? (ie: 30% rule)	
- Audit	What level of importance that there be an audit committee and that it be composed of independent directors?	
- Remuneration	Is it important that executive remuneration be disclosed and aligned with the long term performance of the company?	
- ESG specific	Is it important that Boards assess ESG criteria such as diversity? Is a specific ESG committee important?	
- Transparency	How important is it that disclosure be timely, clear, informative?	
<b>Responsibility</b>		
- Dialogue and Engagement	In case of lack transparency or poor results	

# ESG Framework Tool

Environment	Questions	Scoring (1 = low / 10= high)
<b>Risk</b>	How important is it that <b>environmental</b> risks are taken into account by top management?	
– Climate Change	Is climate mitigation of strategic importance?	
– Pollution	Is it important that there be a comprehensible policy for reducing the negative impact on air, ground waste and water?	
– Biodiversity	Is the impact of activities on eco-systems important and whether biodiversity is protected?	
– Product	Are eco-design objectives and R&D expenses dedicated to the life-cycle of importance?	
<b>Opportunity</b>	How important that environmental opportunities are promoted and within the assessment of business contribution?	
– Products env. friendly	Is it important for R&D to be dedicated to new technology, to solutions which are environmentally friendly?	
<b>Responsibility</b>	What level of communication on CR and environmental actions is important?	
– Transparency on:	Is there a comprehensible, credible, measurable policy?	
– Risks	Are the risks made clear to the investor?	
– Actions	How essential is it that companies communicate on the process and actions?	
– Results	How essential is it that the company disclose on the results and performance?	
– Dialogue and Engagement	In case of lack of information or poor results	

# ESG Framework Tool

Social	Questions	Scoring (1 = low / 10= high)
<b>Human Rights</b>	How important is it that HR risks are taken into account by the top management?	
– Country risks	How important that HR focus on these issues when developing business in countries where the respect of the HR is not a priority	
– Supply Chain	How important that companies take into account their HR principles with their contractors? is there a scoring? External audit?	
– Controversies/ Crisis management	What importance is the track record on this issue?	
<b>ILO</b>	How important is it that the risk to be in breach with ILO Conventions is taken into account by the top management?	
– Social dialogue/ relationship with Trade-union	Quality of the dialogue with the employees whatever the regulation and law?	
– Supply Chain	How important that companies take into account their ILO principles with their contractors? External audit?	
– Responsible restructuring/ discrimination	How important is the conduct around restructurings ? What about diversity and discrimination and whether it is respected?	
<b>Responsibility</b>		
– Dialogue and Engagement	In case of lack transparency or breach with ILO and HR principles	

# ESG Framework Tool: Actions for Implementation

Assets	Approach	Scoring (1 = low / 10= high)	Where	Scoring (1 = low / 10= high)
Equities	<ul style="list-style-type: none"> <li>- Screening</li> <li>- ESG integration</li> <li>- Engagement</li> <li>- Voting</li> </ul>		<ul style="list-style-type: none"> <li>- Domestic country</li> <li>- Europe</li> <li>- World ex emerging</li> <li>- World emerging included</li> </ul>	
Fixed Income	<ul style="list-style-type: none"> <li>- Screening</li> <li>- ESG integration</li> <li>- Engagement</li> </ul>		<ul style="list-style-type: none"> <li>- Domestic country</li> <li>- Europe</li> <li>- World ex emerging</li> <li>- World emerging included</li> </ul>	
–Corporate				
–Sovereign	<ul style="list-style-type: none"> <li>- Screening</li> <li>- ESG integration</li> </ul>		<ul style="list-style-type: none"> <li>- Domestic country</li> <li>- World ex emerging</li> <li>- World emerging included</li> </ul>	
Real Estate	<ul style="list-style-type: none"> <li>- ESG Integration</li> </ul>			
Private Equity	<ul style="list-style-type: none"> <li>- ESG Integration</li> </ul>			
Other Asset Class				

# Framework to Develop the ESG Policy that Respects Fiduciary Duty

## Principles: The Basics

1. **Beliefs**
  - Definition of RI
  - Why ESG factors are important
  - (Connection to CR Strategy of Corp)
2. **Scope**
  - Asset manager relations
  - Asset classes
  - Fiduciary relationship/oversight
3. **Governance of the ESG Policy**
  - Role of Investment Committee
  - Role of Pension fund board
  - Frequency of monitoring/review

## Approaches: The Specifics

1. **Exclusions**
  - Sensitive issues based on local and international context
2. **Engagement**
  - Appetite for engagement
  - How/issues
3. **Voting**
  - Best practice global standards
  - Specifics based on domestic market
4. **Manager monitoring**
  - KPIs
  - Progress/developments
  - Asset class priorities

# Ideas for ESG Framework (1)

## Pension Fund ESG Principles: The Basics

### 1. Beliefs

- Fund is a long term investor, duty to act in best interests of its beneficiaries
- ESG definition: integration of ESG considerations into investment processes and stewardship practices
- ESG factors have the potential to impact investment portfolios across companies, sectors, regions and asset classes
- Monitoring of ESG issues can help with financial returns
- Others

### 2. Scope

- The ESG policy covers xx activities as an asset owner
- Asset managers will be informed of ESG policy; monitoring will be implemented over time
- Guidelines specific to each asset class will be refined within the ESG policy over time

### 3. Governance of the ESG Policy

- Responsibility for the development, implementation and monitoring of the ESG policy resides with the Investment Committee
- The ESG policy should be monitored and reviewed on an annual basis
- Reporting on ESG activities should include asset manager implementation, engagement and voting activities

## Pension Fund ESG Approaches: **The Specifics**

### 1. Exclusions

- Some ESG issues are particularly sensitive and require considerations beyond ESG integration
- Fund excludes the worst cases of companies in violation of International Norms and monitors cases that are at risk through engagement

### 2. Engagement

- Fund's objective in addressing ESG factors is to use its influence as an asset owner to encourage ESG best practice
- Fund expects its fund managers to employ engagement of ESG factors as a monitoring and evaluation technique

### 3. Voting

- Fund uses global best practice standards to develop its view on the most important high-level governance issues based on ICGN and OECD Guidelines
- Key principles include:

Effective Boards	Shareholder Responsibilities
Accountability & Risk Management	Remuneration
Shareholder Rights	Transparency

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