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TEN STRATEGIES FOR PENSION FUNDS TO BETTER SERVE THEIR BENEFICIARIES

Keith Ambachtsheer and Rob Bauer

Conclusions from a workshop on Sustainable Capitalism
organized by Rotman International Centre for Pension Management
in collaboration with The Generation Foundation

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PART 1: WORKSHOP CONTEXT, DESIGN, AND CONCLUSIONS

Workshop Context and Design

The tagline of the Rotman International Centre for Pension Management (ICPM) is “better pension design...better pension management”. The Centre fosters these aspirations through research funding, its semi-annual journal and discussion forums, and through its week-long board effectiveness education program. Based at the Rotman School of Management, University of Toronto, its programs are wholly funded by 40 major thought-leading pension organizations from 12 countries. Last year, ICPM began to explore opportunities with other organizations judged to have synergistic ‘1+1=3’ collaboration potential with it.

This outreach initiative led to discussions with The Generation Foundation (GF). The Foundation is funded by Generation Investment Management, an investment firm founded by former US Vice President Al Gore and investment banker David Blood. The aim of the Foundation is to foster sustainable capitalism as laid out in the widely-cited 2012 White Paper titled “Sustainable Capitalism”. Specifically, the Paper proposed five action steps asset owners, asset managers, and company boards and executives could take for the benefit of their own stakeholders, that would at the same time promote ‘the greater good’ by fostering longer horizon thinking and acting in financial markets.

The ICPM-GF discussions led to a 1½-day workshop design which would see the five White Paper action steps explained, discussed, and debated on the first day, and then converted into feasible implementation strategies the following morning. The event took place on June 4-5 2013 at the Rotman School of Management, University of Toronto with some 80 board members, senior executives, and investment professionals from the 40 ICPM-sponsoring organizations, as well as a number of additional guests from other interested organizations, actively participating during various parts of the process.

In summary, each of the five White Paper action steps was subjected to a six-step protocol:

<u>Tuesday</u>

1. Two lead-off presentations for each topic by acknowledged subject experts
2. Small-group discussions for each topic with report-outs
3. General discussion for each topic based on the small-group report-outs

<u>Wednesday</u>

4. Small-group assignments to create own-fund and collective action implementation plans for each of the five action steps
5. Small-group own-fund and collective action implementation recommendations followed by general discussion
6. Impact/feasibility assessment by each workshop participant for each implementation recommendation

This document summarizes the Tuesday topic presentations and discussions, as well as the implementation conclusions reached by the small-groups on Wednesday. The summaries are based documentation collected during the process, as understood/interpreted by workshop moderators Keith Ambachtsheer, Director of Rotman ICPM and Rob Bauer, Associate Director of Rotman ICPM Programs.

See Appendix A for a listing of Participating Organizations, and Appendix B for Moderator and Speaker Bios.

Healthy Doses of Scepticism

Though it might sound strange, the most helpful element in the room over the course of the 1½ days may well have been healthy doses of scepticism about the value and feasibility of at least some of the proposed five action steps in the White Paper. For example, one attendee observed that the 'real world' and 'responsible' investor crowds usually live in parallel universes, attending separate events often designed to re-enforce their own strong pre-conceptions. Such an 'either or' state of affairs is not conducive to constructively challenging those pre-conceptions.

In contrast, the ICPM-GF workshop offered opportunities for people to examine the basis of their current beliefs about issues ranging from investment horizon choice, to stranded asset risks, to material information disclosure, to compensation structures. The subtleties embedded in these issues are too often left unexamined. Sometimes, when these subtleties are taken into account, things which may have seemed obvious, are no longer so. Or, alternatively, apparent differences of opinion sometimes turn out to be nothing more than different understandings of the meaning of a word or a phrase. Such interactions can move 'either or' thinking to 'and and' thinking.

While it would be naive to assert that all workshop participants were lustily singing from the same song sheet by Wednesday noon, we do believe the experience raised the collective understanding of what the five action proposals (and their interconnectedness) were really about, and how they might best be implemented.

The Five Action Steps Proposed in the 'Sustainable Capitalism' White Paper

Former Vice President of the United States, Al Gore, opened the workshop on June 4 with a review of the essential messages set out in the "Sustainable Capitalism" White Paper, published in February 2012. His partner David Blood ended the day with concluding observations and comments on the day's discussions, debates and deliberations. They noted that some of the original White Paper action recommendations had evolved over since their original publication, based on subsequent research findings. The five action steps presented to workshop participants on June 4 for discussion and debates, including the lead-off speakers were:

- Addressing Stranded Asset Risks – Bob Litterman and Mark Fulton
- Embracing Integrated Reporting – George Serafeim and Anita McGahan
- Ending the Default Practice of Quarterly Earnings Guidance – Judith Samuelson and Eric Wetlaufer
- Rethinking Executive Compensation Structures – Roger Martin and Stephen Brown
- Promoting Constructive Investor Behaviour – Jane Ambachtsheer and George Buckley

Rotman colleague David Beatty led off June 5 with an explanation of the protocol to be followed in reaching consensus on actual implementation plans. In order to create as realistic a setting as possible, we split the participants into small groups and gave them concrete assignments. In each case, we asked the group to think about what micro actions their own pension organization might take internally, and what collective macro action they would propose for their fund to participate in with one or more larger industry, national, or international collaborations.

Summary of the Five Own-Organization Action Recommendations

Here are the five micro action recommendations workshop participants came up with for consideration within their own pension organization (with some editing to enhance clarity):

1. Stranded Asset Risks Recommendation: *Undertake an in-house project aimed to raise the understanding of the stranded asset risks issue at both the Board and management levels.*
2. Integrated Reporting Recommendation: *Commence and advocate the adoption of <IR> both for reporting our own organization's results and for assessing the long horizon prospects of our investments.*
3. Quarterly Earnings Guidance Recommendation: *Focus discussions on yearly results in 1-on-1 meetings between investors and corporate managements.*
4. Compensation Structure Recommendation: *Think carefully about how to best exercise our shareholder rights in order to foster effective compensation practices.*
5. Investor Behavior Recommendation: *Design and implement concentrated long horizon investment mandates, and ensure that we have the necessary resources to successfully implement them.*

Summary of the Five Collective Action Recommendations

Here are the five macro action recommendations workshop participants came up with for consideration in collaboration with other national or international institutional investor organizations (again, with some editing to enhance clarity):

1. Stranded Asset Risks Recommendation: *Seek out effective collaborations with like-minded organizations to best manage the climate change issue and its potential investment-related impacts.*
2. Integrated Reporting Recommendation: *Ensure that we are fully informed about the evolution of the <IR> initiative, and that our own organization is in line to become an early adopter.*
3. Quarterly Earning Guidance Recommendation: *Call for a joint declaration by professional investment associations (e.g., the CFA Institute) that analysts should not pressure corporations to provide quarterly earnings guidance.*
4. Compensation Structure Recommendation: *Collaborate to achieve consistent regulations on executive compensation that have enforceable consequences for corporate Boards.*
5. Investor Behavior Recommendation: *Develop a 'model investment mandate' through an organization like ICPM that can be widely shared and reported on by investors.*

Readers will immediately note that some of the recommendations are quite concrete, while others are less so. This is no doubt in part due to the pressures of time that we imposed on the small-group problem solvers. We offer more detailed comment on the recommendations in the following pages.

PART 2: ADDRESSING STRANDED ASSET RISKS

Initial Presentations and Discussion

Bob Litterman and Mark Fulton led off the stranded asset risks discussion. While the stranded asset risk concept has broad applicability in both private and public markets, they focused mainly on the potential impact of climate change on asset pricing in public markets.
Bob Litterman Presentation
Mark Fulton Presentation

Their key messages included the following:

- Fossil fuel consumption is still subsidized today to the tune of $16/metric ton of CO2.
- The subsidy will eventually disappear and CO2 emissions will be priced. We don't know the time path of this transformation, just as we don't know the time path of global warming.
- We need to distinguish between the expected damages of global warming (e.g., rising sea levels, stronger storms, droughts, floods, degradation of ecosystems) and the risks (e.g., positive feedbacks, tipping points, time compression, geo-political events, etc.).
- Delays in CO2 emissions pricing raises the price point needed to control global warming, and increases the risk of catastrophic outcomes. This is a serious intergenerational issue.
- Could China's severe air quality problems lead to acceleration in carbon pricing? Even emission capping?
- Negative valuation impact of carbon pricing is greatest in construction materials, followed by utilities, metals and mining, transportation, chemicals, fossil fuels, and forest products. Also, the power of reputational risks should not be underestimated.
- On a more positive note, global warming also creates promising investment opportunities which should not be ignored.

The subsequent discussion period made it clear that a considerable proportion of the workshop attendees continue to struggle with the complexity and timing uncertainty attached to the global warming issue and its investment implications. One commentator even asked 'what if the scientists are wrong about all this?' Another expressed view was that this was a long horizon issue that will someday become a short horizon issue. We just don't know when. In the end, the room arrived at a constructive resolution. See below.

The Assignment: Addressing Stranded Asset Risks

- Pension Fund X has never addressed stranded asset risks as part of its investment policies and processes.
- You have been asked by the Board of Trustees to advise them on whether they should be concerned about this lack of attention.
- What advice do you have for the Board? If you think it is an important issue, how should Pension Fund X address it?
- Are there broader industry-wide changes (e.g. disclosure-related) that Pension Fund X should collaborate on with its Peers?

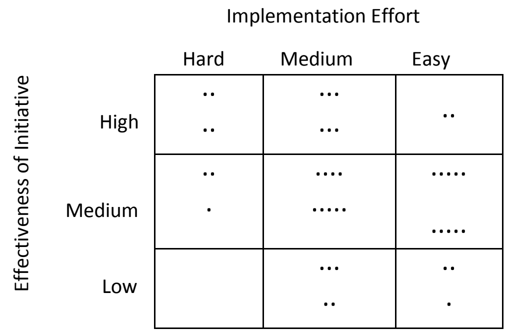
The responses to the assignment follow, as do assessments of the potential impact of the recommendation, and of its ease/difficulty of implementation.

Stranded Assets: Own-Organization Recommendation and Supporting Reasons

Recommendation:
Undertake an in-house project aimed to raise the understanding of the stranded asset risks issue at both the Board and management levels.

Reasons:
1. Understanding the issue is consistent with good risk management practices.
2. A better understanding of the issue will lead to a higher level of conviction in how to best deal with it.
3. Our organization exposes itself to reputational risk if it ignores the issue.

Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation



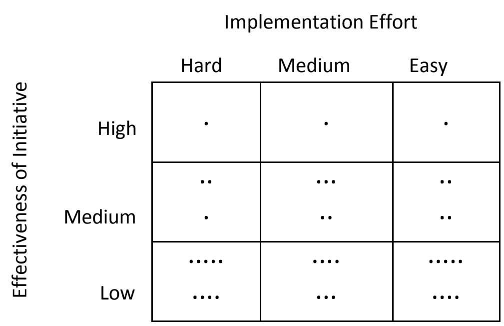
The scatter of the dots suggests relatively few workshop attendees judged the recommendation to be difficult to implement. Similarly, relatively few thought that its effectiveness as a means to raise understanding of the stranded assets risk issue within the organization would be low. So this recommendation has promise.

Stranded Assets: Broader Collaborative Recommendation and Supporting Reasons

Recommendation:
Seek out effective collaborations with like-minded organizations to best manage the climate change issue and its potential investment-related impacts.

Reasons:
1. It is a global problem requiring global action.
2. Understanding and dealing with complexity needs multiple perspectives.
3. Effective collective action will require multiple players (e.g., legislators, regulators, NGOs, investors).

Assessment of Potential Impact and Ease/Difficulty of Implementation/Effectiveness



While there was a diversity of opinion on whether this broad collaboration recommendation was easy or difficult to implement, there was broad consensus that the prospects for it to be effective and have major global impact would be challenging.

Ambachtsheer-Bauer Commentary

Climate change and its host of related challenges constitute a complex set of issues for long-horizon investors. As a result, it is tempting to skip over them and move on to something simpler. So the workshop participants' recommendation to consciously choose to raise the level of own-organizational awareness and understanding of the issue as a first step is right on the mark. It truly reflected 'the wisdom of the crowd' in what had been a challenging, difficult discussion. Also, logically, for any pension organization to collaborate effectively with others on climate change issues, it must develop and adopt a clear organization stance for itself first.

PART 3: EMBRACING INTEGRATED REPORTING OF ORGANIZATIONAL PERFORMANCE

Initial Presentations and Discussion

George Serafeim and Anita McGahan led off the integrated reporting discussion. The integrated reporting initiatives underway (<IR> and SASB) constitute a global movement towards combining material financial and non-financial information about any commercial or non-commercial organization in a single document. This document is intended to be a platform for a common two-way conversation with all of the organization's stakeholders. A unique element of this new integrated approach is to connect the organization's capital resources (i.e., physical, natural, financial, intellectual, human, and social) to the organization's outcomes (i.e., products/services, financial returns, externalities).

This is an idea whose time has come:

- A single document reporting an organization's performance in an integrated, multi-dimensional fashion
- Explicit recognition of materiality
- Levering the Internet to improve dialogue and engagement with all stakeholders
- Instigating global dialogues
- A transition mechanism from the mainly financial-only reporting of today to a more comprehensive form of reporting consistent with the society we want tomorrow
- Clearer examination of tradeoffs, innovation, and sources of productivity
- Fostering inclusive governance

Reaping these benefits requires overcoming material conceptual (e.g., sparseness, comparability), procedural (e.g., global adoption), and societal (e.g., resisting gamesmanship) challenges.

The Assignment: Embracing Integrated Reporting

- Senior management at Fund X has just listened to a presentation on the Integrative Reporting Initiative. The CEO has asked for the team's opinion on how seriously the fund should take the <IR> Initiative.
- What is your response? If the Initiative should be taken seriously, what can the Fund itself do to further the cause?
- Are there broader national or international collaborations it should consider joining?

The responses follow, as do assessments of the potential impact of the recommendation, and of its ease/difficulty of implementation.

Integrated Reporting: Own-Organization Recommendation and Supporting Reasons

Recommendation:
Commence and advocate the adoption of <IR> both for reporting our own organization's results and for assessing the long horizon prospects of our investments.

Reasons:
1. It provides our own stakeholders (e.g., plan participants) with a comprehensive view of our activities, and a clearer collective view of how we achieve our mission.
2. It enhances our long term return prospects through greater transparency about the sustainability of the companies we invest in.
3. It provides a more formal structure within which to carry out our 'due diligence' processes both in our own pension business, as well as in relation to the companies we invest in.

Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	.	.. .	.. ..
Medium	... .	....	..
Low	..	.. .	.. ..

The scatter of the dots indicates many workshop attendees believed implementing this recommendation would be challenging. Most thought its effectiveness impact would be in the medium range.

Integrated Reporting: Broader Collaborative Recommendation and Supporting Reasons

Recommendation:
Ensure that we are fully informed about the evolution of the <IR> initiative, and that our own organization is in line to become an early adopter.

Reasons:
1. Involvement in the process will provide insight in new ways to assess our investments.
2. Involvement with <IR> experts and regulators ensures we are driving forthcoming changes.
3. Involvement will help us rethink performance benchmarks from an <IR> perspective.

Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	.	....	..
Medium	...	....	....
Low	.	.. .	..

This plot looks encouraging, with a good many dots in the 'high effectiveness/medium effort' and 'medium effectiveness/easy effort' spaces.

Ambachtsheer-Bauer Commentary

The International Integrated Reporting Initiative and SASB have come a long way since they got off the ground a few years back. While many workshop participants were at least somewhat familiar with the initiatives, and understood its potential analytical benefits from a long horizon institutional investor perspective, a higher level of awareness is needed. Only a small number of participants had come to the (obvious?) realization that pension organizations themselves should embrace the integrative reporting philosophy in engaging their own stakeholders in effective two-way conversations.

PART 4: ENDING THE DEFAULT PRACTICE OF QUARTERLY EARNINGS GUIDANCE

Initial Presentations and Discussion

Judith Samuelson and Eric Wetlaufer led off the discussion on the practice of providing quarterly earnings guidance. The problem with this practice is that it can create incentives for corporate executives to manage for the short term. It also encourages some investors to focus on quarterly results rather than on longer term value creation. The practice has become the fodder of business and investment news shows, producing subject matter for daily dialogue on these programs. It also provides the fuel for short term trading strategies based on whether reported quarterly earnings come in above or below the guidance numbers.

Despite these problems, the practice continues to have its defenders. Selected (sometimes disingenuous) feedback from corporate Investor Relations departments:

- “Dropping short-term earnings guidance will lead to lower market valuation and higher volatility.”
- “In today’s markets, short-term pressures are more powerful than the interests of long term investors.”
- “Providing short-term guidance demonstrates commitment to creating shareholder value.”
- “Providing short-term guidance helps us build credibility in the markets.”
- “Analysts demand short-term guidance, so we have to give it to them.”
- “Dropping earnings guidance will signal to markets that we do not value transparency.”
- “We have a system in place to collect and disseminate short-term guidance. Creating a new system to support long-term communications will be costly and time-consuming.”

The obvious counterpoint to the critics of current short-term earnings guidance practices is that nothing requires long-horizon investors to pay any attention to these practices.

The Assignment: Ending Default Short-Term Earnings Guidance

- Fund X has created a task force to lengthen the time-horizon for making investment decisions.
- How do you think this task force should deal with the still-common practice of providing quarterly earnings guidance?
- If you believe the practice fosters short-term thinking and unnecessary price volatility, what is the best way to change the practice?
- Address this question both in the Fund X context, and in the broader national and international contexts.

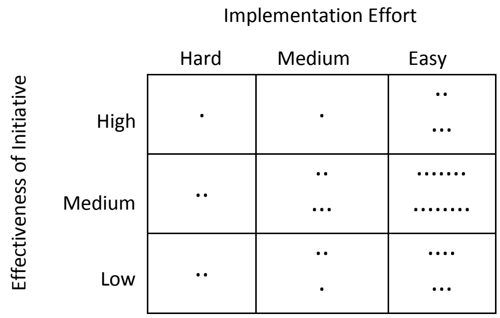
The responses follow, as do assessments of the potential impact of the recommendation, and of its ease/difficulty of implementation.

Default Earnings Guidance: Own-Organization Recommendation and Supporting Reasons

Recommendation:
Focus discussions on yearly results in 1-on-1 meetings between investors and corporate managements.

Reasons:
1. Yearly is standard.
2. Takes pressure off corporate managements to be short-term.
3. Discussing quarterly results is an unproductive use of time.

Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation



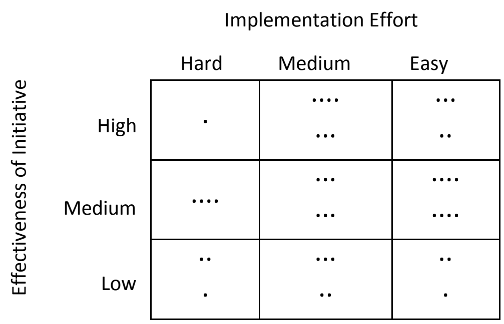
There was broad agreement this recommendation was easy to implement. Most participants also thought that the effectiveness of the action was at least in the medium range.

Default Earnings Guidance: Broader Collaborative Recommendation and Supporting Reasons

Recommendation:
Call for a joint declaration by professional investment associations (e.g., the CFA Institute) that analysts should not pressure corporations to provide quarterly earnings guidance.

Reasons:
1. Takes pressure off corporations to worry about short-term results.
2. Annual reporting is the global standard.
3. It signals that only longer-term results count.

Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation



There was reasonable consensus in the direction of both implementation effectiveness and implementation ease for this recommendation.

Ambachtsheer-Bauer Commentary

An important aspect of this default practice of providing quarterly earnings guidance is that it is fairly USA-centric. Given that most workshop participants were not American, the modest consensus towards both effectiveness and ease-of-implementation on the broader collaborative recommendation is not a surprise. We should definitely relay the broader collaborative recommendation to the CFA Institute for their consideration. More generally, the mood of the meeting was to move towards richer, more productive conversations between investors and corporations. Some of the other recommendations in this report speak to this desire as well.

PART 5: RETHINKING EXECUTIVE COMPENSATION STRUCTURES

Initial Presentations and Discussion

Roger Martin and Stephen Brown were the kick-off speakers for this session. In describing and assessing current corporate executive compensation arrangements, the word 'puzzled' was used more than once. The speakers, and many of the workshop attendees, had difficulty understanding why and how the generally rich, stock-based compensation arrangements of today would motivate executives to create sustainable long term value in their corporations. Indeed, one of the attendees, a recently-retired CEO of a major global corporation, confirmed that his stock-based compensation scheme was not a major motivator in the strategic decisions he made during his seven years at the helm.

So what do we make of a world where there is no obvious connection between executive performance and the level and structure of executive compensation? How did we get here? Reference was made to a self-generating 'club effect', where individual compensation is determined by the collective compensation levels and structures of the 'CEO club' the individual belongs to. In other words, there is an implicit understanding that if a Board wants to attract and retain the right CEO, it must be willing to pay that CEO 'competitively' in relation to the pay packages of other CEOs of corporations if similar size in similar industries. These embedded rules of the game make it challenging for institutional investors to materially impact the levels and structures of executive compensation.

The Assignment: Rethinking Executive Compensation Structures

- Fund X is receiving increasing pressure by plan members to have and communicate the Fund position on executive compensation practices in the companies in which it invests.
- Your task force mandate is to articulate what that position is.
- How would you state it, and how do you incorporate it into your own fund's investment policies and practices?
- What kind of broader collaborative strategies are most likely to have a positive impact?

The responses follow, as do assessments of the potential impact of the recommendation, and of its ease/difficulty of implementation.

Executive Compensation Structures: Own-Organization Recommendation and Supporting Reasons

<u>Recommendation</u>:
Think carefully about how to best exercise our shareholder rights in order to foster effective compensation practices.

<u>Reasons</u>:
1. Our fiduciary duties require this of us.
2. Effective compensation practices will foster long term value creation.
3. We must signal our concerns to corporate boards and management in a visible manner.

<u>Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation</u>

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	••	••• •••	••• •••
Medium	•••	•••	•••• ••••
Low	•	••• •••	••• •••

There was broad agreement this recommendation was relatively easy to implement, but there was a lack of agreement on its potential effectiveness.

Executive Compensation Structures: Broader Collaborative Recommendation and Supporting Reasons

<u>Recommendation</u>:
Collaborate to achieve consistent regulations on executive compensation that have enforceable consequences for corporate Boards.

<u>Reasons</u>:
1. Enforceable consequences are needed to get Boards to move on compensation.
2. Consistency needs to be a key part of the message.
3. Global consensus by institutional investors will carry weight.

<u>Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation</u>

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	••••• ••••	••••• •••••	•••• •••
Medium	••• •••	••	••• •••
Low	••		

There is significant consensus that this is a 'high impact' initiative. There is less consensus on its degree of implementation ease/difficulty.

Ambachtsheer-Bauer Commentary

Arguably, the current executive compensation situation constitutes a 'market failure' situation in the sense that there is no obvious relationship today between executive performance and the levels and structures of executive compensation. So the sense in the room that a strong, coherent collective action initiative is needed is on the mark. Further, the sense that the outcome should be a coherent, internationally-consistent regulatory regime with enforceable consequences for corporate Boards also seems on the mark. Another implication of the current state of affairs is that considerable effort should be devoted to the design and implementation of logical, internally-consistent executive compensation schemes that do promote long horizon value creation. Finally, again, what is good for the goose is good for the gander: pension funds need to ask themselves how well their own compensation schemes align desired outcomes and incentives.

PART 6: PROMOTING CONSTRUCTIVE INVESTOR BEHAVIOR

Initial Presentations and Discussion

Jane Ambachtsheer and Sir George Buckley offered opening remarks. Issuing some form of 'loyalty reward' to long horizon shareholders was proposed in the "Sustainable Capitalism" White Paper. Subsequent research suggests that loyalty rewards (e.g., extra voting rights, extra dividends, special warrants) are likely to be problematic in fostering productive long horizon investing for a number of reasons (e.g., discrimination between shareholders, entrenchment problems, administrative complexities, weak incentives). Maybe most importantly, loyalty rewards may not require investors to be thoughtful stewards of capital.

It may be better to focus on the investment supply chain and ensure that alignment exists from one end of the chain to the other. Specifically, focus on the relationship between investors and their investments:

- What should pension plan participants require from their pension organization?
- What should the pension organization require from its internal and external investment managers?
- What should these investment managers require from the companies they invest in?
- And what should the companies require from these investment managers?

Arguably, the answers to these four questions will be important determinants of the future course of capitalism.
Jane Ambachtsheer Presentation

The Assignment: Promoting Constructive Investor Behavior

- You are members of an investment industry task force created to promote engaged ownership of publicly-traded corporations.
- What is your view on corporations rewarding long-term shareholders with increased influence through extra voting rights? Or through additional dividends or warrants?
- At the Fund level, what can investors do to encourage companies to focus on longer-term value creation?
- Are there regulatory, legal or industry initiatives which might incentivise (or mandate) a longer-term value-creation mindset by investors? By publicly-traded corporations?

The responses follow, as do assessments of the potential impact of the recommendation, and of its ease/difficulty of implementation.

Investor Behavior: Own-Organization Recommendation and Supporting Reasons

<u>Recommendation</u>:
Design and implement concentrated, long horizon investment mandates, and ensure that we have the necessary resources to successfully implement them.

<u>Reasons</u>:
1. Our own longer term thinking will support longer term thinking in our investee corporations.
2. It better aligns our organization's goals with those of our own stakeholders.
3. It will reduce our transaction costs.

<u>Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation</u>

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	... ...	....	.. ...
Medium	.. ...	....	.. ..
Low	.		

This recommendation was seen as a potentially high-impact initiative. There were mixed views on how easy or difficult it would be to implement.

Investor Behavior: Broader Collaborative Recommendation and Supporting Reasons

<u>Recommendation</u>:
Develop a 'model investment mandate' through an organization like ICPM that can be widely shared and reported on by investors.

<u>Reasons</u>:
1. It will lever existing knowledge through collaboration.
2. It will force the development of new performance measures and incentive compensation schemes.
3. It will challenge the dysfunctional inertia that continues to exist in many pension organizations.

<u>Assessment of Potential Impact/Effectiveness and Ease/Difficulty of Implementation</u>

Implementation Effort

Effectiveness of Initiative	Hard	Medium	Easy
High	.. ..	.. ...	.. ...
Medium	.. ...	.. .	.. ...
Low	.. .	.. .	.. ...

There was no consensus in the room on either the potential impact of this recommendation, or on its degree of implementation ease/difficulty.

Ambachtsheer-Bauer Commentary

The key concept here is the broad adoption of 'concentrated long term investment mandates' that require investor engagement. This would be a radical departure from the traditional Keynesian 'beauty contest' style of active management, and also from the broadly-diversified 'formula' style of passive management. A high number of workshop participants judged this to be a potentially high-impact initiative at the individual fund level. A number of practical implementation issues would have to be addressed (e.g., risk-related, relationship management-related, asset size-related). Nevertheless, there was agreement that wide adoption of this investment approach would constitute a major step towards the sustainable form of capitalism envisioned in the Generation White Paper.

PART 7: CONCLUDING THOUGHTS

The Medium as the Message

University of Toronto philosopher Marshall McLuhan once observed that "the medium is the message". The ICPM-GF collaboration captured in this document illustrates McLuhan's point nicely. The medium of collaboration has produced important messages about where we should take the 5 recommended steps in the GF White Paper from here.

One of those messages is that well-planned, well-executed collaborations (e.g., the ICPM-GF collaboration) can indeed produce '1+1=3' outcomes. That same message can once again be applied to the five macro collaboration recommendations that came out of the workshop. Each of these collaboration recommendations will require further discussion, careful planning, and strong execution before it can become a reality. We note here that ICPM is funding research on the theory of optimal collaboration models and on related validating empirical work and case studies. We also note that the challenge of building effective collaboration strategies from here is more about organizing already-existing organizations into '1+1=3' collaborations, than it is about building entirely new ones.

Another message is that pension organizations must walk the talk themselves if they are to be credible collective action mediums. Recall that for each of the original five action step recommendations in the White Paper, workshop participants were asked to think carefully about what each pension organization should be doing on the inside to move the yardsticks in the right direction. Doing so will re-enforce the connectedness of the five action steps, and foster the understanding and conviction required for effective participation in the collective action initiatives identified in the workshop.

A Commitment and an Invitation

We conclude by encouraging the people and organizations who participated in this historic workshop to follow through on the five micro and five macro action steps they worked so hard to produce. We at Rotman ICPM commit to assess the degree to which the ten action steps are being implemented and having 'real world' impact, in the not too-distant future.

In the meantime, we invite your comments and suggestions on this work.

We look forward to hearing from you.

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APPENDIX A

PARTICIPATING ORGANIZATIONS

Worldwide
Global Risk Institute In Financial Services (GRIFS)
Mercer
UN Principles for Responsible Investment (UNPRI)
World Bank

Australia
Catholic Superannuation Fund
QSuper
Queensland Investment Corporation (QIC)
SunSuper

Canada
Alberta Investment Management (AIMCo)
Alberta Local Authorities Pension Plan (ALAPP)
British Columbia Investment Management (bcIMC)
Caisse de dépôt et placement du Québec
CEM Benchmarking
CPP Investment Board (CPPIB)
Healthcare of Ontario Pension Plan (HOOPP)
Ontario Ministry of Finance
Ontario Municipal Employees' Retirement System (OMERS)
Ontario Teachers' Pension Plan (OTPP)
Public Sector Pension Investment Board (PSP)
Rotman School of Management, University of Toronto
York University

Denmark
Danish Labour Market Supplementary Pension (ATP)

Finland
Finland State Pension Fund / Valtion Eläkerahasto
Ilmarinen

France
Etablissement de Retraite Additionelle de la Fonction Publique (ERAFP)

Japan
Nomura Research Institute

Korea
NPS Korea

Netherlands
ABP
Algemene Pensioen Groep (APG)
Cardano
De Nederlandsche Bank (DNB)
Maastricht University
MN
Ownership Capital
PGGM
Syntrus Achmea

New Zealand
New Zealand Superannuation Fund

South Africa
Government Employees Pension Fund (GEPF)

United Kingdom
BT Pension Scheme Management (BTPS)
Generation Investment Management
National Employment Savings Trust (NEST)
Railways Pension Trustee Company (RPMI)
Universities Superannuation Scheme (USS)

United States
The Aspen Institute
California Public Employees Retirement System (CalPERS)
Commonfund
Generation Foundation
Harvard Business School
MSCI Barra
State of Washington
TIAA-CREF Investment Management
Washington State Investment Board (WSIB)

APPENDIX B

MODERATOR AND SPEAKER BIOS

Jane Ambachtsheer
Partner, Global Head of Responsible Investment, Mercer

Jane Ambachtsheer is Partner at Mercer and their leads global responsible investment business. Jane helped to establish this group in 2004, which assists investors in considering environmental, social and governance factors within investment decision-making and governance processes. Jane advises investors in North America, Europe and Asia Pacific, and is actively involved in a number of industry initiatives. She was consultant to the United Nations through the development of the Principles for Responsible Investment, which has now been signed by more than 700 investors worldwide. Jane is also a global advisor to the Carbon Disclosure Project and sits on the investment committee of the Toronto Atmospheric Fund. Jane is the 2011 recipient for the SIO's Canadian SRI Lifetime Achievement Award which recognizes those committed to the promotion of ESG in the Canadian investment space. Jane is an Adjunct Professor at the University of Toronto, where she teaches a graduate course on responsible investment. She holds a Bachelor of Economics and English literature with honours from York University, and a Master of Social Science from the University of Amsterdam.

Keith Ambachtsheer
Director, Rotman ICPM, Rotman School of Management, University of Toronto

Keith Ambachtsheer is Director of the Rotman International Centre for Pension Management (ICPM), Adjunct Professor of Finance, Academic Director of the Rotman-ICPM Board Effectiveness Program, and Publisher and Editor of the Rotman International Journal of Pension Management. His firm, KPA Advisory Services Ltd., has provided advice to governments, industry associations, pension-plan sponsors, foundations and other institutional investors since 1985. He is the co-founder of CEM Benchmarking Inc. which monitors the performance of 300 pensions worldwide. Keith has authored three books on pension management. He has received numerous industry awards, including EBRI's Lillywhite Award for "outstanding service enhancing Americans' economic security", and the CFA Institute's James R. Vertin Award for "producing a body of research notable for its relevance and enduring value", and its Professional Excellence Award for "exemplary achievement and true leadership within the profession".

Rob Bauer
Professor of Institutional Investors
Faculty of Economics and Business Administration, Maastricht University

Rob Bauer is Professor of Finance (Chair: Institutional Investments) at Maastricht University, School of Business and Economics in the Netherlands. He is also Managing Director of an investment consulting firm in which he advises pension funds and institutional asset managers on pension and investments related subjects. His present academic research focus is on pension funds, mutual funds, behavioral finance, socially responsible investments (SRI) and corporate governance. His academic work has been published in various professional and academic (international) research journals. Rob is Associate Director, Programs, of the Rotman International Centre for Pension Management (ICPM) at the University of Toronto, Director of the Netspar-UM SBE Academy and Director of the European Centre for Corporate Engagement (ECCE) at Maastricht University. Rob is also a Senior Researcher with Netspar. Moreover, he teaches at various executive courses around the world.

David Beatty
Director, Clarkson Centre for Business Ethics, Rotman School of Management, University of Toronto

David Beatty is an experienced businessman in Canada and abroad. He spent a decade managing one of North America's largest food companies. Over his career he has served on 30 different boards in Canada, America, Mexico, Australia and England and been chairman of seven public companies. Today he serves as Director of Walter Energy (a global metallurgical coal producer) and FirstService Corporation as well as being a member of the board of the privately-held Canada Steamships Line. He was the founding Managing Director of the Canadian Coalition for Good Governance (2003-2008), an organization that represents 50 institutional investors with ~C$1,300 billion of assets under management. David is a Professor at the Rotman School of Management, Universty of Toronto where he teaches corporate strategy and corporate governance. David served on Peter Drucker's Foundation Board in the United States for over a decade, the last few years as Vice Chairman. Her Majesty Queen Elizabeth II inducted him as an Officer of the Most Excellent Order of the British Empire (O.B.E.) in 1994 at Buckingham Palace. He has also been awarded the Papua New Guinea Independence medal, the Papua New Guinea Independence 30th Anniversary Commemorative medal and the Queen Elizabeth 60th Anniversary Jubilee medal.

David Blood

Managing Partner, Generation Investment Management

David Blood is co-Founder and Senior Partner of Generation Investment Management. Previously, he spent 18 years at Goldman Sachs including serving as co-CEO and CEO of Goldman Sachs Asset Management from 1999-2003. David received a B.A. from Hamilton College and an M.B.A. from the Harvard Graduate School of Business. He is on the Board of Harvest Power, New Forests, SHINE, Social Finance UK, Social Finance US, The Nature Conservancy, Fondation Lombard Odier and Hamilton College; as well as on the Advisory Board of Bridges Ventures and the Harvard Business School Visiting Committee.

Stephen Brown

Senior Director of Corporate Governance and Associate General Counsel / Advocacy and Oversight

TIAA-CREF Investment Management

TIAA-CREF is a full-service financial services group of companies with over $500 billion assets under management. Since 2011, Stephen has been named by the National Association of Corporate Directors as one of the 100 most influential people in corporate governance and the boardroom. In 2009, Mr. Brown was named as one of 10 global Rising Stars of Corporate Governance by the Yale School of Management's Millstein Center for Corporate Governance and Performance. Prior to joining TIAA-CREF, Mr. Brown practiced corporate and securities law with WilmerHale and Skadden and was a financial analyst with Goldman Sachs. Mr. Brown is an Adjunct Professor at Yale University and City College of New York. Mr. Brown's pro bono practice has included advising several education related public entities and economic development organizations. He has served on the boards of the Englewood, N.J. public schools, Queens Economic Development Corporation, Harlem Renaissance Economic Development Corporation and the Public Interest Law Foundation at Columbia University Law School. Stephen received his B.A. from Yale University and his J.D. from Columbia University Law School where he was a Harlan Fiske Stone Scholar and an Olin Law & Economics Junior Fellow.

Sir George Buckley

Former Chairman and CEO, 3M Company

Sir George Buckley is the Chairman of Ownership Capital, an independent, long-horizon investment management firm based in Amsterdam. At Ownership Capital, Sir George is responsible for engaging with investee companies and advising on new investment opportunities. Prior to joining Ownership Capital, Sir George was Chairman, President and CEO of 3M from 2005-2012, where he was credited with re-igniting the company's famous innovative culture. Prior to that, Sir George was Chairman and CEO of Brunswick Corporation from 2000-2005. He also held senior general management roles at Emerson and British Railways. Sir George is a Member of the Board of Directors of PepsiCo, Hitachi, Archer Daniels Midland, Stanley Black & Decker, and Technogym. He is also Chairman of Arle Capital LLP and Expro International. He sits on the Americas Advisory Board for Deutsche Bank and the Advisory Board for Rothschild North America.

Mark Fulton

Director, SustainableEye

Mark Fulton has 35 years experience in financial markets as an economist, strategist, head of research and manager spanning three continents in London, New York and Sydney. Mark was head of research at DB Climate Change Advisors at Deutsche Bank from 2007 to 2012, where he produced thought leadership papers for investors on climate, cleaner energy and sustainability topics and advised investment teams in asset management. Mark is currently advising on sustainability issues and is Director of SustainabilityEye. Mark has a BA in Philosophy & Economics from Oxford University.

Al Gore

Former US Vice President and Chairman, Generation Investment Management

Former US Vice President Al Gore is co-Founder and Chairman of both Generation Investment Management and Current TV. He is also a Senior Partner at Kleiner Perkins Caufield & Byers, and a Board member of Apple, Inc. Gore spends the majority of his time as Chairman of TheClimate Reality Project, a non-profit devoted to solving the Climate Crisis. Gore was elected to the U.S. House of Representatives four times and the U.S. Senate twice. He served eight years as Vice President. He authored the bestsellers Earth in the Balance, An Inconvenient Truth, The Assault on Reason, and Our Choice. He is co-recipient of the 2007 Nobel Peace Prize.

Bob Litterman

Board Member, Commonfund

Bob Litterman is the inaugural recipient of the S. Donald Sussman Fellowship at MIT's Sloan School of Management and serves on a number of boards, including Commonfund, Kepos Capital, the Sloan Foundation and World Wildlife Fund. Prior to joining Kepos Capital in 2010, Bob enjoyed a 23-year career at Goldman, Sachs & Co., where he served in research, risk management, investments and thought leadership roles. He oversaw the Quantitative Investment Strategies Group, a portfolio management business formerly known as the Quantitative Equities and Quantitative Strategies groups, and Global Investment Strategies, an institutional investment research group. While at Goldman, Bob also spent six years as one of three external advisors to Singapore's Government Investment Corporation (GIC). Bob was named a partner of Goldman Sachs in 1994 and became head of the firm-wide risk function; prior to that role, he was co-head of the Fixed Income Research and Model Development Group with Fischer Black. He has researched and published a number of groundbreaking papers in asset allocation and risk management and co-authored books including The Practice of Risk Management and Modern Investment Management: An Equilibrium Approach (Wiley & Co.). He is the co-developer of the Black-Litterman Global Asset Allocation Model, a key tool in investment management. Bob earned a Ph.D. in Economics from the University of Minnesota and a B.S. in Human Biology from Stanford University.

Roger Martin

Dean, Rotman School of Management, University of Toronto

Roger Martin is the award-winning author of 'The Opposable Mind' (2007), 'The Design of Business' (2009) and 'Fixing the Game' (2011) and frequent contributor to Harvard Business Review, Financial Times, BusinessWeek and other leading international publications. He has been named the 32nd top management thinker in the world (The Times and Forbes.com), one of the ten most influential business professors in the world (BusinessWeek) and one of the 27 most influential designers in the world (BusinessWeek). He has served as Dean of the Rotman School of Management at University of Toronto since 1998. He also serves as a board member of leading global corporations (Thomson Reuters Corporation and Research in Motion) and as a strategic advisor to the CEOs of several others, including P&G and Steelcase.

Anita M. McGahan

Associate Dean, Research, Rotman School of Management, University of Toronto

Anita M. McGahan is Associate Dean of Research, PhD Director, Professor and Rotman Chair in Management at the Rotman School of Management at the University of Toronto. She is cross appointed to the Munk School of Global Affairs; is a Senior Associate at the Institute for Strategy and Competitiveness at Harvard University; and is Chief Economist at the Massachusetts General Hospital Division for Global Health and Human Rights. Her credits include two books and over 100 articles, case studies, notes and other published material on competitive advantage, industry evolution, and financial performance. McGahan's current research emphasizes entrepreneurship in the public interest and innovative collaboration between public and private organizations. She is also pursuing a long-standing interest in the inception of new industries, particularly in global health. McGahan has been recognized as a master teacher for her dedication to the success of junior faculty and for her leadership in course development. In 2010, she was awarded the Academy of Management BPS Division's "Irwin Distinguished Educator Award" and, in 2012, the Academy conferred on McGahan its Career Distinguished Educator Award for her championship of reform in the core curriculum of Business Schools.

Judith Samuelson

Executive Director, The Aspen Institute

Judy Samuelson created the Aspen Business and Society Program, an independently supported program at The Aspen Institute, in 1998. Aspen Business and Society Program respects the power of business to shape the long-term health of society, and works to align business decisions with the public good. It engages leaders and social-intrapreneurs—from MBAs to CEOs—in dialogue, networks and public programs that put common sense decision-making at the heart of business practice and education. Signature programs include Beyond Grey Pinstripes, a global data base and report card on MBA business education, and the Corporate Values Strategy Group, a forum for business leaders to promote change in policy and business practice in pursuit of long-term value creation. Judy spearheaded the creation of the Aspen Principles, a set of guidelines, to spotlight short-termism in business and capital markets, and promote long-term focus by companies and institutional investors. The Principles are widely cited and were recently named one of "50 Stars in Seriously Long-Term Innovation". In 2011, Judy was named a Top 100 Thought Leader in Trustworthy Business Behavior. Judy's publishes widely and blogs for Huffington Post.

George Serafeim

Assistant Professor of Business Administration, Harvard Business School

George Serafeim is an Assistant Professor of Business Administration at Harvard Business School. He teaches the course "Leading the Global 1000" in the MBA elective curriculum and co-chairs the Executive Education program "Innovating for Sustainability". Previously he taught the "Financial Reporting and Control" course in the MBA required curriculum, the "South Africa; Innovating for Sustainability in an Emerging Market" course in the elective curriculum, and the doctoral seminar "The Role of the Corporation in Society". George's research interests are international, focusing on understanding the relation between environmental, social and governance (ESG) performance and financial performance, how innovations in processes, products and business models can lead to improvements in both ESG and financial performance, and the role of disclosure, information and financial intermediation in efficient capital allocation and long-term value creation. His work has been published in prestigious academic and practitioner journals such as the Strategic Management Journal, Journal of International Business Studies, Review of Accounting Studies, Journal of Accounting Research, Journal of Finance, Contemporary Accounting Research, Management Science, Financial Analysts Journal, MIT Sloan Management Review, Journal of Applied Corporate Finance, Director Notes, Harvard Business Review and has also appeared in media outlets including Bloomberg, Financial Times, The Wall Street Journal, The Guardian, NPR and Responsible Investor. In the area of corporate sustainability, he has written more than twenty business cases on organizations from around the world. He is the co-author of a book on the transparency and valuation of insurance companies and the co-author of a study, commissioned by the European Union, that evaluated the relevance of public information disclosed during the transition of European companies to IFRS. Professor Serafeim currently serves on the Technical Review Committee of the Global Initiative for Sustainability Ratings that is designing a generally accepted standard for sustainability ratings. Moreover, he is a member of the Standards Council of the Sustainability Accounting Standards Board that is engaged in the development and dissemination of industry-specific sustainability accounting standards.

Eric Wetlaufer

Senior Vice-President and Head of Public Market Investments, CPP Investment Board (CPPIB)

With over 20 years of experience in investment management, Eric is responsible for leading the CPP Investment Board's Public Market Investments department which invests in publicly-traded assets and related derivatives. Prior to joining CPPIB in June 2011, Eric was the Group Chief Investment Officer, International at Fidelity Management & Research in Boston, Massachusetts. Eric was also the co-founder and partner of Oxhead Capital Management and has held the roles of Chief Investment Officer of U.S. Mid Cap and Specialty Growth at Putnam Investments and Managing Director at Cadence Capital Management. Eric is also active on several non-profit boards including Bay Cove Human Services and the Melanoma Foundation of New England. Eric earned a B.A. in Earth Science from Wesleyan University, Middletown, Connecticut and is a Chartered Financial Analyst.