Super Fund Responsible Investment Benchmark Report 2018

riaa Responsible Investment Association Australasia

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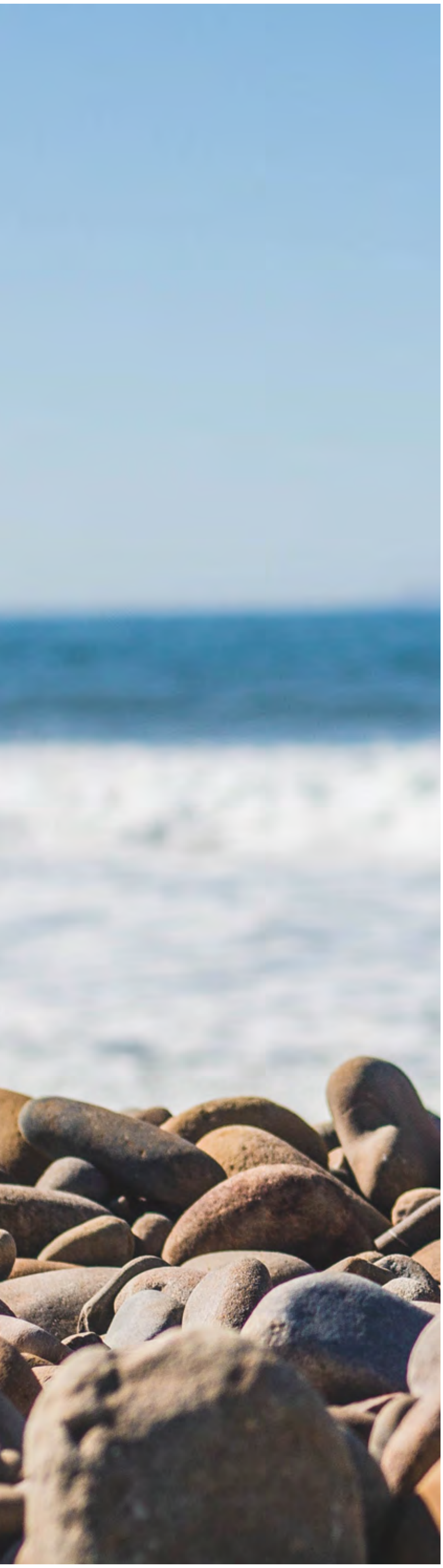

Contact us

RESPONSIBLE INVESTMENT ASSOCIATION AUSTRALASIA

Level 9, 387 George Street
Sydney, NSW 2000
Australia

+61 2 8228 8100
info@responsibleinvestment.org
responsibleinvestment.org

Executive Summary

CONTEXT AND BACKGROUND

Responsible investment (RI) continues its upward trajectory into the mainstream with just under half of all professionally managed assets in Australia now employing responsible investment strategies, as detailed in the Responsible Investment Association Australasia's (RIAA) *Responsible Investment Benchmark Report 2017*.

We are witnessing a strong take up by super funds and other large asset owners of a responsible approach to managing retirement savings largely driven by two factors:

- an ever-greater acceptance that environmental, social and corporate governance (ESG) factors are critical to consider as part of investment practice as they are increasingly impacting upon valuations and investment returns; and
- a growing interest by Australians in whether their retirement savings are being invested in a responsible manner, with recent surging consumer interest around issues and themes relating to social, environmental, sustainability and ethical issues.

Consumer research conducted for RIAA in 2017 revealed that an overwhelming nine in ten Australians expect their super or other investments to be invested responsibly and ethically. Seven in ten Australians would rather invest in a responsible super fund that considers the environmental, social and governance issues of the companies it invests in and maximises financial returns, rather than a super fund which considers only maximising financial returns. Notably, four in five Australians would consider moving their superannuation or other investments to another provider if their current fund engages in activities not consistent with their values.

These figures, coupled this with the ever-increasing size ($2.5 trillion) and influence of the Australian superannuation industry, highlight the critical nature of the data contained in this report.

If the superannuation industry is to realise its potential for fuelling a productive, prosperous, and healthy future for Australians, it needs to be one that embeds ESG considerations alongside traditional financial factors, avoids contributing to harmful activities and backs the building of tomorrow's businesses, industries and communities.

But to get there, Australian super funds need to commit to strong RI governance and accountability and invest only in companies and assets that genuinely deliver long-term, risk adjusted, performance outcomes. They also need to be courageous and skillful stewards, learning when and how to engage with companies and sectors in which they are invested.

At this point in time, when consumers are demonstrating heightened interest in the way their super is being invested, and when super funds are deepening and refining their responsible investment strategies, the second report in this research series begins to show an evolution of RI for Australia's largest super funds.

ABOUT THIS REPORT

The *Super Fund Responsible Investment Benchmark Report 2018* builds on research first published in November 2016 to map and inform asset owners of leading practice in responsible investment and to drive continual improvement in the development and implementation of responsible investment strategies.

Data in this report is sourced from a survey of the largest 48 superannuation funds in Australia, as well a handful of significant asset owners in our region including the two sovereign wealth funds in Australia and New Zealand. These 53 funds, in total, comprise an estimated $1.4 trillion in assets under management.

This report has undertaken analysis drawn from examining the practices of funds across a Five Pillar Framework covering Governance and Accountability; RI Commitment; RI Implementation; Measurement and Outcomes; as well as Transparency and Responsiveness. These pillars describe the elements of good governance for RI by super funds and used well, guide super funds on how to comprehensively and effectively implement RI strategies consistent with their investment beliefs and informed by their stakeholders.

WHERE HAVE WE ARRIVED AT IN 2018?

With the Super Fund Benchmark Report now in its second iteration, we can see a number of leading practice trends emerging:

Leading super funds are vigilant, skillful and courageous stewards

81% of the largest super funds now have embedded a formal commitment to RI (up from 70% in 2016), highlighting just how deeply the move to invest with a responsible approach has become integrated into Australian investment markets.

Along with this, the concept of universal ownership has landed in Australian super funds, and with this comes the ever-increasing sophistication of approaches to stewardship through activities such as corporate engagement and shareholder activities. This flexing of asset owners' muscles has been evident over 2017 and 2018 with super funds engaging around shareholder resolutions across diverse issues, such as improved climate risk and carbon disclosures and minimising the impact of gaming activities on livelihoods.

Leading super funds can be traditional and ethical

We are seeing an acceptance, and increasingly, an expectation, that super funds take a strong stance on activities within their portfolio companies that are harmful to humans, society and the environment – e.g. companies involved in tobacco production or cluster bomb manufacturing – whether those funds are self-declared ethical funds or not.

Leading super funds are aggressively transparent

Super funds – as the long-term investors in society and with beneficiaries spanning those in their first job through to those in retirement – are increasingly under pressure to not just tell, but show clients how money is being invested on their behalf. This means demonstrating financial performance, disclosing full portfolio holdings as well as the positive impact their investments are making, such as the fund's portfolio carbon footprint, contribution to affordable housing, greener buildings or renewable energy.

Leading super funds know what's important for their clients and offer choice

In 2016 the largest super funds offered 54 RI options collectively. In 2018, this figure has grown to 75, with 65% of these options obtaining RIAA certification. This certification helps super funds provide clients with a level of confidence over the quality of the investment process behind their RI strategies and commits funds to high levels of transparency – performance, holdings etc. – leading to more informed consumer choice.

Even for those funds that embed ESG across the entire fund and don't consider specific RI options as critical for meeting the RI expectations of their clientele, knowing their clients, by way of regular surveys for example, is becoming increasing important. Being in 'the know' about clients' interests and expectations is a common attribute of the stronger RI-performing super funds in this report.

KEY FINDINGS

1 More boards are becoming accountable for RI, and formal processes to measure and report performance are increasing

More boards are now accountable for RI policies

Accountability for overseeing policies and systems for managing ESG risks and opportunities is becoming more visible with 70% of funds having their full board, or board committees, overseeing ESG risks and opportunities, an increase of 14% from 2016.

RI commitments are growing as are the formal processes to support implementation

81% of super funds have some form of RI commitment in place, up from 70% in 2016. Almost all of these funds identify a formal process for reviewing this policy and 74% explicitly state RI commitments in a standalone policy or in their investment beliefs.

2 Climate change is entering the boardroom with climate risk making it onto board agendas and some portfolios being stress-tested, however commitments for portfolio decarbonisation are still in their infancy

Climate risk is making it onto board agendas

The trustees of 64% of super funds are actively considering ESG, including an explicit focus on climate risk. While this represents a strong proportion of this year's research universe, up to a third of trustee boards are still not actively considering climate risk in the face of increasing materiality.

Climate weighs into strategic asset allocation

10 funds identify climate change risk as a key consideration in strategic asset allocation. This takes the form of decision-making around asset allocation and weightings based on emissions intensity, as well as stress-testing and scenario planning.

Portfolio decarbonisation is on the radar, however few have translated this into targets

Only a handful of super funds have decarbonisation targets relating to their business and investment portfolios, with the vast majority of funds yet to actively respond to climate risks and opportunities through portfolio decarbonisation targets.

3 Internal resourcing to deliver on RI doubles

45% of super funds are employing one or more full-time employees with significant responsibility for RI. RI employee numbers have doubled since 2016 adding the in-house resourcing weight to support the RI commitments.

4 Stakeholders continue to be at the centre of investment beliefs but less than half the funds regularly monitor clients' satisfaction

74% of super funds use stakeholder input to inform their investment beliefs, while 32% engage in regular monitoring and at least annual surveys of client interests and satisfaction. This is up from 22% in 2016.

5 Fund-wide-exclusions are now applied to over 60% of super funds

Negative/exclusionary screening has traditionally been a RI strategy applied to specific responsible investment options, particularly ethical investment options; however, in 2018, this style of RI strategy is more inclusively applied across whole funds. 60% of super funds have a least one negative screen across the whole of the fund, up from 34% in 2016.

The most popular fund-wide exclusions are tobacco and armaments (including cluster munitions, nuclear weapons and other classifications under controversial weapons). Fossil fuels and human rights violations are the equal third most cited exclusionary screens.

6 Super funds seek quality data sources to enhance RI decision making

58% of super funds are able to identify how reliable ESG information is sought (up from 36% in 2016). External manager ESG information is the key source of ensuring robust ESG integration followed by use of accredited company ESG ratings/scorecards or databases, and sourcing comprehensive ESG research.

7 Most super funds rely on external managers to implement their RI responsibilities but very few consider external manager fund certifications and/or the qualifications of key personnel

70% of super funds, to some measure, identify external managers' responsibility for RI. 53% consider external investment managers as either wholly or largely responsible for the ESG information provided to the fund.

The RI expectations on external managers is stepping up, with 47% of super funds noting that minimum RI expectations across listed equities and/or fixed income are discussed with external managers. 45% require that external managers discuss how ESG factors have impacted specific investment decisions/ portfolio performance, and 40% require them to discuss their role in influencing investee company behaviour.

8 ***Super funds value and seek external verification of RI options***

Nearly half of super funds offer a total of 75 RI options (compared to 24 funds offering 54 options in 2016). 65% of these RI options have obtained RIAA Certification. This includes three super funds that have obtained whole-of-fund certification by RIAA as external verification of their responsible investment strategies and disclosures.

9 ***The setting of quantifiable performance targets to ground the implementation of RI policies remains in its infancy but attempts to measure RI performance is gaining traction***

25% of super funds have performance targets for their RI strategy. These targets vary from reducing carbon intensity and ensuring voting of a certain percentage of shares, to PRI reporting as a standard for measuring performance.

10 **Stewardship commitments are embedded in super funds however disclosure on activities remains low**

Company engagement is increasing, but nearly half do not disclose engagement activity or outcomes
43% of super funds indicate involvement in direct company engagement, an increase from 30% in 2016. 64% engage in collaborative company engagement, an increase from 52% in 2016. While some funds keep reliable data on engagements in the form of engagement reports, fewer still disclose their engagement activities.

Nearly all super funds have formal voting policies, but funds have different ambitions for influencing companies through voting
An impressive 94% of super funds have a formal voting policy, and all but one of these funds make their policy public. This compares with 58% in 2016.

Of the 29 funds providing responses to how they voted in 2017/18, only three funds voted with the company board and/or, proxy voting adviser on every occasion. In contrast, five funds voted independently of boards and proxy voting advisers on more than 10% of votes.

11 **With the rise in consumer expectations for RI and commitments to RI, more super funds are reporting on their RI activities**

Promotion is primarily via the super fund's website
49% of super funds integrate RI into overall promotion. 62% of funds report their website as the primary source for stakeholders seeking RI information.

Formal reporting of RI to stakeholders is increasing
62% of super funds disclose annually on their RI, up from 44% in 2016. Just over half of funds provide annual RI reporting through a standalone RI report, an integrated report, or as a section within their annual report.

LEADING RI SUPER FUNDS

With a view to articulating leading practice in RI for super funds, the funds are assessed across the Five Pillars of the Assessment Framework and alongside a scale – limited, basic, broad and comprehensive – indicating the quality and scope of disclosures.

13 of the 53 funds articulate and demonstrate comprehensive RI approaches across the Five Pillars. These 13 funds disclose RI data that scales as 'comprehensive' on at least 4 out of 5 of the pillars to gain the final overall rating of 'comprehensive' in 2018.

The 13 leading RI super funds are listed below.

FUND NAME	FUND CATEGORY
Australian Ethical	Retail
AustralianSuper	Industry
Cbus	Industry
Christian Super	Industry
First State Super	Public/non-regulated
Future Fund	Public Sector
HESTA	Industry
Local Government Super	Public/non-regulated
Mercer Superannuation (Australia)	Retail
NZ Super Fund	Public/non-regulated
Unisuper	Industry
VicSuper	Public/non-regulated
Vision Super	Public/non-regulated

Table of Contents

GLOSSARY

ACSI	Australian Council of Superannuation Investors
APRA	Australian Prudential Regulation Authority
CFA	Chartered Financial Analyst
ESG	Environment, Social and Governance
FSC	Financial Services Council
GRESB	Global Real Estate Sustainability Benchmark
GSIA	Global Sustainable Investment Alliance
IGCC	Investor Group on Climate Change
IMA	Investment Mandate Agreement
NABERS	National Australian Built Environment Rating System
PRI	Principles for Responsible Investment
RI	Responsible investment
RIAA	Responsible Investment Association Australasia
RSE	Registrable Superannuation Entity
SAA	Strategic Asset Allocation
SDGs	Sustainable Development Goals
TCFD	Task Force on Climate-related Financial Disclosures

ABOUT THIS REPORT

The Responsible Investment Association Australasia (RIAA) is the peak industry body representing responsible, ethical and impact investors across Australia and New Zealand. RIAA is an active network of over 220 members managing more than $5 trillion in assets, including superannuation funds, fund managers, consultants, researchers, brokers, impact investors, property managers, banks, community trusts and financial advisers.

RIAA's goal is to see more capital being invested more responsibly. RIAA works to shift more capital into sustainable assets and enterprises and shape responsible financial markets to underpin strong investment returns and a healthier economy, society and environment.

We are witnessing a strong take up by super funds and other large asset owners of a responsible approach to managing retirement savings. That is, more and more of our largest institutional investors are considering environmental, social, governance and ethical issues as a core part of their investment decision making, resulting in a community of asset owners that is ever more actively engaging, investing and divesting on the basis of issues that have sometimes been viewed as 'non-financial' issues.

This shift towards responsible investing (RI) by super funds and other asset owners has largely driven by two factors:

- an ever-greater acceptance that environmental, social and corporate governance (ESG) factors are critical to consider as part of investment practice as they are increasingly impacting upon valuations and investment returns;[1 2 3 4 5 6 7] and
- a growing interest from Australians in whether their retirement savings are being invested in a responsible manner, with recent surging consumer interest around issues and themes relating to social, environmental, sustainability and ethical issues[8].

As the peak industry body and within this context of an explosion of approaches to RI, RIAA sees the importance of providing more clarity and definition around the constituent parts of a comprehensive responsible investing approach by super funds.

It is important at the outset to note that in this report, we use the term super fund to describe 53 asset owner institutional investors. This universe of funds includes 48 Australian Prudential Regulation Authority (APRA) regulated super funds, but also includes some other large significant asset owners in our region, such as the two sovereign wealth funds in Australia and New Zealand, as well as some non-APRA regulated public funds. Within these 53 funds in total, there is a diverse range of funds that operate quite differently, in part due to their different beneficiaries. Despite this, and to simplify, in this report all are referred to as super funds.

The Super Fund RI Benchmark research is designed to help:

- *super funds* better understand the practical components of leading practice in responsible investment; and
- *consumers* understand the broad array of approaches and strategies in place, assisting them to make informed decisions regarding their superannuation.

This report builds on research first published in November 2016 and maps the broad array of RI approaches adopted by the Australian super fund industry as well as providing insights to changes in practice between July 2016 and June 2017. This project builds on longitudinal research aimed at constructively articulating the evolution of RI for Australia's largest super funds with the aim of highlighting the leading practices in the market and driving continual improvement.

The research methodology and assessment framework is modelled from similar initiatives globally, specifically the Dutch responsible investment pension fund survey issued annually since 2006 by the Dutch Sustainable Investment Organisation (VBDO).

For consistency across global definitions of responsible investment practice, the language and assessment approach has been reviewed and aligned in parts to other global frameworks including the PRI Reporting Framework 2017 Overview and Guidance and the Global Sustainable Investment Alliance set of responsible investing approach definitions.

An assessment framework has then been further refined in consultation with RIAA super fund members and through feedback from those participating in the first version of this report.

The result is RIAA's Framework for Assessing RI Practices of superannuation funds and asset owners (the Framework) which comprises five pillars.

1 RIAA (2017), Responsible Investment Benchmark Report Australia and New Zealand > https://responsibleinvestment.org/resources/benchmark-report/australia/2017-report/
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5 Statman, M., & Glushkov, D. (2016). Classifying and Measuring the Performance of Socially Responsible Mutual Funds. *Journal of Portfolio Management*, 42(2), 140-151 > http://www.cfapubs.org/doi/full/10.2469/dig.v46.n6.17
6 Gunnar, F., Busch, T., & Bassen, A. (2015) ESG and financial performance: aggregated evidence from more than 2000 empirical studies. *Journal of Sustainable Finance & Investment* 5.4: 210–233 > https://www.tandfonline.com/doi/full/10.1080/20430795.2015.1118917
7 NAB, (2017) *SRI in Australia,* Australian Centre for Financial Studies, June
8 See for example: RIAA (2017) *From Values to Riches: Charting consumer attitudes and demand for responsible investing in Australia*; November > https://responsibleinvestment.org/wp-content/uploads/2017/11/From-values-to-riches-Charting-consumer-attitudes-and-demand-for-responsible-investing-in-Australia-2017.pdf

The Framework's Five Pillars:

1 **Governance and Accountability**
Board-level buy-in to RI supported by formal accountability processes

2 **Responsible Investment Commitment**
Extent and breath of RI approach and coverage aligned with investment and RI beliefs

3 **Responsible Investment Implementation**
Widely used quality systems for delivering RI consistent with commitments and RI approaches

4 **Measurement and Outcomes**
Systems and metrics to track and manage RI performance internally and externally; ways for measuring success

5 **Transparency and Responsiveness**
Disclosures that build member confidence and broader stakeholder trust in the super fund's governance

The Five Pillars of the Framework describe the elements of good governance for RI by super funds and if used well, guide super funds on how to comprehensively and effectively implement RI strategies consistent with their investment beliefs and informed by their stakeholders. The Framework is a management system that helps articulate commitment to RI and the process that supports its implementation, through measurement, reporting and review.

Noting the many styles of RI – from an ethical approach to one more focused on stewardship responsibilities – the Framework is agnostic to the style of RI undertaken by a super fund and invites funds to describe their own way of doing RI, and to demonstrate how this is consistently put into action along the Five Pillars of good governance. This is key to the value of this Framework; it allows super funds to reflect the many different approaches appropriate to different styles of funds with different beneficiaries.

The data used in this project is derived from a combination of both primary and secondary research: firstly, desktop research was undertaken of each of the super funds' public information and then data was elicited via an information request to the 53 funds.

The purpose of seeking additional input from funds was to both verify fund data sourced by RIAA in the desk top research and to enhance RIAA's understanding of how a super fund implements RI throughout its fund. RIAA was especially keen to ensure that it collected information relating more to the quality of implementation of RI, by way of evidence of how it is integrated across the fund, rather than just proxies for this in published statements or formal policies.

In assessing each of the 53 funds on their RI disclosures against the Framework, a scaling system was adopted and applied. The scale (limited, basic, broad, comprehensive) describes the RI data scope and quality in disclosures for which RIAA considered all fund data for each aspect of the Five Pillars. The data was then categorised into these four points on the scale for each fund.

Funds whose RI data in their disclosures was scaled as 'comprehensive' on at least 4 out of the 5 pillars, received an overall scaling of 'comprehensive' in 2018. These funds are those that can comprehensively describe their approach to RI and demonstrate the implementation of this approach within their fund's operating context.

See the Appendices Report for the information requested of participants under each of the RI pillars and for a detailed overview of the project's methodology.

RIAA believes that by delivering this research, we can play an important role in furthering the capacity building of the industry based on highlighting leading practices, across not only super funds, but also the asset managers and asset consultants that support them. Through working to progress a deeper commitment and implementation of RI, we believe this will underpin the delivery of long term value for clients and a more sustainable financial system.

GLOBAL SUSTAINABLE INVESTMENT ALLIANCE RI APPROACH CLASSIFICATIONS

Responsible investing, also known as ethical investing or sustainable investing, describes a holistic approach to investing, where social, environmental, corporate governance and ethical issues are considered alongside financial performance, when making an investment.

To maintain a global standard of classification, this report is aligned with the seven strategies for responsible investment as detailed by the Global Sustainable Investment Alliance (GSIA). These strategies are:

1 **Negative/exclusionary screening:** the exclusion from a fund or portfolio of certain sectors, companies or practices based on specific ESG criteria;
2 **Positive/best-in-class screening:** investment in sectors, companies or projects selected for positive ESG performance relative to industry peers;
3 **Norms-based screening:** screening of investments against minimum standards of business practice based on international norms;
4 **Integration of ESG factors:** the systematic and explicit inclusion by investment managers of environmental, social and governance factors into traditional financial analysis;
5 **Sustainability themed investing:** investment in themes or assets specifically related to sustainability (for example clean energy, green technology or sustainable agriculture);
6 **Impact/community investing:** targeted investments, typically made in private markets, aimed at solving social or environmental problems, and including community investing, where capital is specifically directed to traditionally underserved individuals or communities, as well as financing that is provided to businesses with a clear social or environmental purpose; and
7 **Corporate engagement and shareholder action:** the use of shareholder power to influence corporate behaviour, including through direct corporate engagement (i.e. communicating with senior management and/or boards of companies), filing or co-filing shareholder proposals, and proxy voting that is guided by comprehensive ESG guidelines.

Source: Global Sustainable Investment Alliance (2016) Global Sustainable Investment Review
> http://www.gsi-alliance.org/

ACKNOWLEDGEMENTS

RIAA heartily appreciates the support of Amundi Asset Management which has allowed us to resource this research project.

We are very appreciative of the funds who responded to our request for information, contributed data and information and provided feedback to RIAA that provided the basis for this research and report.

This report has been researched and authored by a team at RIAA including Nicolette Boele and Simon O'Connor as well as the research team at CAER: Nithya Iyer, Phil Sloane Julia Leske and Erin Levey. The report was edited by Carly Hammond.

Research Universe and Data Assumptions

REPORTING BOUNDARY

This report covers the 2017 financial year being from 1 July 2016 to 30 June 2017[9]. There are some exceptions to this, including data sourced from participants' websites that may have occurred outside the period yet considered in this research. Furthermore, data sourced from PRI Transparency Reports published in 2017 primarily cover the financial year period ending on 30 June 2016. A small number of funds provided PRI Transport Report data for their 2017 data; most is of a qualitative nature.

Financial figures are in AUD.

SOURCES OF DATA

Much of the data included in this research comes from publicly available sources such as corporate websites (e.g. policies, guidelines and annual reports); Principles for Responsible Investment (PRI) Transparency Reports; RIAA's Responsible Investment Certification Assessment Program; and other publicly available information (including news and media). Data was also collected from super funds by way of a detailed information request issued between December 2017 and April 2018. This data was sought to help RIAA more deeply understand internal governance processes related to the implementation, measurement and outcomes of respective responsible investment strategies.

In the case, particularly for retail super funds, where the vast majority of investment services are provided by the investment management arm of the RSE, RIAA has accepted data directly from the underlying manager. Refer to Index of Funds on page 31.

9 except for a few funds such as NZ Super Fund, Statewide Super, UniSuper and First State Super that run their data for the 12 months to 31 December 2017

RESEARCH UNIVERSE

There are three main inputs to the research universe:

1. APRA's list of Australia's largest super funds as regulated and reported in February 2017 – 50 Registrable Superannuation Entity (RSEs) responsible for the largest total FUM;
2. select non-APRA regulated but sizable and significant asset owners in our market such as ESS Super and the Future Fund (with the latter having $117 billion AUM as at 1 July 2016); and
3. RIAA member super funds that fall outside the two categories above and that have opted in to this research (this includes New Zealand Super Fund, Australian Ethical and Christian Super).

Additionally, the following treatments were applied to guide the creation of the universe:

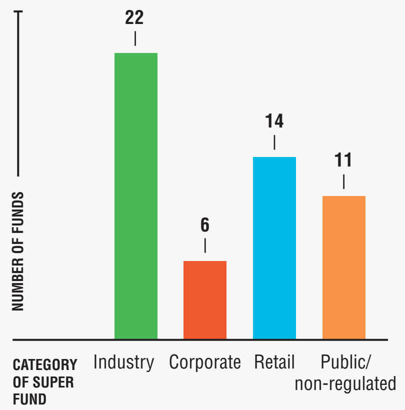
- If funds appeared in the largest 50 list, had the same RSE, and RIAA received notice from that RSE that the overall approach to RI was largely consistent across the separate funds, then RIAA rolled-up these funds and considered them as one single fund (e.g. Commonwealth Superannuation Corporation includes the Public Sector Superannuation Scheme & Accumulation Plan and the Military Superannuation & Benefits Fund No 1);
- If a RSE managed multiple funds in the largest 50 list but under materially different responsible investment strategies, then the funds have been treated as separate listings as part of this research (e.g. Colonial First State Investments Limited has two listings; one each for Colonial First State FirstChoice Superannuation Trust and one for Commonwealth Essential Super); and
- A number of mergers were noted (e.g. State Super Financial Services Australia Limited with FSS Trustee Corporation and Rio Tinto Staff Fund Pty Limited with Equipsuper Pty Ltd) but only the 'acquiring' RSE was included in the research universe.

29 out of 53 funds provided responses and/or additional information to this research process, being 55% of the sample, up from 40% in 2016. The 2018 research covers a total estimated $1.4 trillion in funds under management. The sample of regulated APRA funds included in this research manage 94% of all APRA-regulated super fund assets.

Guided by the categories used by APRA, RIAA placed research participants into four categories of funds: industry funds, retail funds, corporate funds and public/non-regulated funds. For the purposes of most analysis, the two sovereign funds – the Australian Government's Future Fund and NZ Super Fund – were classified as public/non-regulated. Figure 1 shows the split between these across the survey universe.

The Appendices Report includes the full project methodology.

FIGURE 1 **SURVEY PARTICIPATION BY SUPER FUND CATEGORY**



RECLASSIFICATION OF FUNDS FROM 2016

In 2016 VicSuper, Vision Super, and Local Government Super self-classified as industry funds, despite having an APRA classification as public/non-regulated funds. Accordingly, the 2016 data for industry funds included these funds' performance findings. For the purposes of being able to provide truly comparable data, year on year, RIAA has reclassified these three funds to be consistent with APRA's classifications for this 2018 report. ESS Super is not regulated by APRA but was also classified as an industry fund in 2016 and has been classified as a public/non-regulated fund in 2018.

Worth noting is the two sovereign wealth funds – New Zealand Super Fund (NZ Super Fund) and the Future Fund are classified as public/non-regulated funds and included in the figures for this fund category, except where explicitly excluded.

The Appendices Report includes the full list of funds by fund classification.

LANGUAGE SURROUNDING KEY STAKEHOLDERS

RIAA acknowledges that all super funds have a key stakeholder group – the beneficiaries. However, different funds have different labels for this group. Retail funds tend to have 'clients' or 'customers', corporate and industry funds have 'members' and public funds have 'members' or 'beneficiaries'. A sovereign wealth fund such as the Future Fund has 'future generations of Australians'. For simplicity, in this report the term 'clients' describes this key stakeholder group for all categories.

Findings

1 ACCOUNTABILITY AND GOVERNANCE

Policy and strategy based on sound understanding of client needs and expectations; and board-level buy-in to RI supported by formal accountability processes

Overall, super funds demonstrate a good level of accountability to stakeholders through both identifying ESG and/or RI as important in their fund's beliefs, and by identifying board-level accountability for RI performance. Accountability for overseeing policies and systems for managing ESG risks and opportunities has become more visible in this second year with more funds (37 out of 53; 70%) stating that the full board or board committees have oversight for ESG risks and opportunities, an increase of 14% from 2016.

WHAT IS ACCOUNTABILITY AND GOVERNANCE?

Accountability refers to the demonstration of the understanding of the stakeholders to whom the fund is accountable. Governance provides the structures (processes and delegations) necessary for the strategy to be effectively implemented. A key aspect of governance is the acknowledgement of the role of key stakeholders into the fund's RI strategy vision, mission or investment beliefs.

Clients tend to be a fund's key stakeholder group; but a fund may consider others as well (e.g. broader society, future generations, the environment, government/regulators etc.).

RESEARCH GOAL:
To assess the maturity of an organisation's accountability practices (stakeholder inclusivity and responsiveness; materiality issues) and whether the organisation has suitable governance structures in place to enable their RI strategy to be effectively delivered.

KEY ASPECTS USED TO ASSESS ACCOUNTABILITY AND GOVERNANCE:

- has commitment to RI in the overall fund strategy and internal structures in place to drive this;
- has and discloses appropriate responsibilities and accountabilities for RI;
- identifies, engages and considers stakeholders in the development and ongoing review of investment beliefs and RI strategy; and
- has incentives in place to perform duties consistent with the RI strategies and to the benefit of key stakeholders.

RI policies and accountability

This year's research finds that 43 out of 53 funds (81%) have some form of RI commitment in place – up 11% from 2016. Almost all (42) of these funds identify a formal process for the review of this policy.

For 74% of the universe (39 funds), RI commitments are explicitly stated in the investment beliefs or in a standalone policy – up from 70% in 2016.

There are clearer trends by fund category. For example, a greater proportion of industry funds lean towards explicitly stating RI commitments in a standalone policy (14 out of 22 industry funds or 64%). This is true of half of the corporate funds, with the other half explicitly stating RI commitments in their overall investment beliefs, rather than a standalone policy. Public/non-regulated funds also tend towards this form of integrating RI commitments into investment belief statements. Retail funds are the least likely to have an explicit commitment to RI stated through either of these forms, with 50% disclosing either a standalone policy, or an embedded statement in their investment beliefs, and the remainder either mentioning RI on their website (2) or not at all (5). This trend extends to board-level oversight as well.

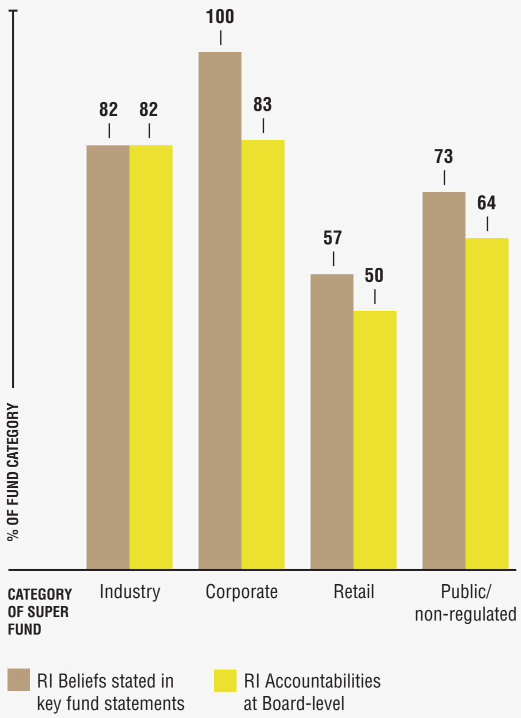
RI resourcing

Acknowledging that the resourcing of RI knowledge, skills and activities is not a direct proxy for capturing the maturity of RI in certain funds, RIAA sought to improve understanding about how different funds incubate, develop and embed RI practices.

In 2018, 24 out of 53 funds (45%) employ one or more full-time employees with significant responsibility for RI. Results suggest that approximately 48 RI employees are employed by these 24 funds. This is as compared with 24 FTE specialist staff employed across 12 funds in 2016; a 100% increase.

By fund category, just over one-third of industry (36%) and corporate funds (33%) disclose having FTE staff with significant RI responsibilities. This represents a 6% increase for industry funds since 2016, and a 16% increase for corporate funds, possibly suggesting that RI awareness is growing among this cohort. Interestingly, a higher percentage of retail funds, at 43%, have more FTE staff with RI responsibilities than any other fund category. This is perhaps due to the increasing focus on retail funds being able to provide a large variety of RI options for their diverse clientele. 78% of public/non-regulated funds disclose having at least 1.5 FTE staff for RI responsibilities, a significant increase from 29% of funds in 2016. This result is partially enhanced by the inclusion of the Future Fund – with two FTE RI staff – in the survey as well as the reclassification of Vision Super, VicSuper and Local Government Super as public (rather than industry) funds.

FIGURE 2 **RI COMMITMENT AND BOARD-LEVEL ACCOUNTABILITY**



SPOTLIGHT ON CLIMATE RISK

To help test the self-declared results on RI accountability, in 2018 we asked funds whether their trustees actively consider ESG and RI issues – including consideration of climate risk. A positive response was provided by 34 out of 53 funds (64%), with funds noting varying methods for doing so.

Two funds (**Australian Ethical** and **Christian Super**) state climate risk is discussed at each board meeting as part of their ethics report; a standing item on the board agenda. Some other funds (**Cbus**, **Maritime Super** and **First State Super**) systematically consider climate risk during dedicated Trustee sub-committee meetings (either quarterly or half-yearly alongside reporting on adherence to policy and implementation of ESG integration plans). **Cbus** reports that its Trustees undertake annual training on climate change and RI. Other funds may also undertake training, but the question was not specifically asked of funds. 29 out of 53 funds (55%) state climate risk is considered by the Trustee board at least annually (22) or on an ad hoc basis and as matters arise (7).

It is possible that some of the funds that did not respond to the request for further information do address climate risk at a board level.

However, it is of concern that the boards of nearly one-third of Australia's largest super funds may not consider climate risk at all. This could have both financial and regulatory implications, particularly in light of the recent explicit statements from APRA that it considers climate change to be a foreseeable, and often-times material, financial risk issue, and one that directors of institutional investors should consider with due care and diligence.

Four Funds – **First State Super**, **Macquarie**, **Mercer** and **BT Financial Group** (for **BT Funds Management** and **Westpac Securities** combined) – indicate they employ more than four FTE staff who spend over 50% of their time on RI (note all but First State Super are from the investment arm of the super funds for which they manage funds and would likely be well resourced with RI staff). A further 11 funds – **Australian Ethical, AustralianSuper, Cbus, Christian Super, Commonwealth Superannuation Corporation, HESTA, Future Fund, Local Government Super, NZ Super Fund, UniSuper** and **BT Financial Group** funds – **Westpac Securities** and **BT Funds Management** – have two or more staff members with more than 50% of their focus on RI.

Some funds indicate that responsibility for RI is integrated into each of the specialist asset class roles i.e. each asset class specialist is expected to know the RI issues for that asset class. Funds also indicate that they have RI committees for issue-specific investment decision-making, such as climate risk committees. These are consolidated at a board-level and across sub-committees, with key RI staff embedded into the process. For some funds, responsibility for RI management is now integrated across many people's roles so these figures may not fully capture the staff capacity for RI in the largest Australian super funds.

Despite the trend to insourcing specialist RI staff, many funds also note that RI is outsourced to asset consultants and investment managers which, in many cases, have dedicated RI teams. This is not represented in these statistics.

Each of the 15 funds included above, as well as an additional seven funds (22 out of 53 funds or 42%) indicate employing specialist RI staff with a focus on ESG integration, up from 24% in 2016.

In most cases, the role of specialist RI staff – as opposed to a staff member with some RI responsibility – is to participate in manager selection and review meetings, to influence manager decision and to coordinate company engagement and proxy voting. In some cases, these roles are also tasked with ensuring adherence to the fund's ethical charter or RI policy. For funds with direct investments, specialists are also tasked with finding appropriate thematic research and controversies research to complement the RI processes.

Stakeholders identified and engaged

Central to good governance is the explicit acknowledgement of key stakeholders and the issues that matter to them. Given the fiduciary duty of super funds, this engagement is even more critical for this industry than most others. We explored each fund's data for this, as well as the means to engage stakeholders on the formation of RI strategy on an on-going basis.

39 out of 53 funds (74%) report that stakeholder input informs investment beliefs – an increase of 6% from 2016. The preference across all fund categories was to have trustees as representatives of stakeholders, with nearly 50% across all fund category selecting this preference.

Interestingly, corporate funds demonstrate a lower propensity to rely on stakeholder input to inform beliefs, perhaps reflecting the assumption that corporate fund clients are more homogenous and so additional engagement is not required to fully understand needs and expectations.

17 out of 53 funds (32%) disclose that regular monitoring and annual (or more regular) surveys of client interests and satisfaction takes place. This is up from 11 out of 50 funds (22%) in 2016. Annual (or more regular) monitoring, particularly via surveys is most popular among retail funds (29%), although industry and public/non-regulated funds follow closely, both at 27%.

CASE STUDY 1

HESTA: GOVERNANCE AND ACCOUNTABILITY IN ACTION

HESTA's governance and accountability processes are developed around a sound and proactive understanding of member interests and a macro view of the role it plays as a long-term and universal investor. This understanding feeds through to the fund's core investment beliefs.

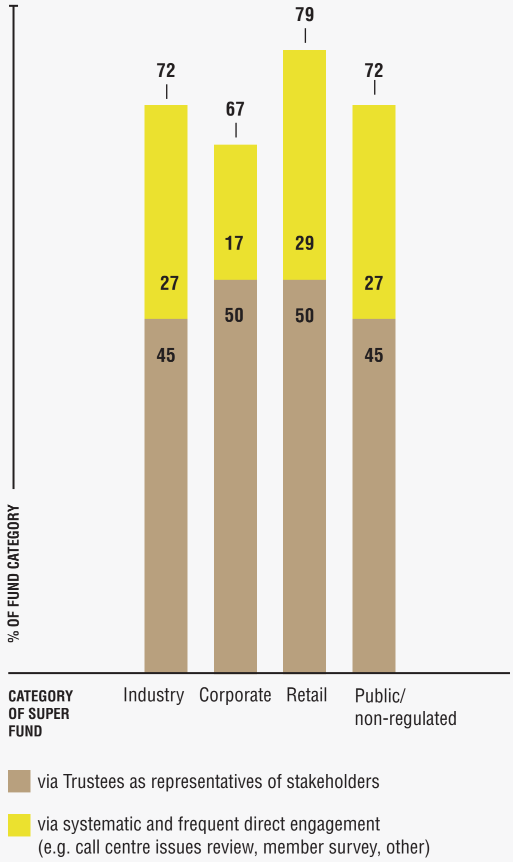
'HESTA is committed to creating better futures for our members. One of the ways we do this is through being a responsible investor. It is one of the Core Investment Beliefs that underpins how we look after members' assets… HESTA will be a responsible investor and recognises that members' best interests are served by supporting a healthy economy, environment and society.'

In seeking to understand member interests, HESTA regularly monitors issues raised at its call centres, as well as gauging member satisfaction levels and interests via a survey conducted at least annually. HESTA explores members attitudes to ESG issues in the annual satisfaction survey and, if required, also seeks feedback through its insight community.

HESTA's Responsible Investment Policy conveys that the incorporation of ESG issues into investment processes and decision making ultimately delivers against their members' interests.

'Incorporating ESG risks and opportunities contributes to a stronger economy, which is a prerequisite for delivering the best risk-adjusted returns for members; and it improves the overall retirement outcome for members, as their retirement outcome will not only be affected by the financial returns received, but by the state of the environment and the society into which they retire.'

FIGURE 3 **STAKEHOLDER INPUT BY SUPER FUND TYPE**



2 RESPONSIBLE INVESTMENT COMMITMENT

Extent and breath of RI approach and coverage aligned with investment and RI beliefs

The universal owner

The concept of the Universal Owner is gaining traction with the largest super funds. A number of funds (e.g. **First State Super, Local Government Super, NZ Super Fund** and **Future Fund**) explicitly discuss their respective roles in making investment decisions that deliver whole-of-economy, long-term outcomes for clients, broader society and the environment.

For many, the Universal Owner concept informs their preference of RI approach/es. **BT Financial Group** (for RSEs BT Funds Management and Westpac Securities), when considering ESG factors in the investment process, is not seeking to take a moral or ethical stance on ESG issues. Instead, its approach is motivated by financial goals, aiming to create long-term sustainable value and/or manage risk. As a Universal Owner, **BT Financial Group** applies stewardship principles and practices, (i.e. proxy voting and engagement) with the companies in which it invests, as fundamental in driving positive portfolio outcomes.

WHAT IS RI COMMITMENT?

RI Commitment relates to the fund's statements and activities around the promulgation of responsible investing both within the fund and within its relevant market.

Statements and activities include the making of public statements (by way of a policy and underlying guidelines) to formalise a fund's RI beliefs and informing stakeholders to what they are committed. RI beliefs ordinarily contained in policies include ESG themes, key approaches for implementation (e.g. ESG integration, positive/best-in-sector screening etc.) as well as a statement about its coverage (over certain asset classes, or the whole of the fund). Policies are formal documents endorsed by executives at the highest level of the fund.

RI Commitment also includes activities such as engaging and communicating with staff and clients on issues related to RI as well as industry activities such investor initiatives, memberships and involvement in industry associations.

RESEARCH GOAL:
To identify the nature and coverage of fund's RI commitments (e.g. RI beliefs as captured in policies, and through collaborations) aligned to investment beliefs, and the governance aspects supporting the fund's approaches to delivering on these commitments.

KEY ASPECTS USED TO ASSESS RI COMMITMENT:

- has publicly stated commitment to responsible investment endorsed at the highest level of the organisation (policy and/or guidelines). Elements of the policy that ensure that it can be put into action include ambitious but specific and achievable targets and KPIs;
- has full coverage of RI policy over the total portfolio and asset classes;
- has defined commitments to RI approaches, e.g. for active ownership and stewardship practices, a process for corporate engagement and voting are in place;
- has expressions of RI commitment such as through memberships of collaborative investor initiative/s; and
- if applicable, the fund offers consumers choice with the addition of responsible, sustainable or ethical investment options.

CASE STUDY 2

FUTURE FUND: IMPLICATIONS OF BEING A LONG-TERM INVESTOR

The Future Fund Act 2006 states that the Board must seek to maximise the return earned by the Fund over the long term.

'There are three main comparative advantages to being a long term investor:

i. the ability to take on greater levels of market risk, on the assumption that a long-term investor is able to tolerate the shorter-term losses that come with the greater market risk exposure. The greater market risk ought to (albeit in practice it need not necessarily) be rewarded with higher long-term returns;

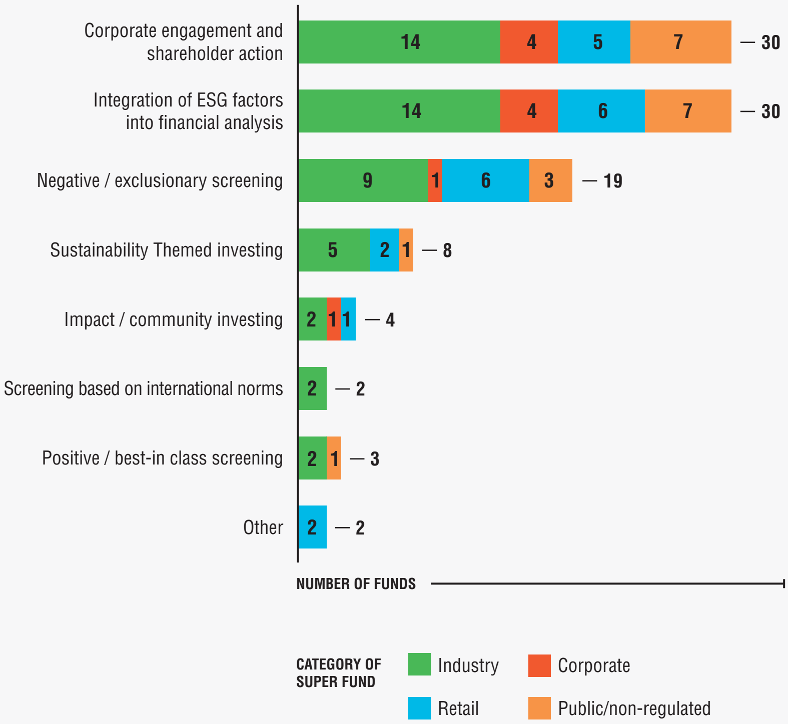
ii. the ability to accept capital being locked up in assets or structures that are impossible and/or costly to sell out of within a short period of time. Such investments ought to (albeit in practice they need not necessarily) attract a premium return to compensate for this loss of liquidity; and

iii. the ability to be counter-cyclical, patient and opportunistic. The investor can use its long-term nature to reduce risk when prospective returns are unattractive and wait for more compelling opportunities to buy (or sell). At times of market stress when other investors are selling, the long- term investor is able to step in and provide liquidity to the markets in return for outsized forward looking expected returns. This is often referred to as maintaining 'dry powder'.'

Funds that view themselves as Universal Owners also have strong stewardship commitments related to direct or collaborative company engagements, participating in collaborative industry-building and advocacy initiatives as well as commitments to vote on as many company resolutions as practicably possible.

For example, **Local Government Super** states its commitment to incorporating ESG issues into investment analysis and decision-making processes, being an active owner and voting on shareholder issues and participating in collective engagement, seeking disclosure on ESG issues by investment managers, promoting the acceptance and implementation of the PRI Six Principles in the investment industry and collaborating with other organisations to enhance effectiveness.

FIGURE 4 **RI APPROACHES ADOPTED BY SUPER FUNDS**



EXAMPLES OF FUND FOSSIL FUEL EXCLUSIONS WITH REVENUE THRESHOLDS

Christian Super's fossil fuel screen covers the following excluded fossil fuel activities (15% revenue tolerance):

- Mining thermal coal;
- Exploration and development of oil sands;
- Liquefaction of coal;
- Exploration and development of oil shale (not to be confused with shale oil or shale gas); and
- Brown coal (or lignite) fired power generation.

HESTA implements the following restrictions on new investments:

- Any unlisted company that derives more than 15% of revenue or net asset value from exploration, new or expanded production, or transportation of thermal coal;
- Any newly listed company, from listing onwards, that derives more than 15% of revenue or net asset value from exploration, or new or expanded production of thermal coal; and
- The provision of direct funding to any listed company, via rights issues or share placements, for any of these activities.

RI approaches and coverage

Funds' RI approaches, the assets covered by RI approaches, and other forms of committed action towards RI objectives were reviewed to identify the styles and gauge the extent of funds' commitment to RI.

Typically, funds link the RI approaches they implement to their RI beliefs and commitments e.g. a fund whose beliefs are around an ethical approach to investing would most likely include negative/exclusionary screening in its RI approach, whereas a fund whose primary beliefs are around taking a stewardship approach would most likely employ ESG integration, corporate engagement and voting as key RI approaches.

43 out of 53 funds (81%) adopt a RI approach across at least one asset class, with 17 out of these 43 funds implementing RI strategies across five or more asset classes.

Most popular RI approaches

ESG integration, as well as corporate engagement and shareholder action, are the most popular RI approaches adopted by funds and are noted by more than ten funds as a primary or secondary strategy in relation to equities (Australian and international), fixed income (all), private equity, property and infrastructure.

Negative/exclusionary screening and sustainability-themed investing are the third and fourth most popular choices respectively. 17 out of 53 funds (32%) are implementing negative screening as a strategy across at least one asset class – most frequently for equities (Australian and international), however also with regards to fixed income, private debt and private equity.

Sustainability-themed investing is most cited as a strategy across property (8 funds), with a few funds also noting its use in infrastructure, international equities and private equity.

Positive/Best-in-class screening is the least cited strategy, however is mentioned at least once across most asset classes as a secondary strategy.

Negative/exclusionary screening
Negative/exclusionary screening has traditionally been an RI strategy applied to responsible investment options, particularly ethical investment options; however, in 2018, this style of RI strategy is more inclusively applied across whole funds.

32 of 53 funds (60%) have a least one negative screen across the whole of the fund, up from 17 out of 50 funds (34%) in 2016 – a significant increase of 26%. 82% of public/non-regulated funds, 73% of industry funds and 67% of corporate funds are committed to a whole-of-fund screen. Retail funds are clearly demarcated from this group at only 21%.

Tobacco and armaments (including cluster munitions, nuclear weapons and other classifications under controversial weapons) are the most frequently cited whole-of-fund exclusion, implemented across 28 and 14 funds respectively (see Figure 5). The trend to divest from tobacco-producing companies can be credited to the recent successes of the activist group *Tobacco-free Portfolios*. It is likely that the KiwiSaver scandal of August 2016 has also had a bearing on Australian super funds explicitly divesting their portfolios from exposure to controversial weapons.

Fossil fuels and human rights violations are the equal third most cited exclusions, implemented across six funds each, however definitions and thresholds for these exclusions vary.

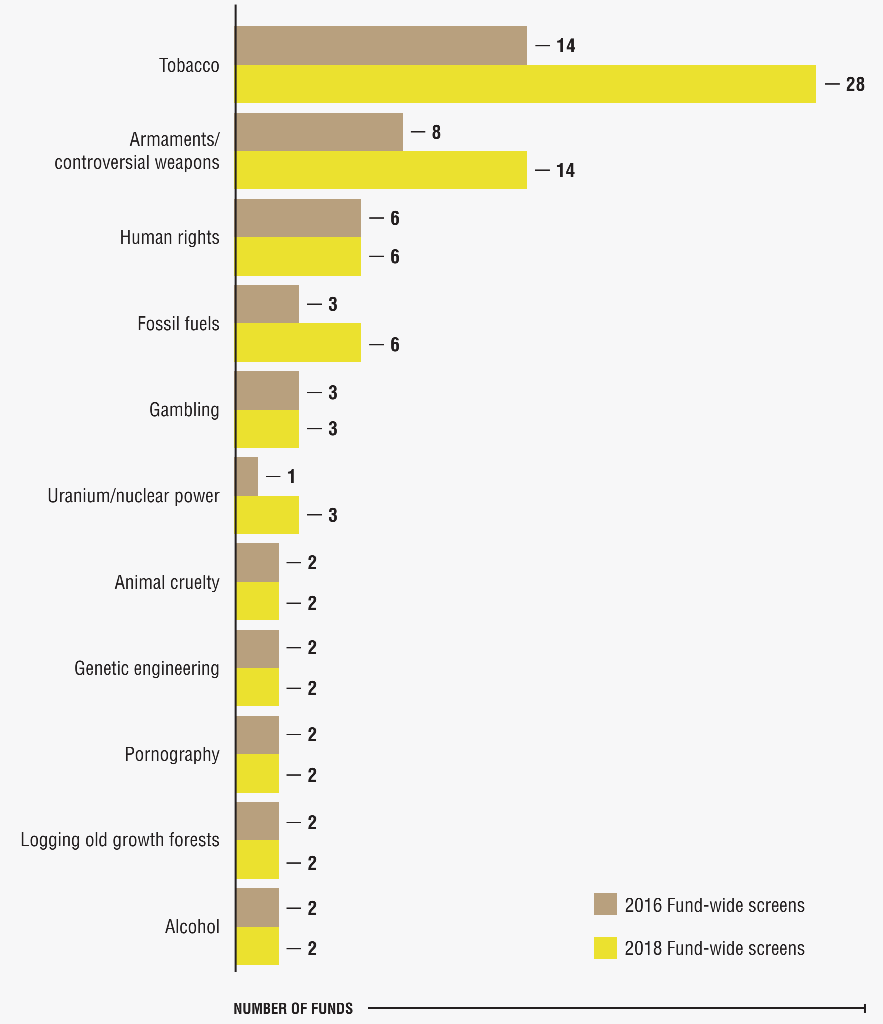
In the case of fossil fuels, for example, some funds cite that companies that derive a certain percentage of revenue from high carbon intensive activities are excluded (e.g. **Christian Super, HESTA**).

A second group wholly excluded high emissions industries such as brown coal or oil sands (e.g. **Australian Ethical** and **Local Government Super**).

A third group (not included in these figures) does not purposefully exclude companies involved in the production of fossil fuels, but takes a portfolio decarbonisation approach over time, which ultimately leads to the shorting of or complete removal of high carbon profile companies and assets. This style of RI approach would be classified as sustainability themed (see next section). **NZ Super Fund** and **Vision Super** are two funds part adopting this approach. **NZ Super Fund** has a 2020 target for reducing carbon emission intensity of the Fund by at least 20%, as well as reducing the fossil fuel reserves of the Fund by at least 40% (on a baseline of 30 June 2016). **Vision Super** has implemented a low carbon benchmark to its index equity portfolios which is essentially reducing exposure to companies with a high carbon risk factor. **Australian Ethical** also has a portfolio decarbonisation target.

Human rights exclusions vary widely in scope and in interpretation. In scope, they vary between funds screening for human rights abuses (screening for controversies), human rights violations (generally in relation to formal breaches against international convention), human rights concerns about a specific group of people (child rights) as well as specific geographic or issue-based concerns, such as **HESTA** divesting from operators of Australian offshore detention centres. In interpretation, they vary from labour rights to women's rights in relation to gender access to company board directorships. As such, the figures allocated to human rights in Figure 5 are a composite of several different approaches to this issue.

FIGURE 5 **FUND-WIDE RI SCREENS – 2016 VERSUS 2018**



Sustainability-themed and impact/community investing

14 out of 53 funds (26%) separately disclose allocations to impact and/or sustainability-themed investing as one part of a larger investment strategy used across specific asset classes.

Sustainability-themed investing:
12 out of 53 funds (22%) indicate the use of sustainability-themed investing, that is, investments that specifically target positive sustainability outcomes. Eight funds cite the use of this approach as the preferred secondary strategy in property (e.g. **Cbus** targeting greener, more energy efficient property portfolios), with a handful of funds also using the strategy across international equities, fixed income – government, private equity and infrastructure – to target highly sustainable companies and assets.

This speaks to a maturing understanding of the ways (such as the emergence of third-party certification over climate bonds, Green Star property etc.) in which sustainability-themed investing can be used across other real assets. An example of this is **UniSuper**'s allocation of $196 million to its green bond portfolio and **NZ Super Fund**'s sustainability themed investments in FSC or PEFC certified forestry[10].

Whilst not a dedicated allocation as such, other examples that include a focus on achieving targeted social and/or environmental impacts include **CareSuper** which invests 10% of its FUM to investments in green buildings, sustainable forestry and social infrastructure; and **Hostplus** with allocations to companies involved in a number of sustainability themed activities, such as biomedical processes and devices. **Hostplus** also boast a $550 million investment in venture capital funds who are in turn investing in 'water treatment systems, autonomous taxis and cars, and supporting clean energy funds to create new ways to produce, store, distribute, own and trade renewable energy'.

> ***We use responsible investment strategies because we believe*** *this will best achieve our objective of positive outcomes for both the planet and the financial interests of our clients.*
>
> ***Australian Ethical***

Impact/community investing:
Six funds (unchanged since 2016) report some targeted activity and investments in impact or community investing with a number of differing approaches and definitions. For example, two funds appear to define allocations to their community grants programs as community investing activity.

10 FSC, Forestry Stewardship Council; PEFC – Programme for the Endorsement of Forest Certification

CASE STUDY 3

FIRST STATE SUPER'S IMPACT PORTFOLIO

'The impact portfolio is a key element of First State Super's broader principle of Universal Ownership which aim to reconcile the Fund's fiduciary duty to members with our broader focus on sustainability. The impact portfolio seeks to positively screen a broader universe of opportunities which might otherwise be arbitrarily screened out due to size, classification or complexity for things that present strong positive socio-economic externalities. The portfolio currently has a strong focus on:

- *Job creation, innovation and small business growth*
- *Affordability and access to basic services, e.g. healthcare, retirement living*
- *The transition to a low carbon economy*
- *Regional development*
- *Other social initiatives*

All opportunities are assessed via a robust due diligence and decision-making process and must present a compelling reward for risk, although we proactively consider how to rescale, reshape or de-risk sub-optimal opportunities to strengthen the investment thesis. More generally the portfolio gives explicit consideration to the Sustainable Development Goals and our own ESG policies in assessing opportunities.'

HESTA reports a $30 million allocation via its Social Impact Investment Trust and a $35 million commitment to the Leapfrog Fund (II), which invests in high-growth companies that provide affordable healthcare and related services in Asia and Africa. HESTA's target focus for impact investment is in the health and community services sector, including increasing accessibility to health insurance and social and affordable housing. This strategy has a strong values-alignment with HESTA's core membership of healthcare workers.

In 2017 the **NZ Super Fund** made its first investment in a social impact bond, investing NZ$5.45 million (AU$5.07 million) in a bond issued by the NZ Government to finance a program seeking to reduce reoffending rates amongst a cohort of youth offenders by 15% over a 6-year period.

Australian Ethical's investments in social impact bonds, green bonds and private equity impact funds have intentionally targeted positive social and environmental outcomes including home and commercial renewable energy generation, energy usage reduction, low emissions transport through electric vehicle sharing and energy efficient buildings.

Alongside its targeted impact investments, **Christian Super** aims to achieve additional impact by providing the financially excluded (i.e. rural, women, students, emerging consumers) with the financial tools necessary to achieve their goals.

Use of targets in RI commitments

RIAA asked funds whether their investment and/or RI policy includes specific RI targets such as the percentage of AUM to be fully ESG integrated, portfolio carbon targets (such as meeting <350ppm) or voting targets. The box on page 16 contains examples by funds. 12 out of 53 funds (22%) define specific targets in their RI policy (31% of those with RI commitments). While this is a proportionally low figure, it marks an increase of five funds since the 2016 report, highlighting a growing trend whereby RI commitments are starting to be measured and tracked in some way.

Six funds (**Future Fund, CareSuper, Local Government Super, UniSuper, Vision Super** and **First State Super**) provide a commitment to voting on 100% or the majority of shareholdings, with one fund (**Australian Ethical**) specifically outlining corporate engagement and advocacy targets.

The second most frequently cited target, indicated by five funds (**Australian Ethical, Mercer, NZ Super, Vision Super** and **First State Super**), focuses on climate change-related targets and includes reducing the emissions intensities of portfolios, measuring carbon footprints of portfolios, and/or having targets regarding investments in renewable energy. This is consistent with 2016 findings.

Another popular target is to commit to vote on all company resolutions, where practicably possible to do so (**CareSuper**, **Future Fund**, **First State Super**, **Local Government Super**, **UniSuper**).

HESTA has a target on engaging 100% of its fund managers via survey on how their underlying investments fare against targets of board (gender) diversity (being at least 30% female).

Another fund (**Mercer**) notes a target to ensure investment managers achieve a certain minimum standard of ESG rating.

Otherwise, targets tend to be more generalised objectives regarding adhering to a fund's overarching beliefs and investment philosophy, rather than identifying numerical, technical or threshold-related performance aims of the fund. It should, however, be noted that a handful of these funds disclose that more specific targets, including thresholds across asset classes – are set internally for RI outcomes, but that these are not publicly disclosed.

WHY DO RI TARGETS MATTER?

Setting RI targets has a flow-on effect to good RI governance and stronger management of business risks and opportunities.

Benefits of targets include:

- **Targets compel fund personnel at the highest level to set a level of ambition for the fund** Building on an understanding of the standards and expectations of beneficiaries and clients, the fund can determine how it is best positioned in the market and how this aligns with the purpose of the fund;
- **Targets require senior management to consider how progress against targets may be measured** Identified outcomes or proxies for outcomes provides evidence for aspects of the policy being operationalised by the relevant personnel;
- **Targets enable a clear articulation of successful behaviours** With progress indicators identified, as well as the level of ambition, trustees and/or senior management are able to clearly articulate to the rest of the fund the shape and form of successful behaviours. Should a fund use incentives schemes to reward personnel for achieving performance outcomes, then this is also more effectively done when targets are set for RI;
- **Targets provide a basis for credible communication** Better measurement of progress enables clearer, more credible communication to key stakeholders, including in annual or integrated reporting and marketing materials; and
- **Targets improve overall business outcomes** Targets help decision-makers at all levels of the fund to see whether a particularly operational strategy is working or not; ultimately this information should help improve business outcomes over all.

EXAMPLES OF SPECIFIC AND QUANTIFIABLE RI-RELATED TARGETS

'We target an ESG3 rating or better across managers.'
Mercer Super Trust

'We have a target of zero portfolio emissions by 2050. Our annual Advocacy and Engagement plan includes target outcomes for our advocacy and engagement priorities.'
Australian Ethical

'We have a number of targets for our internally managed property portfolio covering energy and water efficiency, waste and renewable electricity consumption.'
Local Government Super

'By 2020 to reduce the carbon emission intensity of the Fund by at least 20%; and reduce the fossil fuel reserves of the Fund by at least 40% (baseline is 30 June 2016).'
NZ Super Fund

'We are committed to:

- disclosing the carbon emissions footprint of our share portfolios. We will move to other asset classes in the coming years.
- making our portfolio carbon neutral by 2050; this will include divesting from companies involved in mining/extraction, transportation and consumption of coal, oil and gas.'

Vision Super

'We anticipate our Climate Change Adaption Plan priorities shall result in reduced greenhouse gas emissions, attributable to our portfolio holdings, of 30% by 2020 and 50% by 2030. Those priorities include weather-proofing the investment portfolio by assessing asset specific climate change risks and looking at options to build resilience; engaging with boards and executives to proactively assess and mange climate change risk; and seeking new investment in renewable energy assets and other sectors that benefit from climate change adaptation.'
First State Super

CASE STUDY 4

NZ SUPER FUND SHIFTS PASSIVE EQUITIES TO LOW-CARBON

In a move to make the NZ Super Fund's investments more resilient to climate change, it moved its NZ$14 billion global passive equity portfolio (40% of the overall fund) into lower-carbon assets in mid-2017. The transition involved reallocating NZ$950 million away from companies with high exposure to carbon emissions and fossil fuel reserves into lower carbon-risk companies.

The Fund found that carbon exposures were highly concentrated in a relatively small group of companies and that by targeting specific industries, were able to significantly reduce the Fund's carbon footprint while retaining the diversification benefits of passive investment.

Reducing the Fund's exposure to companies at risk from climate change was a commercial decision based on long-term risk to our portfolio as a whole.

Companies can re-enter the portfolio in the future, if they improve their management of climate risk.

The Fund's approach is based on a bespoke carbon measurement methodology for listed equities developed by the Fund and MSCI ESG Research. The Fund publicly reports on its carbon footprint in relation to these targets annually.

The Fund has a target to reduce carbon emission intensity by at least 20% and reduce the carbon reserves exposure of the Fund by at least 40%, compared to if the changes hadn't been made by 2020. As at 30 June 2017, the Fund's total carbon emissions intensity is 19.6% lower, and its exposure to carbon reserves is 21.5% lower, than if the changes hadn't been made (baseline 30 June 2016).

Source: NZ Super Fund media release 15 August 2017

Ethical/responsible investment options

With the aim of providing clients choice, many funds also offer responsible, sustainable or ethical investment options.

25 out of 53 funds now offer a total of 75 dedicated RI options (compared to 24 funds offering 54 funds in 2016). 49 of the 75 RI options offered (65%) have obtained RIAA certification. Included in the group are the default and/or balanced options of **Christian Super, Australian Ethical** and **Local Government Super**, that have each obtained whole-of-fund certification by RIAA for their responsible investment strategies and disclosures.

Proportional to the fund categories in the universe, retail and corporate funds offer the largest variety of RI options per fund[11] (on average, 2.3 RI options for each retail fund and 1.8 for each corporate fund) despite, as reported earlier, showing the least inclination to implement RI strategies at a fund-wide level. Conversely, industry funds tend towards fewer RI options (0.9 RI options per industry fund), but consistently integrate RI at a fund-wide level, and public/non-regulated funds (excluding **Local Government Super** which has all options as certified RI options) tend to offer only one or two funds with a specific RI strategy.

These findings are consistent with the fund-client relationship that underlies the RI offering of each type of fund. An industry fund is more likely, by its operating model, to have a greater alignment with client views than a corporate or retail fund, perhaps enhancing the appropriateness of being able to implement fund-wide RI strategies that resonate with the majority of clientele. Similarly, corporate and retail funds aim to provide a large range of offerings for a more diverse client base, and hence the operating model relies more heavily on offering an array of choice and alternatives, rather than demonstrating whole-of-fund alignment with specific client values on RI.

11 The ratio of RI options per public/non-regulated funds is 1.8, however it is important to note that this result is biased, as NZ Super Fund and Future Fund are excluded from the ratio calculation due to their specifically legislated operating model. Otherwise public/non-regulated funds would show 1.3 RI options per fund.

***The integration of ESG factors enables investors and companies to** better understand the full spectrum of future risks and opportunities to which assets are exposed. Beyond its impact on the specific investments of the Funds, sound management of ESG factors contributes to the development of more efficient and sustainable markets, in turn enhancing long-term returns.*

The Board builds this perspective into its investment decision-making including the integration of ESG into the process for selecting external investment managers, evaluation of ESG factors in direct investments, and the management of ownership rights.

Future Fund

RI commitment to international norms

Another way in which funds are grounding their commitment to RI is through the reference to a wide variety of international conventions and guidelines that inform their RI policy (see Figure 6). This demonstrates a level of consideration of not only the fund's commitment to RI, but how that commitment aligns with activities of other institutions operating internationally.

The PRI's *RI Reporting Framework 2016 Overview and Guidance* is the most frequently cited international reporting guideline, used by 29 out of 53 funds (55%). This is followed by the *UN Global Compact's Ten Principles,* cited by 14 funds, then the *Cluster Munitions Convention* and *International Labour Organization Conventions,* cited by eight funds.

Other examples of this in practice include Australia being a signatory to the Convention on Cluster Munitions and the Ottawa Treaty on Anti-Personnel Mines, which have guided funds such as the **Future Fund, Sunsuper** and **Qantas Superannuation** to apply fund-wide exclusions.

Voting policy - themes

Decision-making processes and governance remain at the top of the list of voting priorities in 2018 (see Figure 7). Decision-making processes are most frequently articulated in the voting policies of 23 out of 53 funds (43%), followed by general governance factors (22 funds; 42%) and executive remuneration-focused governance factors (19 funds; 36%). Conflicts of interest and transparency are the fourth most reported priority (18 funds each or 34%), with environmental and social factors noted by 17 funds; 32%) with a voting policy.

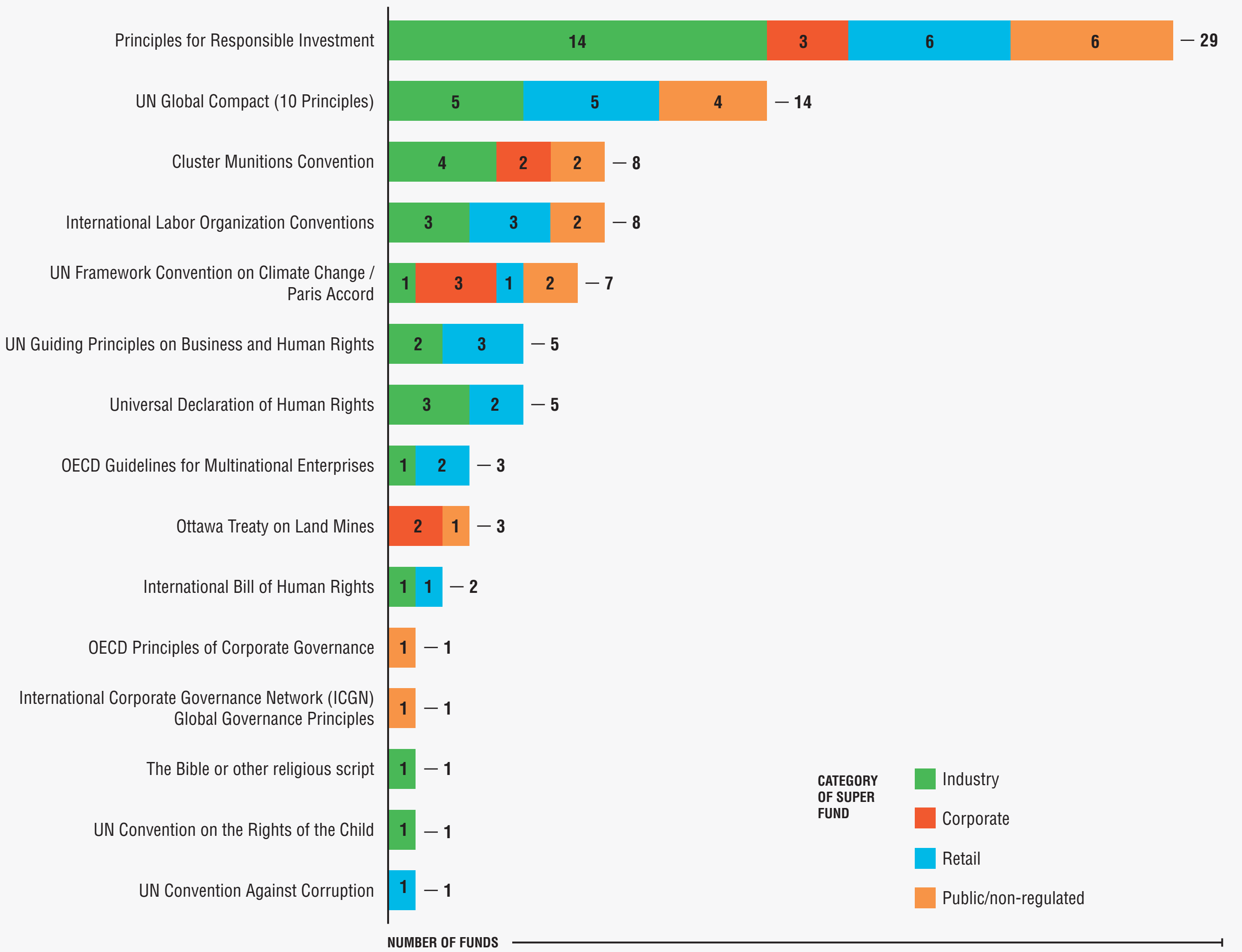
The order of these priorities is fairly consistent with 2016 findings.

Collaborative company engagement

A total of 34 out of 53 funds (64%) indicate involvement in collaborative company engagements, an increase from 52% of funds in 2016. This figure aligns with the ongoing popularity of membership-based organisations that provide participation in collaborative company engagement, such as the Australian Council for Superannuation Investors (ACSI) and the Principles for Responsible Investment (PRI). A total of 30 funds note their participation in collaborative company engagements through ACSI, and 26 funds through PRI. The Investor Group on Climate Change and RIAA are the third and fourth most cited groups with 23 and 20 funds respectively. Other ways in which funds collaborate on company engagement activities is via service providers such as Regnan and Hermes.

24 out of 53 funds (45%) have a formal engagement policy or process in place.

FIGURE 6 **INTERNATIONAL NORMS, CONVENTIONS AND GUIDELINES BY FUND CATEGORY**



Commitment to more sustainable financial markets

RIAA members support RIAA in its mission and objects which include working to deliver more sustainable financial markets. 19 out of the 53 funds surveyed are RIAA members and there are numerous examples of funds individually and collectively working towards improving:

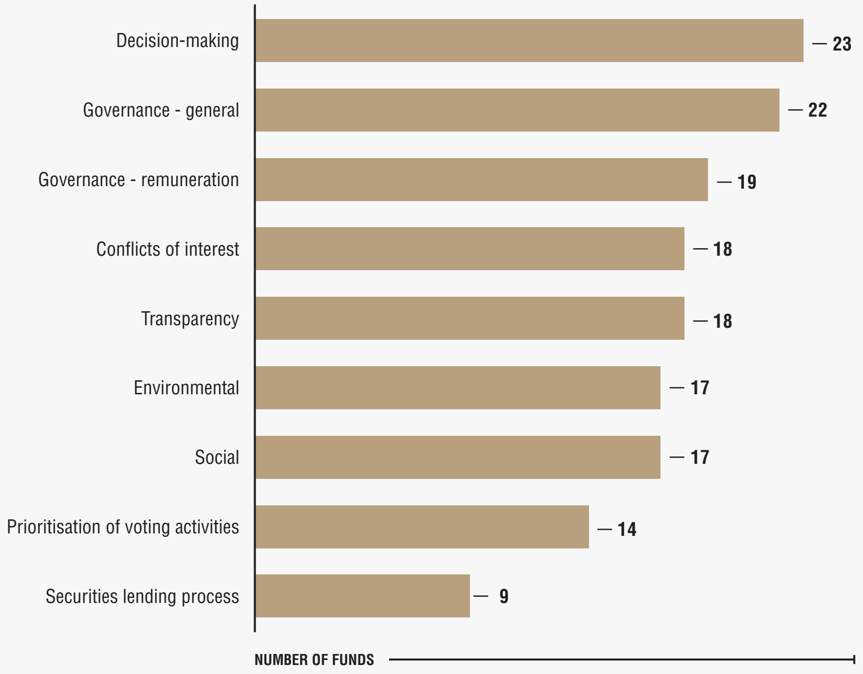
a stewardship practices e.g. Financial Services Council Working Group which delivered FSC Standard 23: Principles of Internal Governance and Asset Stewardship (for example, CFSGAM for **Colonial First State Investments**);
b transparency disclosures e.g. establishing the Modern Slavery Act in Australia with a view to improving supply chain transparency and company due diligence in supply chain management (for example, **Australian Ethical**); and
c accountability standards e.g. submission on the draft legislation of the Banking Executive Accountability Regime (for example, **AustralianSuper**).

Advocacy may be collaboratively or individually carried out and usually with a view to influencing processes and outcomes in favour of long-term value creation for and on behalf of clients. The themes for advocacy are wide and varied. **Australian Ethical** reports a number of themes for advocacy in 2018 including modern slavery legislation, licensing of labour hire providers and better business protection of human rights in supply chains, facilitation of impact investment, increased corporate carbon risk disclosure and emissions reduction targets, better understanding of fiduciary responsibilities of directors, trustees and investors, ethical treatment of asylum seekers, responsible credit card lending, marriage equality and eliminating inappropriate use of antibiotics in agriculture.

Collaborative initiatives (other than company engagement)

Funds join and participate in collaborative initiatives for a range of reasons, from keeping abreast of thematic developments (e.g. wage theft in Australian grocery supply chains) to participating in a 'community of practice' and collectively advocating to shape and influence the overall governance environment of underlying assets in which the funds invest (see *Commitment to more sustainable financial markets* above). There are many different vehicles for collaborative advocacy and the most popular ones are featured in Figure 8.

FIGURE 7 **VOTING POLICY THEMES**



The themes for collaboration are wide and varied. Examples include working with RIAA to advocate in favour of a Modern Slavery Act in Australia that requires companies to produce more accessible, reliable and comparable data on human rights risks in their complex supply chains.

Other examples of collaboration include the Climate Action 100+ initiative engaging the world's largest corporate greenhouse gas emitters to improve governance on climate change (**AustralianSuper, HESTA, Cbus, Australian Ethical, First State Super, Local Government Super, NZ Super Fund, VicSuper** and **Vision Super**); the 30% Club (of which **CareSuper** is a member) promoting gender diversity on the boards of listed companies; and, via the PRI, the Task Force on Climate-related Financial Disclosures (TCFD) Advisory Group and the Sustainable Development Goals (SDG) and Active Owner Advisory Group (**AustralianSuper**).

FIGURE 8 **MOST POPULAR COLLABORATIVE ADVOCACY VEHICLES**

Principles for Responsible Investment	34
Australian Council of Superannuation Investors	29
Responsible Investment Association Australasia	26
Investor Group on Climate Change	23
ESG Research Australia	9
Australian Institute of Superannuation Trustees	7
Financial Services Council	7
Association of Superannuation Funds of Australia	5
Regnan	2
Hermes EOS	2

3 RESPONSIBLE INVESTMENT IMPLEMENTATION

Formal processes that operationalise the responsible investment policy effectively and consistently across the fund and supply chain

Australia's largest super funds have formal processes in place for selecting, managing and monitoring the RI performance of underlying managers to ensure their fund commitments to RI are being implemented, where relevant, with their external agents. There is also a somewhat consistent trend towards better resourcing the management of RI in specialist teams, as well as within traditional investment teams, influencing the embedding of RI across a broader range of asset classes. Furthermore, there appears to be a move to the largest super funds insourcing their RI and ESG capabilities, including ESG data analysis.

This year's data reveals a step up in the formal management of external managers to deliver on the ESG and RI expectations of super funds. This is confirmed by a large increase in existing and new investment management agreements (IMAs) including RI performance expectations and reporting requirements. It is also consistent with anecdotal feedback RIAA has received that ESG expertise is an increasingly critical component of being awarded mandates by super funds, and the trend is expected to continue as mandates come up for renewal, and new mandates are awarded. However, there remains a large group of super funds (47%) whose minimum RI expectations set out for external managers is limited to a small scope of asset classes (usually only listed equities and/or fixed-income).

WHAT IS RI IMPLEMENTATION?

RI Implementation considers the operationalisation of the responsible investment policy and beliefs.

RESEARCH GOAL:
To assess whether the responsible investment beliefs are operationalised effectively across the fund and consistently with the RI policy and strategy.

Understanding RI implementation is less about what the fund has committed to in terms of RI and more about how the fund goes about doing it. Strong RI implementation starts with the fund's investment beliefs (which may or may not sit within the investment policy approved by the board and disclosed publicly) and follows an explicit process, both internally and with key external stakeholders, such as fund managers and asset consultants, to deliver investment strategies that are consistent with the fund's investment beliefs.

For example, if the investment belief is 'we aim to be active owners', then the evidence provided on the process involved in delivering successful stewardship behaviours (such as company engagements, proxy voting policies and disclosures etc.) should take a larger role in the implementation than say, impact/community investing or other RI approaches.

KEY ASPECTS USED TO ASSESS RI IMPLEMENTATION:

- can provide confidence that RI strategies are implemented through relevant channels;
- can demonstrate systematic process for RI implementation (e.g. such as how decisions are made within the organisation and between its external service provides);
- provides confidence that these processes are applied consistently and effectively (e.g. external research providers, third party verification, industry certification, evidence of continual professional development by key personnel etc.);
- has mechanisms for reporting internally against the policy implementation
- has clear and formal processes in place for selecting, managing and monitoring of underlying managers consistent with the fund's RI expectations;
- clearly sets RI expectations in relevant documents for and discussions with managers of underlying assets;
- can show how RI strategies are applied across material asset classes within the fund (or expressed as a percentage of AUM covered); and
- has clear processes for delivering RI approaches (e.g. ESG integration, sustainability themed, etc.) across the funds' various asset classes.

Given that a true picture of a fund's implementation is not possible without an extensive assurance process, which is outside the scope of this research, RIAA has relied on the self-declared approaches and performances to fulfil the assessment of RI implementation.

RI influence on asset allocation

19 out of the 53 funds (36%) report that RI influences strategic asset allocation (SAA). Of these, 10 funds specifically note climate change risk as a key consideration; this takes the form of decision-making around asset allocation and weightings based on emissions intensity (9 funds), as well as stress-testing and scenario planning (4 funds).

When asked about the relationship between a fund's RI policy and SAA, these 19 funds report that regular reviews of SAA consider alignment with the RI policy and tend to incorporate ESG issues where they are expected to impact capital market assumptions, economic outlook, or geographic risk. It is also noted that the formal ESG research and reports received by the fund from their asset consultant influence portfolio analysis and therefore SAA. Four funds note specific processes to build ESG risks into formalised portfolio analysis/construction processes.

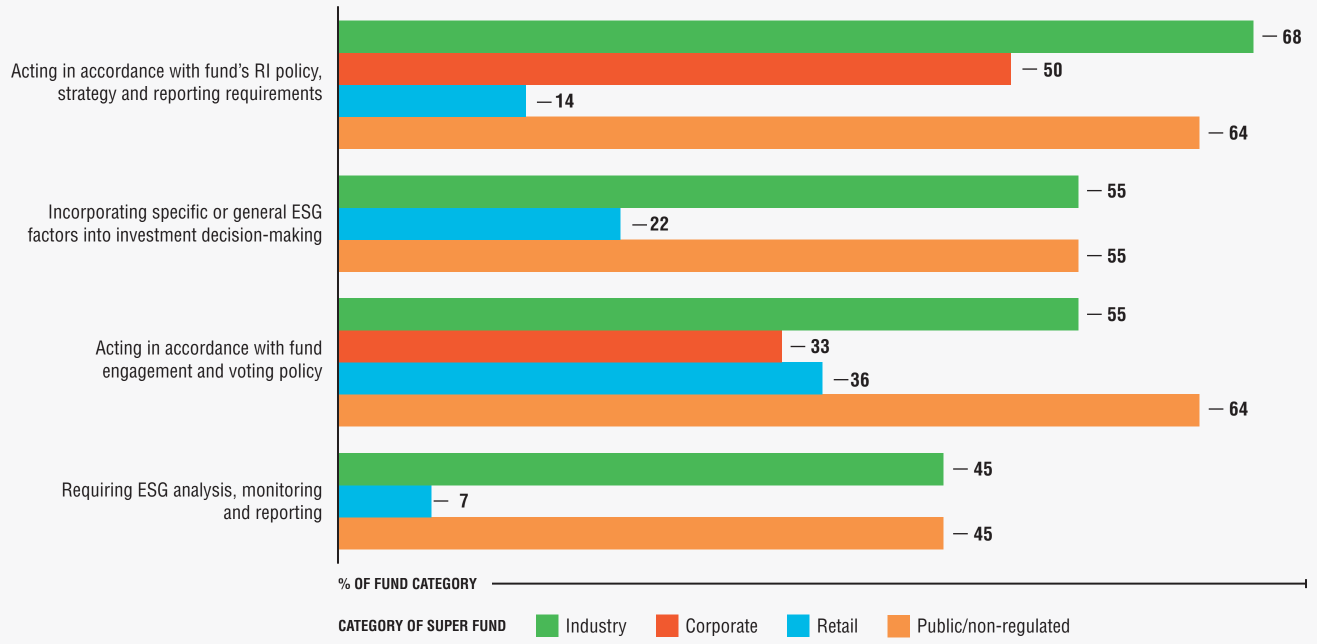
Investment manager management processes

20 out of 53 funds (38%) indicate that responsibility for RI implementation is incorporated into IMAs, marking a 4% increase from 17 out of 50 (34%) in 2016. These funds disclose a range of performance considerations they build into IMAs. Figure 9 notes the frequency and nature of these performance considerations among the funds that employ them.

VicSuper believes that generating long-term value for our members, *and providing them with peace of mind and financial security in retirement, requires a fundamental commitment to investing responsibly. What's more, as a long-term investor, we also have a vested interest in the sustainability of the global economy. Ultimately, if our members' retirement savings are to prosper and grow, the economy, society and the environment need to be healthy and productive.*

VicSuper

FIGURE 9 **RI PERFORMANCE CONSIDERATIONS USE IN IMA**



CASE STUDY 5

AUSTRALIANSUPER: INVESTMENT INTERNALISATION PROGRAM

'As AustralianSuper continues its investment internalisation program, a key focus is integrating ESG into our internal investment process. This significantly extends our ESG work from simply reviewing external manager ESG activities to undertaking ESG and stewardship activities ourselves so that we maximise long term value from these investments.

In listed equities, we produce ESG scores to help us assess the ESG risks and opportunities of each company. As a direct shareholder of the company, we then work with the internal analysts to address these risks and opportunities through stewardship activities such as direct company engagement and voting.

For unlisted assets such as infrastructure and property, ESG risks and opportunities are addressed in the acquisition phase using an internally developed ESG due diligence framework. We also have a program to develop ESG management plans for the ownership-phase of each asset. This includes engaging with the management team at the asset, conducting an annual assessment of individual assets and their ESG related risks and opportunities, and feeding that information into our internal teams' asset management processes.'

Encouragingly, all 17 funds that include RI performance considerations in IMAs indicate formal and periodic processes to evaluate managers on delivering against the defined RI considerations.

Asset consultants and RI

29 out of 53 funds (55%) employ asset consultants with RI expertise. Of these, an overwhelming majority of 27 funds (93%) use asset consultants to provide assessments on the ESG capabilities of managers, as well as for ESG research and advice on specific issues. Industry funds are the largest group using asset consultants for RI (14 out of 22 funds or 64%), with retail funds representing the lowest proportion (only 5 out of 14 funds or 36%).

17 funds have formal processes in place for asset consultants to report on RI outcomes (a further six have informal processes). While this is only a moderate proportion of the sample, several industry funds note that there is an increasing expectation that asset consultants are able to provide RI expertise and disclose evidence of that expertise. This is consistent with the historical development of the industry fund operating model, whereby asset consultant services have been integrated into the fund's business. As such, it is reasonable that an increased focus on asset consultant RI expertise appears to be driven by industry fund requests.

External managers - responsibility for and expectations in RI

37 out of 53 funds (70%) identify external managers responsibility for RI to some degree. 28 (53%) consider external investment managers as either wholly (18) or largely (10) responsible for the ESG information provided to the fund. A further nine funds identify that investment managers are partially responsible for RI.

Correspondingly, 25 out of 53 funds (47%) note that minimum RI expectations across listed equities and/or fixed income are discussed with external managers, either directly by the fund, or via the asset consultant. 24 out of 53 funds (45%) require external managers to discuss how ESG factors have impacted specific investment decisions/portfolio performance, and 21 require them to discuss their role in influencing investee company behaviour.

RI qualities factored into investment manager selection processes

21 out of 53 funds (40%) discuss expectations around ESG reporting with investment managers, while 17 out of 53 funds (32%) task investment managers with executing voting policies in alignment with the fund or the asset consultant's investment beliefs and strategy. 14 out of 53 funds (26%) also weight specific ESG factors when evaluating investment managers.

CASE STUDY 6

HESTA: EXTERNAL MANAGER MANAGEMENT

'Investment Strategy Unit ('ISU') and HESTA's Investment Execution Unit ('IEU') are jointly responsible for ensuring that external investment managers are aligned with our commitment to responsible investment and are appropriately incorporating ESG issues into the selection and management of investments and for otherwise implementing responsible investment, as relevant to each asset class.

To ensure implementation of the responsible investment in each asset class, the asset class teams, with support from the ESG team, incorporate consideration of ESG into their investment decisions.

Responsible Investment implementation activities will be prioritised based on a range of factors including the size of the asset class, the relevance and importance of ESG issues, the potential for HESTA to influence change (which is affected by a range of factors including investment type and style) and the progress of implementation to date.

At the time of publication, HESTA was actively engaging its 70 external managers in how they identify and manage gender diversity risks and opportunities in their respective underlying investments.'

CASE STUDY 7

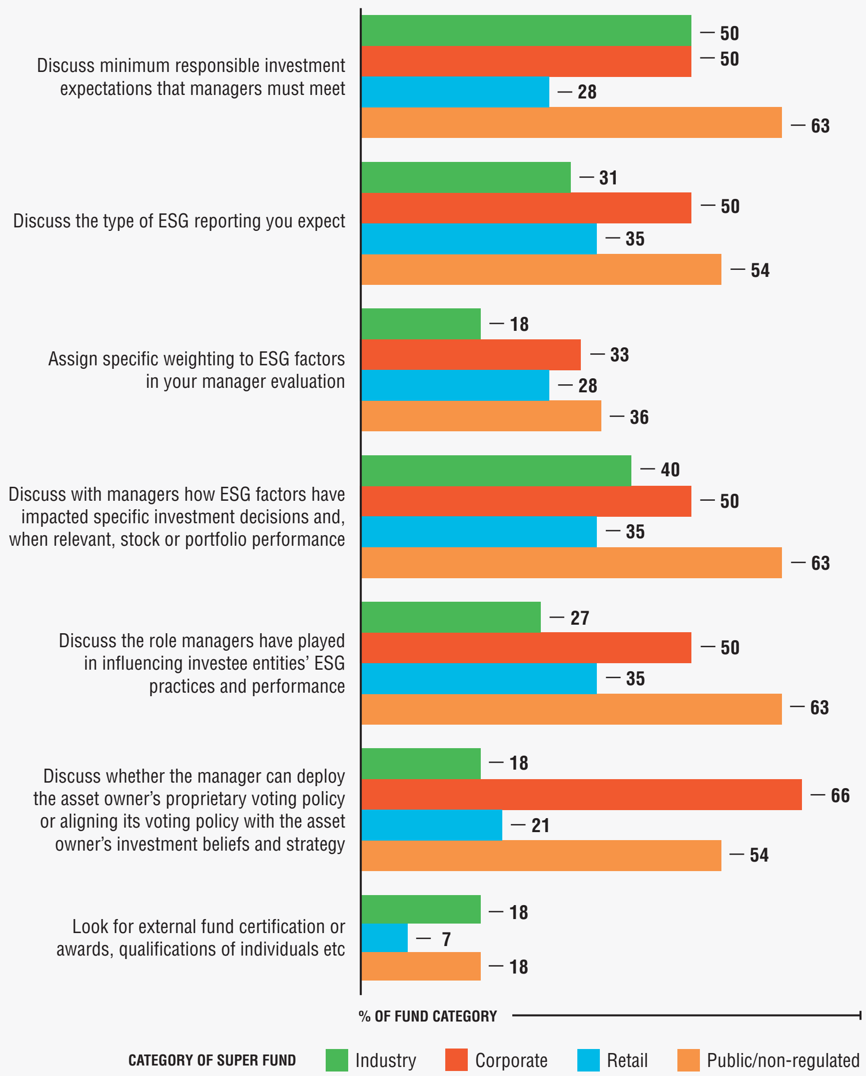
ENERGY SUPER: IMPLEMENTATION OF CLIMATE CHANGE RISK IN ESG POLICY

Climate Change Risk, which forms a subset of Environmental Factor Risks, is specifically addressed by the Fund through:

a. *Consideration of the impacts of climate change on stranded assets, which are defined as being assets deployed for the exploitation of a fossil fuel resource that, due to reduced demand, will no longer be exploited and will thus have no, or little value;*
b. *Engaging with its Investment Managers on the risks of climate change to:*
   - *Ensure that they have an adequate ESG Policy, which includes and considers the impacts of climate change,*
   - *Ensure that they have considered the risks and impacts of climate change in the pricing of assets – for both acquisition and exits,*
   - *Manage their underlying portfolio exposures to climate change risks, and*
   - *Report on portfolio risks and pricing of such risks.*

Energy Super, ESG Policy of September 2017.

FIGURE 10 RI QUALITIES FACTORED INTO MANAGER SELECTION PROCESS



20 funds explicitly require ESG reporting as part of standard IMAs with external investment managers. Eight funds require them across all IMAs, while 12 only required them across some asset classes, such as for equities managers. These findings indicate a growing complexity of the RI expertise required of investment managers by super funds.

Where funds rely on asset consultants as their intermediary with fund managers, this deepening complexity is also reflected upstream with increased expectations on the consultants' expertise.

Interestingly, only seven funds – **Australian Ethical, CareSuper, Future Fund, Hostplus, REST, VicSuper** and **NGS Super** – consider third-party certifications of investment managers and/or their products, or the qualifications of key personnel, as part of their process for the selection and review of external managers. This suggests that the enhanced complexity of information required by funds from asset consultants has largely been organic and negotiated on a case-by-case basis. **BT Financial Group** (for RSEs BT Funds Management and Westpac Securities) notes that they require managers to act consistently with the CFA Institute's Asset Manager Code of Professional Conduct.

Again, as in the case with asset consultants' integration within the operating structure of industry funds, this represents a growing embedding and harmonising of relationships between the various service providers and funds when it comes to executing RI strategies and beliefs.

CASE STUDY 8

COMMONWEALTH SUPERANNUATION CORPORATION AND COMPANY ENGAGEMENT

'CSC has a large and dedicated specialist engagement capability executed through our governance partner, Regnan. Regnan proactively engages with Australian companies in our portfolio. We also use our investment managers in this regard. In addition, our proxy voting advisor, CGI Glass Lewis, undertakes engagement with companies on a global basis. Direct engagement occurs when called for and on a very occasional basis.'

Evidence of quality data sources to enhance RI decision making

In 2016, 18 out 50 funds (36%) were able to identify how reliable ESG information was sought. In 2018, this has increased to 31 out of 53 funds (58%).

External manager ESG information is the key source of ensuring robust ESG integration (32 funds), followed by use of accredited company ESG ratings/scorecard or databases (21 funds) and sourcing comprehensive ESG research (20 funds). These results are largely consistent with 2016 findings.

Several funds note that whilst external managers are often looked to for ESG research and due diligence, this is complemented by fund's sourcing their own RI information, particularly on issue specific or asset specific concerns. This is done through securing ESG research or data providers (in many cases, more than one), or by increasing the requirements for external manager RI accountabilities (e.g. reviewing PRI reports or other disclosures). Some funds refer to their RI specialist staff as responsible for ensuring the thoroughness of due diligence around this.

Encouragingly, only six funds indicate sole reliance on ESG information from external investment managers. Nine of the 22 industry funds (41%) use three or more sources of ESG information; as do four out of 11 public/non-regulated funds (44%); three out of six corporate funds (50%), and three out of 14 retail funds (21%).

Corporate engagement and shareholder action

Overall, a greater number of funds disclose formal engagement policies and voting policies than in 2016. In the case of voting, this increase is partially attributable to a greater number of funds responding to the survey and providing completeness of information.

Company engagement
34 out of 53 funds (64%) report involvement with company engagement, an increase from 52% in 2016.

Eight of the funds – **AMP Superannuation, CareSuper, Commonwealth Superannuation Corporation, NZ Super Fund, Sunsuper, TWU Super, UniSuper** and **First State Super** – involved in company engagement, indicated playing a comprehensive role in that engagement, such as agenda-setting, attending meetings, post-engagement monitoring and reporting. 18 out of 34 funds (52%) involved in company engagement reported moderate participation (9 funds) or basic or little participation (9 funds) which involves casual or passive review of company engagement outcomes. These findings are consistent with the idea that company engagement is often seen by funds as a way to provide support for issues that they may not have the resources or expertise to attend to directly.

24 out of the 53 funds (45%) have formal engagement policies and processes in place, while 23 out of the 53 funds (43%) undertake direct engagement activities, up from 30% of funds in 2016.

Voting
An impressive majority of 50 out of 53 funds (94%) indicate they have a formal voting policy, and all but one of these funds make their policy public. This compares with 58% in 2016.

In 2018 funds were requested to provide data around votes cast against boards, proxy voting advisers, and both boards *and* proxy voting advisers. This information was sought to help more fully understand the scope and depth of stewardship in practice, working off the assumption that funds which resource their stewardship commitments and implement their stewardship principles will likely vote against recommendations, at least some of the time.

Of the 29 funds providing responses to how they voted in 2017/18, three funds voted with the company board and/or, proxy voting adviser on every occasion. In contrast to this, five funds voted most frequently independent of board and proxy voting

CASE STUDY 9

NEW ZEALAND SUPER FUND ON COMPANY ENGAGEMENT

'Our engagement objectives are to monitor, identify and engage with companies which breach international standards of good practice, in particular the UN Global Compact. Our engagement seeks to encourage companies to address poor ESG practices and improve ESG disclosure.

We have four priority areas for engagement:

- *Human rights (child labour; worker safety; operations in weak states);*
- *Business ethics (bribery& corruption);*
- *Severe environmental damage; and*
- *Climate change.*

Companies in breach of standards are brought to our attention by MSCI, our ESG research provider, through 'red flag' alerts. If the breach aligns with our priorities, it is added to our Global Engagement Focus List.

We carry out our engagement via five avenues:

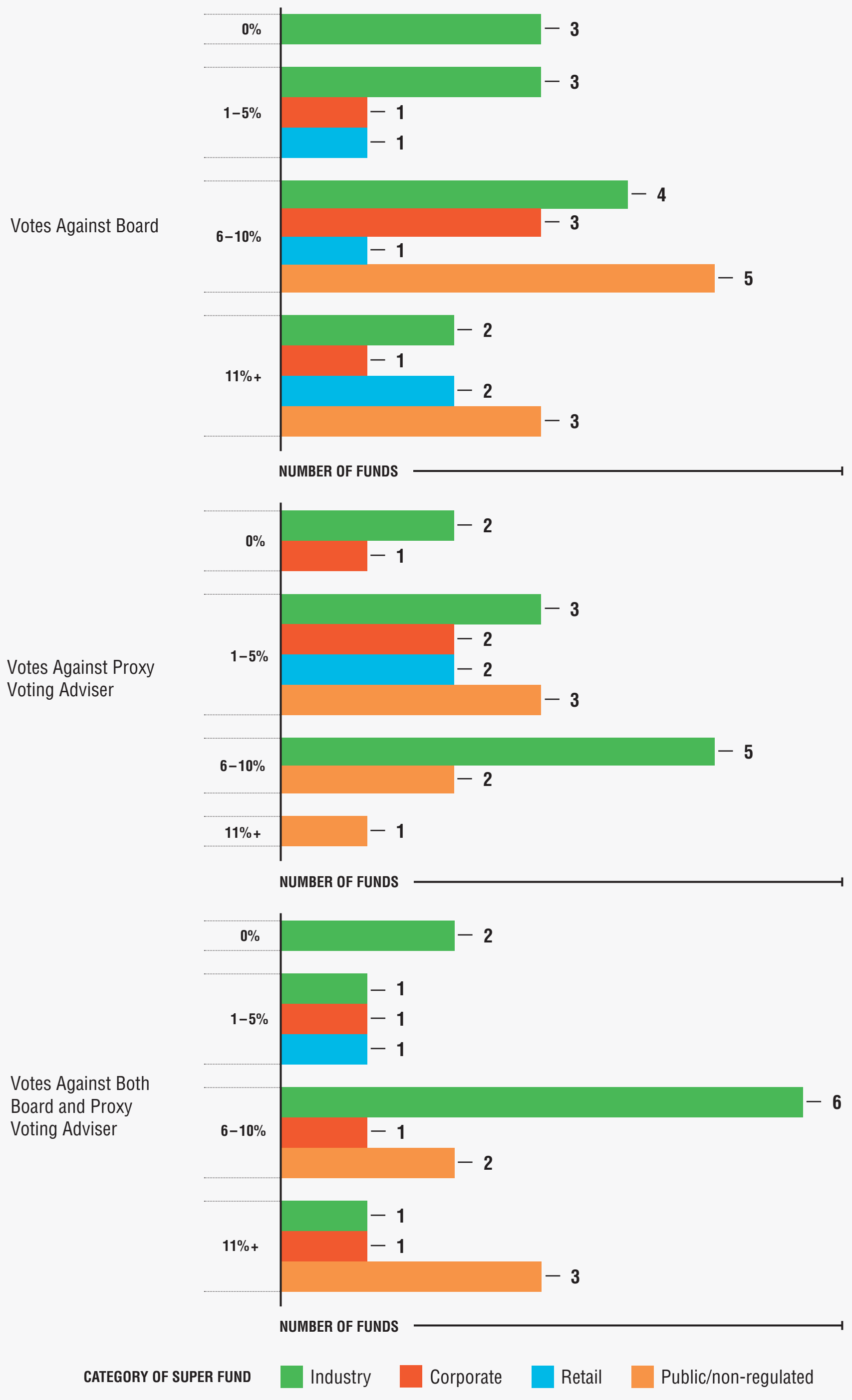
1. *The RI team engages with companies directly; or*
2. *we engage through collaborative efforts;*
3. *we employ BMO as a service provider;*
4. *we require our managers to engage on our behalf; and*
5. *The in-house NZ Active Equities Team engages directly with companies in New Zealand.*

At the beginning of every (direct) engagement, we put together an engagement plan that provides context and reasoning for the engagement as well as setting performance targets and milestones. Progress of the engagement is recorded and reported on quarterly. Monitoring responses (or lack of) are also looked at quarterly.

In 2017, we evolved our engagement tracking system to better provide indicators of progress.

Engagement may be undertaken by any of the investment staff, including CEO or CIO.'

FIGURE 11 **VOTES CAST (%) FOR AND AGAINST BOARDS AND PROXY VOTING ADVISER**



advisers (i.e. on at least 10% of occasions) (**Future Fund**, **HESTA**, **Local Government Super**, **Mercer** and **Vision Super**). As interest in voting decisions by fund members and other stakeholders grows, particularly for shareholder resolutions, the expectation on the oversight of voting decisions, by board and investment committees, is increasing.

Vision Super customises its voting and for example, votes against remuneration reports where any member of the executive team is paid more than twice as much as the next most highly paid executive. The fund holds the view that inequality is one of the leading drivers of poor ESG behaviour and that excessive remuneration in the finance industry has led to some individuals having outsized influence in other areas. In 2017 **Vision Super** voted against board recommendations on more than 10% of occasions, against proxy voting adviser 6-10% of occasions and voted against *both* board *and* proxy voting adviser more than 10% of occasions.

HESTA believes that good ESG management and performance by *companies in which we invest, will reduce risk and improve long-term returns, while poor ESG management and performance will increase risks and reduce long-term return.*

HESTA

Implementation of other approaches such as screens, sustainability-themed investments and impact investing

This year's research explores how funds approach implementing screens, sustainability-themed investing and impact investing. However, the data points to a number of common approaches and inferences can be made from the knowledge gained administering RIAA's Certification Program.

Screening

External ESG data providers play an important role for super funds holding direct investments. These providers (MSCI, Sustainalytics, CAER etc.) provide, for example, regular research on company controversies as well as full exclusions lists or screened indices. This research makes direct investment decisions – on the RI side – easier for internal investment teams implementing negative screens.

Sustainability-themed investing

As with screening, sustainability-themed investments – such as around green buildings and infrastructure, forestry and fisheries – tend to rely on external, third-party verifications and certifications as a proxy for due diligence on the 'sustainability side' of the investment. Internal investment teams use these ratings as an overlay to develop their investable universe alongside traditional financial analysis to select, retain and realise assets.

Impact investing

Some funds stated that the resourcing required to undertake due diligence on impact investing projects, given their limited knowledge of social and environmental aspects and the small scale of projects, makes the ability to invest prohibitive. Some large super funds are trialing their participation in this RI approach by investing into existing funds (such as Impact Investment Group's Giant Leap Fund) or where possible directly into investable projects.

FIGURE 12 **FORMAL INTERNAL RI REVIEW BY FUND CATEGORY**

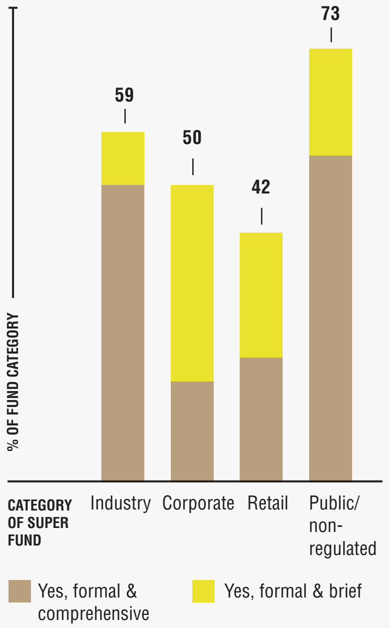
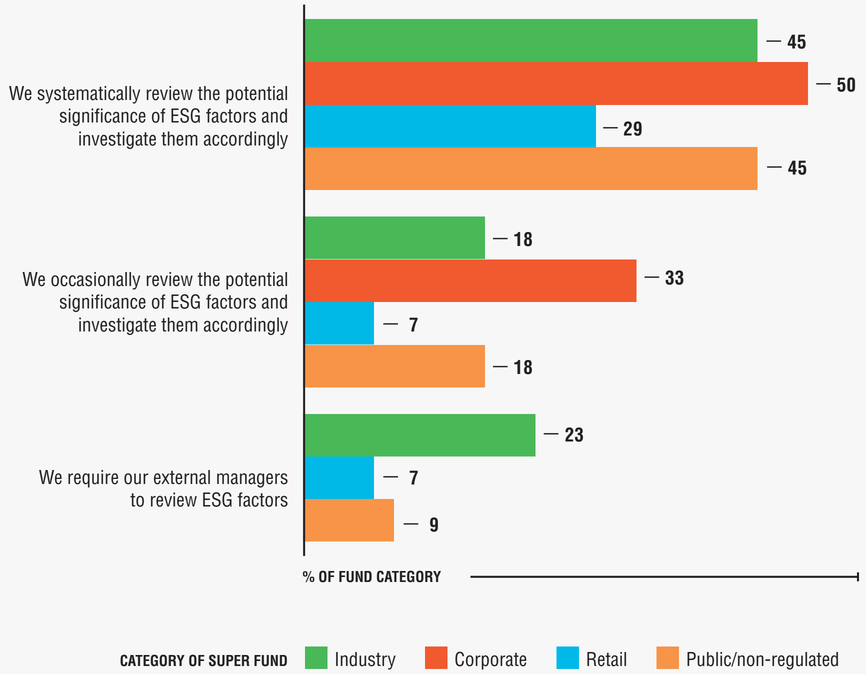


FIGURE 13 **REVIEW OF ESG FACTORS BY INTERNAL TEAMS**



Role of formal review in implementation

Alignment of fund with overall strategy and investment beliefs
30 out of 53 funds (57%) indicate they conduct formal internal reviews to ensure that their RI policy is in alignment with the fund's overall strategies and investment beliefs. This is up from 19 of 50 funds (38%) in 2016, suggesting a greater consolidation of RI implementation across the funds.

This group includes 73% of public/non-regulated funds, 59% of industry funds, 50% of corporate funds and 42% of retail funds. The findings suggest that industry and public/non-regulated funds demonstrate a greater maturity in their implementation of RI at an internal governance level than corporate and retail funds. This can be seen in Figure 13, where a larger proportion of industry and public/non-regulated funds are conducting formal and comprehensive internal RI reviews. These findings are consistent with 2016.

Potential significance of ESG factors
In terms of funds reviewing ESG factors internally, 22 out of 53 funds (42%) note systematic reviews of the potential significance of ESG factors by internal investment teams. This includes 50% of corporate funds, 45% of both industry funds and public/non-regulated funds, and 29% of retail funds.

A further nine funds disclose that these reviews occur occasionally, while seven (five industry funds, one retail fund and one public/non-regulated fund) indicate that this is the responsibility of external managers.

Internal reviews of ESG factors appear to be more consistently applied across all fund categories than formal reviews of RI policy alignment with fund strategy (Figure 14 versus Figure 13). This trend is most evident with corporate funds, which show a greater propensity to implement systematic ESG reviews by internal teams (50%) than formal and comprehensive reviews of RI alignment with fund strategy (17%). Similarly, 29% of retail funds indicate systematic ESG reviews by internal teams, versus 21% which report formal reviews of RI alignment with fund strategy.

As universal owners, we consider that active ownership (i.e. proxy voting and engagement) with the companies in which we invest is fundamental in driving positive portfolio outcomes.

***BT Financial Group** (including RSEs BT Funds Management and Westpac Securities)*

Among industry and public/non-regulated funds, there is a slightly lesser percentage (45%) that implement systematic ESG reviews by internal teams than conduct formal reviews of RI alignment with fund strategy (50% industry funds, 55% public/non-regulated funds). 23% of industry funds also indicate reliance on external managers to review ESG factors, a larger percentage than any of the other groups.

These results are consistent with earlier findings regarding the importance placed on whole-of-fund integration of RI strategies by industry and public/non-regulated funds distinct from corporate and retail funds.

4 MEASUREMENT AND OUTCOMES

Measurement of outcomes for RI policy implementation, including impacts broader than direct financial results and returns

In our exploration of measurement and outcomes, RIAA considered the nuances and measurement challenges for the differing RI approaches; finding that this is simpler for some asset classes and impact areas than for others e.g. the outcomes from applying a sustainability-themed investment approach across property assets can be reasonably measured (e.g. NABERS, Green Star, GRESB) by way of individual asset star or index rankings, or aggregate rating for a 'green' property portfolio. As these third-party ratings possess built-in performance benchmarks, assumptions can be made in terms of reductions in greenhouse gas emissions, tenant energy consumption savings and so forth.

For many funds, ESG integration is driven by the belief that consideration of ESG factors will provide better long-term risk-adjusted performance. As noted by many respondents, this is a difficult area to measure and report, beyond pointing to the strong overall returns of the funds.

Even so, the research findings suggest that measurement of RI strategy impacts and outcomes, across more than a few developed areas (such as investment manager performance) is gaining some momentum with Australia's largest super funds. However, measurement more broadly is well understood and undertaken by funds for financial and reputational purposes.

WHAT IS MEASUREMENT AND OUTCOMES?

Measurement and outcomes refers to the practice of tracking progress on RI implementation against a defined target or set of success measures; and the outcomes of investment practices on environmental, social, governance and ethical issues.

RESEARCH GOAL:
There are growing expectations from beneficiaries and other stakeholders on funds to report on the outcomes of responsible investment strategies. This pillar looks at the ways any funds are starting to measure their outcomes and assess any proxies for measuring the impacts and outcomes of responsible and ethical investment activities beyond financial performance.

This is a new and emerging area for responsible investment. This area ties in closely with transparency and reporting, however seeks to see what approaches are currently being used by funds to measure and therefore clearly discuss the outcomes of their responsible investments.

KEY ASPECTS USED TO ASSESS RI MEASUREMENT AND OUTCOMES:

- defines indicators (or proxies) and/or set targets to measure the performance of their RI activities and outcomes;
- has processes to measure RI strategies against fund beliefs or stakeholder interests demonstrated;
- has a method to measure fund success in RI implementation;
- uses external organisations such as research houses etc. to assist with the measurement of performance and outcomes; and
- puts itself forward for external review and assessment.

Targets and measurement

This year's findings showed a growing number of funds are setting RI-related targets (see section on RI Commitment). Whilst specific or quantifiable targets are not always fit for purpose or always necessary for implementing RI policies and strategies, targets are often set by funds with a high regard for measuring performance and being able to explain the results derived from committing resources to a particular activity.

13 out of 53 funds (25%) report that they have set performance targets for their RI strategy. These targets vary from reducing carbon intensity and ensuring voting of a certain percentage of shares, to PRI reporting as a standard for measuring performance (see RI Commitments page 16 for examples of these). Some examples of fund approaches to measuring performance against set targets are outlined below.

ESG performance – direct and via external managers
The **Future Fund** states that since 2015, its investment team has reviewed and rated investment managers on their capacity and commitment to manage ESG issues on the Fund. It has measured the ESG and carbon footprints of its equities portfolios (every 6 months) since mid-2016**.**

Commonwealth Bank Officers Superannuation and **Colonial First State Investments** measure the ESG ratings of their equity portfolios to discuss the findings with investment managers; and the funds' property managers take note of ESG ratings such as NABERS for water and energy in property and infrastructure.

Positive/Negative screening and sustainability-themed
To measure the outcomes for screening – negative or positive – funds publish excluded stocks or specific investments made due to a positive tilt.

Future Fund's RI strategy includes negative screening of tobacco stocks and this is evidenced by its publication of the excluded company names on the fund's website. **NZ Super Fund** also publishes excluded companies aligned with aspects of their RI strategy – a demonstrable depiction of the fund delivering RI outcomes. **UniSuper** undertakes regular stock assessments to ensure that there is consistency with RI objectives.

In terms of demonstrating the outcomes of positive tilting, some funds highlight their range of sustainability-themed investments in their annual reports or on their website. **First State Super**'s Investment Portfolio Showcase features a range, including hospitals and other public infrastructure, and **Hostplus** lists its biomedical investments aligned with its investment beliefs for a healthy society. **Australian Ethical** measures the extent of alignment of its energy sector investments within a two degrees of global warming pathway. **Mercer** uses the Weighted Average Carbon Intensity Metric (CO2 tonnes/AU$1M revenue) to measure its carbon intensity for listed equity portfolios. **Vision Super** also applies this and then tracks its progress against the fund's portfolio decarbonisation target.

Although not tracking against a particular target, **Australian Catholic Superannuation and Retirement Fund** measures the percentage of portfolio invested in renewable energy and other assets with green ratings.

Company engagement and voting
With respect to company engagement activity, there is a very broad spectrum of tracking performance and measuring outcomes. Of the 23 out of 53 funds (43%) that undertake direct engagement, all of

them report monitoring company actions taken after the engagement, either all of the time (eight funds) or the majority of the time (15 funds). However only 16 out of these 23 funds (70% or 30% of the entire universe) keep reliable data on engagements in the form of company engagement reports. Fewer still disclose their engagement activities (see page 28 for engagement disclosures).

VicSuper relies on service providers ACSI and Hermes EOS to provide a company engagement plan proposal. Throughout the year the Fund is provided with engagement activity updates and a formal report of outcomes achieved at the end of each year. The outcomes of this engagement, supported by further research, are used to shape the following years' engagement activities. ACSI engagement monitoring and review is undertaken semi-annually via progress reports and presentations. **VicSuper** also actively monitors and reviews the activities of its service provider Hermes EOS through quarterly calls, regular reports and use of their online information portal.

CASE STUDY 10

AUSTRALIAN ETHICAL MEASURING PROGRESS ON COMPANY ENGAGEMENT

'We have been a consistent and persistent voice for climate transparency and action by the big four banks, and for more responsible banking in general. This has been pursued through direct engagement with the banks (including those we exclude), and in collaboration with a diverse range of other influencers including RIAA, IGCC and Market Forces.

In several meetings with Westpac and at its AGM, Australian Ethical asked the bank to rule out support for the proposed Adani Carmichael mine in order to clearly and publicly demonstrate the integrity of the bank's climate commitments. Westpac's 2017 climate action plan did rule out lending to Carmichael by excluding any lending to new thermal coal basins.

NAB finished 2017 with an announcement that it will no longer finance any new thermal coal mining projects.

The 2017 financial year reporting of all four banks showed significant reductions in their exposure to coal mining, along with refreshed renewable energy and other low-carbon lending targets. This progress needs to continue.'

Measuring performance and outcomes of other RI approaches

The meaning, measurement and tracking of performance has many guises. For funds whose primary RI approaches are ESG integration, and corporate engagement and shareholder action, RI performance can relate to alignment with investment beliefs, quality of due diligence processes or even overall financial returns. Some examples are provided here.

NZ Super Fund tracks how it ranks in external initiatives such as the Asset Owners Disclosure Initiative. **First State Super** states that its whole RI strategy is based on a long-term investment horizon; and its investment due diligence includes assessment of ESG risks for every investment that it plans to undertake. A key assessment criterion is the alignment of long-term investment horizons as part of this assessment. **AustralianSuper** states its RI activities are integrated into the investment process and this means that portfolio performance indicates the performance of the fund's RI strategies. Portfolio performance is a key performance indicator for the RI team.

For organisations such as **Christian Super** and **Australian Ethical**, which both invest consistent with their broader ethical/values-based charters, measurement, whilst still challenging, is becoming more sophisticated.

Australian Ethical use metrics including MSCI's 'sustainable impact revenue' earned by companies it invests in i.e. revenue from activities contributing towards certain SDGs; and information about the impact of specific investments. **Christian Super** measures and reports on certain impact metrics from its portfolio including number of student loans provided, number of microfinance loans, number of micro-insurance customers, increase in employment in social enterprise companies in which it invests, and carbon emissions avoided through new renewable energy sources.

Challenges to measurement

Reliability of ESG data; limitation in ESG provider methodologies
Funds consistently state that the reliability of ESG data is critical to adequate measurement. **CareSuper** states that one of the challenges is to find the 'holy grail' to measure fund-level ESG risks due to the limitation in methodologies used by most ESG data providers for assessing company level ESG performance.

CASE STUDY 11

CARESUPER TRACKING MANAGER ESG PERFORMANCE

CareSuper requires all managers to integrate ESG into the investment process. To assess how well managers have incorporated ESG, CareSuper formally surveys managers on ESG at annual asset class reviews. In addition, CareSuper's ESG Specialist frequently meets with investment managers and discusses ESG issues together with the Fund's asset class specialists.

ESG metrics can vary across asset classes. For example, for listed equities, it is important for managers to have a responsible investment policy, a voting/engagement policy, and there is evidence that ESG is being incorporated into the investment process.

For other asset classes such as property, managers are also assessed on their portfolio level GRESB ratings and NABERS ratings.

All managers are reviewed on whether they are signatories to ESG collaborative initiatives.

If a manager is assessed to be lacking in any of these areas, CareSuper would engage with the manager on the Fund's expectations regarding ESG integration. It is also important to note that at the stage of manager selection, potential investment managers need to demonstrate to CareSuper how ESG is incorporated into the investment process. An investment manager with a more rigorous ESG approach is more likely to be selected than its peers. In addition, CareSuper incorporates ESG into mandate schedules and side letters where possible.

Inability to attribute outcomes to management of ESG factors
Funds also express difficulty in separating ESG and non-ESG data, which poses a challenge in measuring and performing against RI targets. As such, measuring and reporting on carbon emissions as a target is popular, as is having voting or engagement targets. However, even with voting and engagement, funds voice concerns about the potentiality for disclosure to preference quantity over quality.

In a similar vein, the **Future Fund** states that a key challenge for measurement is the exact and therefore, credible measurement of the impact on investment performance from its RI strategy. Moreover, many relevant ESG metrics may not be material to investment performance.

5 TRANSPARENCY AND RESPONSIVENESS

Practices on transparency in responsible investing reporting and stakeholder engagement with focus on inclusivity, materiality and responsiveness

There are many aspects to transparency and responsiveness; and one of the most central is reporting performance and outcomes against the RI strategy. This has to be done so the information is relevant to and accessible for stakeholders and, by way of example, may be where quarterly newsletters are more appropriate than an annual report.

From an asset owner point of view, particularly one that takes a universal owner perspective, there is also an expectation to provide evidence that the fund is fully and effectively implementing the stewardship responsibilities bestowed up on it. At a minimum this takes in manager disclosures (where relevant), holdings disclosures, engagement and voting disclosures.

Again, the ways in which this is done varies greatly between funds based on the fund's assessment of the most appropriate way to report to and/or engage with clients and beneficiaries about this area of performance. There are many different aspects of relationships and activities reported by funds, some of which are included in Figure 14.

WHAT IS TRANSPARENCY AND RESPONSIVENESS?

Transparency is about the complete and reliable disclosure of investment practices. Responsiveness is about the timely communication with relevant stakeholders in a way that is inclusive, respectful and accessible.

RESEARCH GOAL:
To assess the fund's practices on transparency in reporting and stakeholder engagement with focus on inclusivity, materiality and responsiveness in responsible investing.

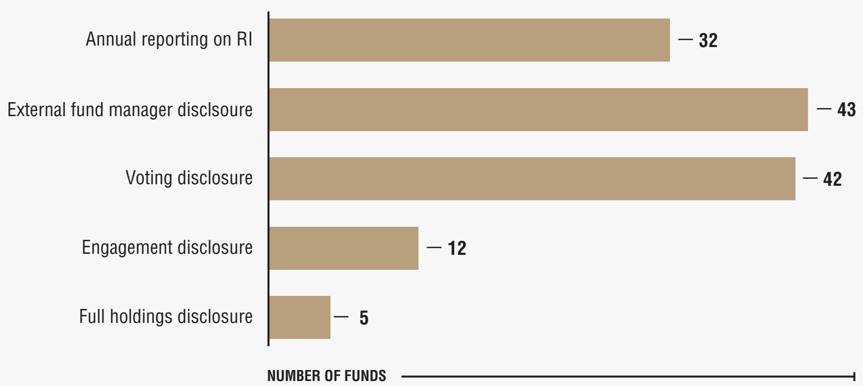
KEY ASPECTS USED TO ASSESS TRANSPARENCY AND RESPONSIVENESS:

- has a demonstrated commitment to transparency of processes and approach;
- reports on the performance and outcomes of the RI strategy;
- enables key stakeholders have access to relevant and accessible information;
    - provides regular disclosures including underlying fund manager names, full stock holdings, fund performance;
    - communicates to clients around responsible investment issues and performance
- makes it easy for clients to identify, compare and choose responsible investing option over others; and
- regularly surveys stakeholders for their RI-related interests, satisfaction with service etc.; this information is used internally for improved decision making.

Proxies identified for funds demonstrating a clear commitment to transparency of approach and RI process included, but were not limited to:

- having an accessible and comprehensive set of policies, guidelines and resources on their public websites;
- clear and regular client communications including RI matters;
- publishing RI transparency reports; and
- putting themselves forward for industry and government awards for performance related to disclosures and transparency.

FIGURE 14 **RI TRANSPARENCY BY DISCLOSURE**



Annual reporting on RI

Formal reporting against RI policy and strategies
33 out of 53 funds disclose annually on their RI activities, representing 62% of the universe, and 77% of the funds that make some form of commitment to RI. This is up from 22 funds (44%) in 2016.

18 funds disclose on RI via their annual report, up by three funds from 2016. Nine funds – **Australian Ethical, CareSuper, Cbus, Colonial First State** (both funds), **MyLifeMyMoney, Mercer, VicSuper,** and **NGS Super** – produce an integrated report, a form which has been much further consolidated since 2016 when it was only used by four funds. It is worth noting that the term 'integrated report' is interpreted by respondents in a general way, and not specifically with reference to the Integrated Reporting initiative managed by the Integrated Reporting Council, which follows specific protocols and guidelines as part of its pilot phase.

Three funds (**Local Government Super, UniSuper** and **Vision Super**) submit a standalone RI report (up by a single fund from 2016), while two funds report on RI through their sustainability reporting (**Westpac** and **NGS Super**) and one fund discloses on RI via their website as the main platform (**First State Super**).

Disclosure of external fund managers
43 out of 53 funds (81%) disclose all external fund managers used; an increase of 21% since 2016. Separately, eight funds disclose major external managers used.

Voting disclosures
80% of the 50 funds with a formal voting policy make voting records public; 38 funds do this after voting, and one before (**Local Government Super**).

While this is increasingly considered emerging practice for voting disclosure in other jurisdictions, it should be noted that many of Australia's larger funds refrain from making voting decisions public prior to voting in situations where the fund has a large equity holding in a stock and public announcement of the fund's decision could unduly distort market perceptions.

Engagement disclosures
23 out of 53 funds (43%) undertake direct company engagements yet only 13 out of 53 funds (25%) also keep reliable data on the activities and outcomes. 9 out of 53 funds (17%) – **AMP Superannuation, Australian Ethical, Cbus, Commonwealth Superannuation Corporation, HESTA, Local Government Super, NZ Super Fund, UniSuper** and **VicSuper** – state that they always disclose company engagements. However the nature of these disclosures vary, with not all the funds providing the names of the companies engaged, only the aggregate number of engagements undertaken and/or the themes of engagement. A further three funds provide links to the external manager report where engagement results are published. This shows that over half of the funds that undertake direct engagement activities do not report on their activities publicly (13 out 23 funds; 57%).

This finding reflects the perspective of some that engagement is not considered an outcomes-based exercise, but one that focuses on long-term stewardship and relationship-building.

CASE STUDY 11

LOCAL GOVERNMENT SUPER ON PUBLIC DISCLOSURE OF ENGAGEMENT ACTIVITY

*'**BHP** – We supported the recent shareholder resolution on membership to associations that were detracting from climate policy progress and engaged with BHP directly and indirectly to show our support. BHP have committed to action following a review published in December 2017.*

***Ansell** – We engaged with Ansell directly and INDIRECTLY through our fund manager and ACSI about a number of human and labour rights issues across their supply chain. As a result of industry engagement on this issue, Ansell addressed a number of issues to improve working conditions in their factories.*

***CBA** – We engaged with CBA directly on climate change and governance issues. Following extensive investor engagement, CBA have committed to increasing their work on climate change and also made significant changes to their board governance and rem payouts for 2017.'*

For some funds, reporting on engagement activities is identified as non-conducive to the encouragement of a positive outcome with companies where discussions are on-going. Respondents report that the efficacy of providing disclosures on engagements must be understood in the context of the investment beliefs held by funds regarding the importance of discretion in engagement activities.

A handful of funds comment that engagement outcomes are not disclosed because the fund cannot assume that an outcome is based on their engagement alone. While these considerations are reasonable in their intention, those funds that do disclose engagement reports (e.g. **Cbus**) state that they regularly demonstrate ways and means to be accountable to their stakeholders for the conversations they are having with companies, without jeopardising the spirit and progress of those relationships.

Disclosure of portfolio holdings
Only five funds publicly disclose full portfolio holdings (**AustralianSuper, Cbus, Christian Super, Australian Ethical** and **NZ Super Fund**), whilst 11 funds publicly disclose at least the largest 21-50 holdings, and a separate 19 disclose the largest 10-20 holdings (up from 16 funds in 2016). This represents 35 out of 53 funds or 66% of the universe providing some level of transparency around their portfolio holdings. It is possible that in the balance of funds surveyed (34%), such as in the retail or corporate funds, may make portfolio holdings available but only directly to clients. **Local Government Super** doesn't explicitly disclose its full holdings, however a list of these can be found by clicking through the voting records which are kept current on its website.

Accessibility of information and stakeholder responsiveness
Effective transparency includes the ability to clearly and relevantly communicate disclosures to stakeholders. In a year when delivering in the best interests of beneficiaries and clients is front and centre of public debate in Australia, the research reveals several different ways that funds proactively inform clients and other stakeholders on their activities and performance around responsible investing.

For the funds that have RI front and centre of their investment beliefs, overall, RIAA found RI information very easy to find on the funds' public websites and in annual or standalone sustainability or RI reports. However other methods included surveys (**Cbus**), public speeches at conference, parliament hearings, media mentions (**Future Fund**); constituent information

***REST believes that investment managers that identify and** effectively manage risks, including sustainability risks, are likely to produce super long-term financial performance.*

REST

sessions such as via seminars and work-site visits (**Vision Super** and **Maritime Super**); as well as newsletters and other electronic communications targeting clients (**Vision Super, VicSuper** and **UniSuper**).

LUCRF states that its Contact Centre staff have been trained to answer member calls around all issues concerning their investments, ranging from returns, options and how ESG is integrated into its process. **UniSuper** states that RI issues form part of most member correspondence and over the past year, one article in each newsletter relates to ESG issues, either within **UniSuper** or at investee companies.

26 out of 53 funds (49%) integrate RI into overall promotion (16), make regular and proactive reference to RI (9) or at least refer to RI in promotions annually (1). 17 funds (32%) actively inform stakeholders about the fund's responsible investment activities and performance through two or more communication channels (i.e. website, newsletter, member emails etc.); a further six funds (11%) actively promote RI through one channel only.

With regards to the accessibility of information for stakeholders, 33 out of 53 funds (62%) report their website as the primary source for stakeholders seeking RI information, and 10 funds 19% use the website, as well as other media channels and proactive outreach, to engage their stakeholders.

An additional method of information provision was demonstrated by two funds that designed and delivered roadshows. While it is unclear the extent to which this outreach included RI information, the commitment demonstrated by these two funds in delivering stakeholder outreach is noted.

With regards to broader outreach activity, **Prime Super** reports that in 2016-17 the fund visited 706 towns across all states and territories of Australia, giving 212 presentations and seminars to 2,711 members and their employers. **Queensland Local Government Super** implemented a similarly ambitious community engagement program in Brisbane and regional locations across Queensland.

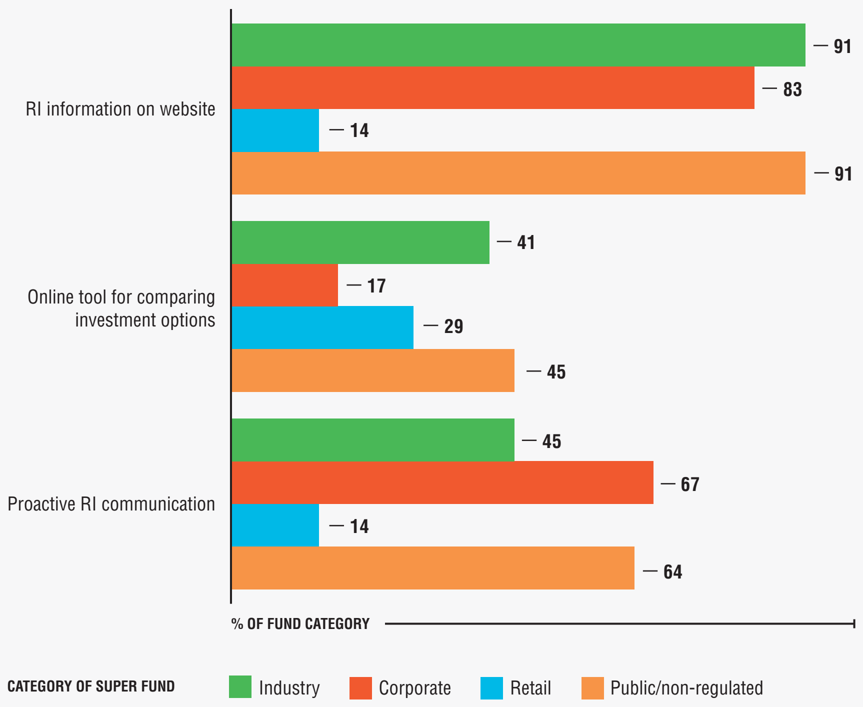
Figure 15 show half of the 53 funds provide RI information on their website. Whilst some funds show a preference for highlighting their RI activities via visibility on primary pages and integration throughout the website as relevant, other funds embedded RI information within less visible areas of the website, making it difficult to find unless via thorough searching for key terms. This is an area where many funds can improve their overall visibility and promotion of RI.

Encouragingly, accessibility of RI information has improved since 2016. In 2018, 37 funds disclose RI information via their website (up from 25 funds in 2016); 19 funds have an online tool for stakeholders to compare investment options (up from 13 funds in 2016); and 23 funds promote RI to stakeholders – an increase of 12 funds, or 21%, from 2016.

Industry funds, and public/non-regulated funds, which have both introduced a greater proportion of fund-wide RI strategies than either corporate or retail funds, demonstrate high levels of accessibility to information via their website and proactive RI communication with clients. Proportionately retail funds offer more online tools for comparing RI options than other fund categories. Again, this may speak to the differences in business models across the fund categories, and possibly to the differing demands of the client base.

The overall improvement in accessibility to information is consistent with the increasing focus on RI from the general public, as consumer and lobby groups have demanded greater transparency from superannuation funds about the ESG impacts of their investments.

FIGURE 15 **ACCESSIBILITY OF RI INFORMATION**



Leading RI super funds 2018

Part of the super fund benchmarking research is to articulate leading practice in responsible investing by super funds in Australia. To achieve this RIAA created a scale – limited, basic, broad and comprehensive – which describes the quality and scope of public disclosures by funds across the Five Pillar Framework and which we published as the Assessment Framework used in the initial *Super Fund Responsible Investment Benchmark Report 2016*.

In 2018, RIAA found 13 out of 53 funds (compared to 12 in 2016) were able to articulate and demonstrate a comprehensive RI approach across the Five Pillars. These 13 funds disclosed RI data that scaled as 'comprehensive' on at least four out of the five pillars in order to gain the final overall scaling of 'comprehensive' in 2018.

Now in its second iteration, RIAA has dissected and identified the common aspects in RI across most of the funds in Figure 16. What follows is a list of the key aspects and the expected level of performance for each in order for funds to demonstrate 'leading practice' within and across the Five Pillars.

For Governance and Accountability

- the fund's investment beliefs are informed by stakeholders (beneficiaries/members/clients) either via trustees as representatives of stakeholders or via systematic and frequent direct engagement;
- the fund has at least a formal, systematic process for measuring RI in alignment with the super fund's strategy;
- accountability for RI is at the highest level of the fund – either the trustee level or an ESG-style sub-committee or dedicated secretariat; and
- successful delivery of RI strategy is considered as part of the satisfactory achievement of staff roles and responsibilities (at least portfolio managers, investment committee and/or board).

For RI Commitment

- the fund's RI strategies apply to a majority of the total FUM and are subject to one or more strategies (i.e. ESG integration, negative screening), across at least four asset classes; and
- the fund participates in at least one collaborative engagement with a view to strengthening the sustainability of the finance system and the broader economy.

For RI Implementation

- the fund and/or investment consultant (if relevant) undertakes a thorough assessment of external manager's ESG capabilities and processes during the manager selection and review processes; at least for managers for listed equities and/or fixed income;
- the fund has explicit external manager reporting requirements relating to RI and ESG activities and performance across all IMAs, for at least some asset classes, such as equities managers; and
- the fund keeps reliable data on the outcomes of company engagements (either direct or via external providers) and reports externally on engagement outcomes.

For Measurement and Outcomes

- the fund has targets in place to measure the success of RI in achieving objectives in at least highly relevant ESG areas, such as alignment with super fund's RI Policy (e.g. incidences of independent voting, successful engagement outcomes), environmental objectives (e.g. a set carbon intensity figure for the portfolio), social objectives (e.g. specific SDGs) and/or governance objectives (e.g. TCFD aligned reporting).

Transparency and Responsiveness

- the fund reports a least annually to external stakeholders on RI activities and performance;
- the fund regularly updates and publishes the list of external managers (where relevant) and its full underlying holdings – directly or indirectly held;
- the fund makes voting records public directly or via a proxy voting service provider; and
- stakeholders' responsible investing interests and service satisfaction are regularly monitored (at least annually) by way of survey for example to assist with measuring success against RI policies and strategies and meeting in the RI expectations of stakeholders.

FIGURE 16 LEADING RI SUPER FUNDS IN 2018

FUND NAME	FUND CATEGORY
Australian Ethical	Retail
AustralianSuper	Industry
Cbus	Industry
Christian Super	Industry
First State Super	Public/non-regulated
Future Fund	Public Sector
HESTA	Industry
Local Government Super	Public/non-regulated
Mercer	Retail
NZ Super Fund	Public/non-regulated
Unisuper	Industry
VicSuper	Public/non-regulated
Vision Super	Public/non-regulated

INDEX OF SUPER FUNDS IN 2018 REPORT: COMMON NAME, RSE, CATEGORY AND NOTES

	NAME IN THE REPORT	RSE NAME	FUND CATEGORY	ADDITIONAL INFO / NOTES
1	AMP Superannuation	AMP Superannuation Limited	Retail	AMP Capital provided responses
2	Australian Catholic Superannuation and Retirement Fund (ACSRF)	SCS Super Pty. Limited	Industry	
3	Australian Ethical	Australian Ethical Superannuation Pty Ltd	Retail	Opt in
4	Australia Post Super	PostSuper Pty Ltd		
5	AustralianSuper	AustralianSuper Pty Ltd	Industry	
6	BT Funds Management	BT Funds Management Limited	Corporate	BT Financial Group provided responses
7	CareSuper	CARE Super Pty Ltd	Industry	
8	Cbus	United Super Pty Ltd	Industry	
9	Christian Super	Christian Super Pty Limited	Industry	Opt in
10	Colonial First State FirstChoice Superannuation	Colonial First State Investments Limited	Retail	
11	Commonwealth Essential Super	Colonial First State Investments Limited	Retail	
12	Colonial Super	Colonial Mutual Superannuation Pty. Ltd.	Retail	
13	Commonwealth Bank Officers Super	Commonwealth Bank Officers Superannuation Corporation Pty Limited	Corporate	
14	Commonwealth Superannuation Corporation	Commonwealth Superannuation Corporation	Public/non-regulated	
15	Energy Super	Electricity Supply Industry Superannuation (QLD) Ltd	Industry	
16	equipsuper	Equipsuper Pty Ltd	Industry	Not including Rio Tinto Staff Fund Pty Limited
17	ESS Super	Emergency Services Superannuation Board	Public/non-regulated	Opt in
18	First State Super	FSS Trustee Corporation		Not accounting for State Super Financial Services
19	Future Fund	Future Fund Board of Guardians (Future Fund Management Agency)	Public/non-regulated	Opt in
20	HESTA	H.E.S.T. Australia Ltd.	Industry	
21	Hostplus	Host-Plus Pty. Limited	Industry	
22	IOOF	I.O.O.F Investment Management	Retail	
23	Local Government Super	LGSS Pty Limited	Public/non-regulated	
24	LGS Queensland	Queensland Local Government Superannuation Board	Public/non-regulated	
25	LUCRF	L.U.C.R.F. Pty. Ltd.	Industry	

26	Maritime Super	Maritime Super Pty Limited	Industry	
27	Media Super	Media Super Limited	Industry	
28	Macquarie	Macquarie Investment Management Ltd	Retail	
29	Mercer	Mercer Superannuation (Australia)	Corporate	Mercer Investments (Australia) provided responses
30	Mine Wealth and Wellbeing	AUSCOAL Superannuation Pty Ltd	Industry	
31	NULIS	NULIS Nominees Australia Pty Limited	Retail	NAB / MLC / Jana provided responses
32	MTAA	Motor Trades Association of Australia Superannuation Fund Pty. Limited	Industry	
33	MyLifeMyMoney	CSF Pty Limited	Industry	
34	Netwealth Super	Netwealth Investments Limited	Retail	
35	NGS Super	NGS Super Pty Limited	Public/non-regulated	
36	NZ Super Fund	Guardians of the New Zealand Superannuation	Public/non-regulated	Opt in
37	Oasis	Oasis Fund Management Limited	Retail	
38	OnePath	OnePath Custodians Pty Limited	Retail	
39	Perpetual	Perpetual Superannuation Limited	Retail	Perpetual Investments provided responses
40	Prime Super	Prime Super Pty Ltd	Industry	
41	Qantas Superannuation	Qantas Superannuation Limited	Corporate	
42	QSuper	Board of Trustees of the State Public Sector Superannuation Scheme	Public/non-regulated	
43	REST	Retail Employees Superannuation Pty. Limited	Industry	
44	Statewide Super	Statewide Superannuation Pty Ltd	Industry	
45	Suncorp Master Trust	Suncorp Portfolio Services Limited	Retail	
46	Sunsuper	Sunsuper Pty. Ltd	Industry	
47	Telstra Super	Telstra Super Pty Ltd	Corporate	
48	Total Risk	Total Risk Management Pty Limited	Retail	Russell Investments provided responses
49	TWU Super	T W U Nominees Pty Ltd	Industry	
50	UniSuper	UniSuper Ltd	Public/non-regulated	
51	VicSuper	Vicsuper Pty Ltd	Public/non-regulated	
52	Vision Super	Vision Super Pty Ltd	Public/non-regulated	
53	Westpac Securities	Westpac Securities Administration Limited	Corporate	BT Financial Group provided responses

APPENDICES REPORT

The Appendices Report is available from RIAA's website here and contains:

1. Questionnaire
2. Project methodology
3. RI approaches over super funds' default and SRI options
4. RIAA's Super Fund RI Benchmark Framework

The Appendices Report is also available upon request from RIAA at info@responsibleinvestment.org

DISCLAIMER

The information contained in this report has been prepared based on material gathered via a desktop research of publicly available information and through an information request to funds in the survey sample (see methodology). The report is intended to provide an overview of RI approaches adopted and being implemented by the largest Australian super funds. The Responsible Investment Association Australasia also scales funds' data found in disclosures, relative to an assessment framework defined by RIAA.

The information in this report is general in nature and does not constitute financial advice. Past performance does not guarantee future results, and no responsibility can be accepted for those who act on the contents of this report without obtaining specific advice from a financial adviser. RIAA does not endorse or recommend any particular firm, fund manager or super fund to the public.

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