System-level Investing: Case Studies of Investors Leading the Way

The Investment Integration Project
2024

Disclosures

Support for this research was provided by the Surdna Foundation.

Design and illustration for this document by April L. Smith.

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For more on antitrust and sustainability considerations, please see Denise Hearn, Cynthia Hanawalt, and Lisa Sachs, “Antitrust and Sustainability: A Landscape Analysis,” Columbia Center on Sustainable Investment and Sabin Center for Climate Change Law (July 2023).

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April 2024

It's time for a new way to think about investing, one that can contend with the complex challenges we face today. Previously, investors could find ways to insulate their portfolios from certain global events. Today, even seemingly 'local' events can immediately and adversely affect all portfolios. The largest, most influential investors are recognizing this trend and considering the interconnection between environmental and societal systems under stress and adverse portfolio performance.

Those same investors are adapting and adopting policies and practices that are additive to conventional investment scrutiny at the security and portfolio levels, helping them to confront global environmental and social systemic challenges in a way that makes financial sense. Adapting to a changing world of risks, these asset owners and asset managers are charting the next, critical shift in the evolution of investment, what we call system-level investing.

To help support this shift, The Investment Integration Project (TIIP) conducted an industry needs assessment in 2021 and 2022 to identify the opportunities, challenges, and breakthroughs needed to advance investor and industry awareness and action. The data made it clear that these stakeholders are concerned about the systemic nature of social and environmental issues and their interconnection with investment. But it also made clear a general need for more information and evidence is a critical next step in making this an accessible path for institutional investors.

TIIP has developed this report, with the support of the Surdna Foundation, on "System-level Investing: Case Studies of Investors Leading the Way" as a result. The report provides case studies on California State Teachers Retirement System (CalSTRS), Domini Impact Investments, Saint Paul & Minnesota Foundation (SPMF), University Pension Plan (UPP), and Wespath Benefits and Investments. These institutions are among the first-mover investment teams that have acknowledged the importance of and have embraced the practices for system-level investing.

The case studies presented here provide a snapshot into the global community of practice of investors bridging the gap between systemic issues and their investment decisions (or portfolios) issues using a diversity of approaches. They demonstrate where the field is headed and present a path forward for other investors to learn from their peers and to join them on the vanguard of this evolution. Over the coming years we will continue to advance the theory and practice of system-level investing and equip the financial industry with tools and strategies to manage systemic social and environmental risks.

We look forward to accompanying you on the system-level investing journey that lies ahead.

Signed,

William Burckart

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Introduction

This report summarizes the findings from The Investment Integration Project's (TIIP's) five case studies of leading system-level investors. It opens with a summary of what it means to be a system-level investor, before then describing how investors adopt system-level investing and introducing five early adopters. It highlights notable findings from across the investors before then presenting in-depth case studies of each. It also posits implications for investment practice and processes moving forward.

System-level investors

System-level investors believe that profitable, long-term investment depends on healthy financial, social, and environmental systems. They acknowledge their portfolio's exposure to systemic risks and aim to use their investments to generate value for such systems rather than extracting it. System-level investors deploy a suite of conventional and advanced investment techniques to achieve this.

Conventional investment techniques used by system-level investors

- **Statements of investment beliefs.** System-level investors explicitly assert their commitment to contributing to the health of social, environmental, and financial systems that pose threats to, or offer opportunities for, their investments across all asset classes.
- **Security selection & portfolio construction.** Beyond incorporating Environmental, Social, and Governance (ESG) considerations into their investment analyses, system-related investors may also set standards or minimum thresholds for social and environmental conduct for whole industries.
- **Engagement.** System-level investors engage with entire industries – not just individual corporations or firms – on the financial implications of systemic social and environmental risks and toward the goal of influencing underlying systems.
- **Manager due diligence.** System-level investors not only assess of managers' competencies at the security and portfolio-level, but they also examine their management of systemic risks and skills.

Advanced techniques used by system-level investors

- **Field building (Self-organization, Interconnectedness, Polity).** Field building techniques pool resources to create collaborative organizational structures across the investment industry that builds the industry's capacity to address system-related challenges (Self-organization), produce and share information about environmental, social, and financial systems (Interconnectedness), and engage in public policy debates with the goal of creating stronger, more resilient social, environmental, and financial systems (Polity).

- **Investment enhancement (Standards setting, Solutions, Diversity of approach).** Investment enhancement techniques use conventional investment activities to advance system-level goals.

  This includes establishing standards that discourage investments in corporations, industries and countries with practices that violate broadly accepted standards or norms (Standards setting); pursuing investments that can solve social and environmental challenges in ways that support the stability and enhancement of broader social, environmental, and financial systems (Solutions); and simultaneously utilizing a range of investment tools to comprehensively address complex systemic environmental and social concerns (Diversity of approach).

- **Opportunity generation (Additionality, Evaluations, Locality, Utility).** Opportunity generation techniques generate a diversity of products, services, data, internal practices and external opportunities to balance short-term priorities with helping systems to adapt to changing circumstances and external shocks.

  This includes things like pursuing investments that provide access to finance to the underserved and address unmet environmental or social needs (Additionality); valuing the difficult-to-price aspects of social, environmental, and financial systems that generate potential long-term wealth creation, societal and environmental value, and investment opportunities (Evaluations); investing to strengthen the environmental or social systems within a given geographic area—be that a city, state, region or country (Locality); and maximizing the alignment of the specific investments within a portfolio's asset classes with the societal functions that these asset classes were designed to serve (Utility).

Investors leading the way

For this analysis, TIIP selected five investors known to be leading the way in incorporating system-level investing techniques. TIIP used publicly available information such as investor annual reports, published investment policies, and news articles to complete each case study. TIIP also conducted interviews with investment officers and staff at each investor and provided them with drafts of the case studies for their review and comments.[ii]

Table 1. Investors selected for case studies

CALSTRS	**California State Teachers Retirement System (CalSTRS)** is the largest teachers' retirement system and second largest public pension fund in the U.S. It has $315 billion in assets under management.
Domini	**Domini Impact Investments** is a women-led investment adviser that focuses exclusively on impact investing, with a focus on forest and land use.
SAINT PAUL & MINNESOTA FOUNDATION	**Saint Paul & Minnesota Foundation (SPMF)** is the largest community foundation in Minnesota with $2 billion in assets under management.
UPP UNIVERSITY PENSION PLAN ONTARIO	**University Pension Plan (UPP)** is a pension fund serving the Ontario university sector. It has $10.8 billion in assets under management.
Wespath BENEFITS | INVESTMENTS	**Wespath Benefits and Investments** is a nonprofit pension fund and a general agency of the United Methodist Church. It has over $24 billion in assets under management.

ii The analysis contained in this report usefully builds TIIP efforts since its founding in 2015 to document the scope and scale of asset owners and institutional investors integrating a systemic impact focus. For example, TIIP report Tipping Points 2016 documented the scope and variety of system-level/systemic investing approaches undertaken by 50 asset owners and managers at that time. It described the activities they have executed, the tools they have used, the progress they have made and what research and support is necessary for further awareness and action. It includes profiles of the specific policies and practices of these asset owners and managers that detail the tactics adopted by individual organizations and the variety of best practices that are being developed. As a follow-up to the Tipping Points 2016 report, TIIP analyzed how and why central banks (CBs) and development finance institutions (DFIs) are incorporating environmental and social system impact considerations into their activities. Published in 2017, the report—Central Bank and Development Finance Institution Approaches to Investing in Global Systems—identified five "on ramp" activities that these financial institutions use to address systemic risks and rewards, and it suggests parallels to how long-term investors attempt to manage systemic risks.

Key takeaways from investor case studies

CalSTRS, Domini, SPMF, UPP, and Wespath are among first-mover investment teams that have acknowledged the importance – of and have embraced the practices for – system-level investing.

The analysis of our case studies shows a field of system-level investing that is still carving out its norms and charting a course for success and replicability. Our studied firms are equipped with tools and techniques for rapid progress however they are also confronting challenges around evaluating their systemic impacts. Below we summarize key takeaways from these case studies, before then presenting the case studies themselves.

1. The studied investors use statements of investment beliefs to declare their commitment to system-level investing and to dictate related investment policy.

The statement of investment beliefs (SIBs) sets an external and internal tone for the investor's practice and values. It is often a starting point for an investor to convey their understanding of financial markets, its place within them, and its desired contribution. While a public statement of investment beliefs is common among investors of all kinds, system-level investors often highlight in their statements the importance of environmental, social, and financial systems, how systems impact investors (and vice versa), and how they aim to strengthen them.

All five investors studied for this analysis discuss in their SIBs the interconnection between investment and environmental, social, and financial systems and express their commitments to strengthening these systems both to protect their bottoms lines and to promote global well-being. These SIBs share two notable core features; they: (1) emphasize the fundamental link between environmental, social, and financial systems and long-term investment and indicate that investors must work to ensure the health of such systems, and (2) dictate investment policy and practice, including security selection & portfolio construction, engagement and proxy voting, and manager selection and due diligence.

Figure 1. Excerpts from system-level investors' statements of investment beliefs

CalSTRS

"…be a catalyst in transforming the financial markets to focus on long-term value creation that fully integrates sustainability considerations and uses CalSTRS' influence as a significant global investor to promote sustainable business practices and public policies."[1]

Domini

"Investments have systems-level impact on finance, society, and the environment. Investors have an ethical obligation to acknowledge these consequences."[2]

Saint Paul & Minnesota Foundation

"Engagement is critical to changing the institutional investing industry and the Foundation should play a leadership role in this industry."[3]

UPP University Pension Plan Ontario

"As a long-term investor, UPP has a responsibility to promote the health of the capital markets and the financial, social, and environmental systems on which capital markets rely."[4]

Wespath Benefits | Investments

"Active ownership and stewardship are powerful tools. We engage with companies, asset managers, public policy makers and other stakeholders to reinforce the importance of considering all information, including ESG factors, which we believe will result in positive outcomes aligned with a sustainable economy."[5]

2. System-level investors view systemic risk management as aligned with their fiduciary duty to their clients.

The investors commonly assert – typically in their SIBs – that ESG factors are material to investment returns, particularly over the long-term, and are therefore relevant components of fiduciary duty. By definition, system-level risks are non-diversifiable and result in cascading effects for the economy and financial system. In other words, system-level risks, such as climate change, biodiversity collapse or social instability pose financially material risks to investor portfolios. Therefore, if certain systemic issues pose risks to achieving financial investment objectives, investors generally have a legal obligation to consider how it can mitigate that risk.

All firms studied in this report note the fiduciary duty they have to their beneficiaries and investors, but some go further to include the management of systemic risk into how they view fiduciary responsibility. For example:

- Domini published a set of 'forest beliefs' that communicate its fiduciary obligation to preserve and enhance the value that forests provide.[6]

- In describing its ESG approach, UPP links ESG factors, capable of adding or extracting value from systems, as accounted for in every stage of its investment process in order to meet its fiduciary duty of providing value to its members.[7]

- In describing its investment philosophy, SPMF states that it cannot meet its fiduciary duty without mission-aligning its investment portfolio.[8]

3. The studied investors are primarily focused on the systemic challenge of climate change.

Consistent with the findings from TIIP's 2022 state of the industry assessment described in *Approaching the tipping point: Recommendations for building the marketplace for system-level investing,* climate change is the systemic issue atop of the studied investors' minds. Four of the five investors not only isolate climate change and its risks to investment in their statements of investment beliefs, but they have also developed roadmaps – or "action plans" – for actions related to climate change. Such action plans include activities focused on the threats of climate change to global well-being and, the risks posed to long-term asset values, and concerns about the transition to a low-carbon economy ("transition risks") and stranded assets.

Notable among these climate roadmaps is UPP's robust Climate Action Plan (outlined below), which UPP developed to guide its security selection activities and which it hopes *sends a signal to all companies demonstrating the importance of decarbonization and the targeting of capital to those who take it seriously.*[9] That is, the plan has a system-level objective.

Table 2. UPP's Climate Action Plan

1	2	3	4
Evaluate climate-related risks, opportunities, and impacts of our current and prospective investments at the total fund and investment mandate levels.	**Invest** in climate solutions in line with the transition to a net-zero world and reduce the GHG intensity of our assets.	**Engage** with portfolio companies and market actors, including asset managers, to encourage a transition to a resilient, low-carbon, net-zero world, and sufficient-climate disclosure.	**Advocate** for public policy and market systems that support limiting the global average temperature rise to 1.5 degrees Celsius.
Commitments: • Implement a climate transition investment framework and evaluate our portfolio. • Integrate climate risk and opportunity assessment into investment strategy and processes.	**Commitments:** • Invest only in new mandates and assets that align with the transition to a net-zero world. • Reduce our portfolio's carbon footprint by 16.5% by 2025 and 60% by 2030 from a 2021 baseline. • Set a target for new investments in climate solutions and selectively exclude investments in companies that present significant climate risk.	**Commitments:** • Engage with at least 20 companies through collective and direct engagement. • Engage with external investment managers to encourage their engagement with companies and emissions reductions.	**Commitments:** • Participate in direct and collective advocacy with policymakers. • Join the UN-convened Net-Zero Asset Owner Alliance and support industry initiatives that advance climate action.

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SPMF is the only studied firm whose primary systemic focus is not climate change. Founded in 1940, SPMF's mission is to create "an equitable, just and vibrant Minnesota where all communities and people thrive."[10] It aims to do so through three core strategies: inspiring generosity by facilitating and amplifying individual philanthropic giving; advocating for equity – and racial equity in particular – through grantmaking and other activities, and; investing in community-led solutions to the challenges faced by local communities across Minnesota. As such, SPMF's system-level investment strategy centers around a highly intentional focus and deep engagement on diversity, equity, and inclusion (DEI) and racial and gender equity. In short, the core objective of the strategy is to align SPMF's investments with the foundation's values and mission and ensuring that SPMF's investment portfolio does not directly or indirectly propagate problems that the foundation is otherwise trying to solve (e.g., racial equity).[11]

4. The studied investors commonly adopt "field building" strategies to advance their system-level goals.

Whereas engagement with individual companies is a relatively common conventional investment technique, all five investors utilize field building to collectively engage with their peers to more effectively impact entire industries and influence broader change. This most commonly includes: (1) creating or otherwise participating in collaborative organizational structures that builds the financial industry's capacity to address system-related challenges, called "Self-organization", and (2) engaging in public policy debates with the goal of creating stronger, more resilient social, environmental, and financial systems, called "Polity". All five investors, for example, are signatories of the Principles for Responsible Investing (PRI), and all have joined collaborative engagement groups such as the Net Zero Asset Owners' Alliance (NZAOA), the Institutional Allocators for Diversity, Equity, & Inclusion (IADEI), Nature Action 100. By joining forces with likeminded firms, including competitors, these investors are leveraging strength in numbers and assets under management to more swiftly demand change.

Table 3. Select examples of the use of field building – Self-organization and Polity – by the studied investors

Self-organization	
Domini	Domini actively pursue opportunities to co-create and joining industry-led organizations in pursuit of its system-level investing goals. This includes, for example, partnering with ten other investment firms announced the launching of Nature Action 100, and joining forces with the Institutional Investors Group on Climate Change, the Finance for Biodiversity Foundation, Planet Tracker, and Ceres to help organize Nature Action 100's operations. Also, through its participation in the Finance for Biodiversity Foundation and Nature Action 100 Domini has helped create a clear, consistent, and actionable set of recommendations for how companies can prevent biodiversity loss.

SPMF became the first U.S. community foundation signatory of the Principles for Responsible Investing (PRI) in 2022, enabling SPMF's investment team to connect with "like-minded institutional investors who are also trail blazers in this field."[12] SPMF's decision to join PRI provides it with a globally recognized and highly credible standard, which further demonstrates its system-level investing commitment. SPMF is also a member of the Institutional Allocators for Diversity, Equity, & Inclusion (IADEI), a consortium of asset owners that seeks to drive DEI within institutional investment teams and portfolios in investment management.

Wespath has made self-organization techniques a key part of its investment activities through leadership positions in specific asset-owner alliances as well as through active engagement in other strategic partnerships. For example, Wespath was a co-author and founding signatory to the UN-backed PRI. It currently serves on the UNPRI's Stewardship Advisory Committee, where it recommends expectations to be set regarding PRI signatories' active ownership practices. Wespath is also co-chair of the Investors for Opioid and Pharmaceutical Accountability (IOPA) (IOPA). In this role it convenes investors to produce better governance structures at opioid producing companies. As a result of IOPA engagements, Wespath has helped achieve the appointment of independent board chairs at major pharmaceutical companies, increased the publication of opioid risk reports, expanded disclosure on pharmaceutical lobbying practices, and has aligned executive compensation with better opioid practice.[13]

Polity

CalSTRS maintains a high level of transparency in its policy efforts by publishing all of its public submissions with clear statements on its policy positions.[14] It engages with the Federal Trade Commission, the International Sustainability Standards Board, the US Securities and Exchange Commission, the European Supervisory Authorities, and many more.[15] Such engagements include advocating for regulation ensuring good governance and the safety and transparency of the market,[16] improving disclosure standards, and identifying and opposing legislation that would weaken shareholder rights.

UPP communicates with regulators and policymakers, both independently and together with peer investors and other organizations. UPP publishes its statements and submissions on its website, for added transparency about its advocacy. In 2022, UPP issued 10 public submissions to agencies, including the Ontario Securities Commission, the U.S. Securities and Exchange Commission, and the International Sustainability Standards Board. In most cases, UPP called for improved regulation of corporate disclosures of environmental, social, and governance risks and opportunities across industries.[17]

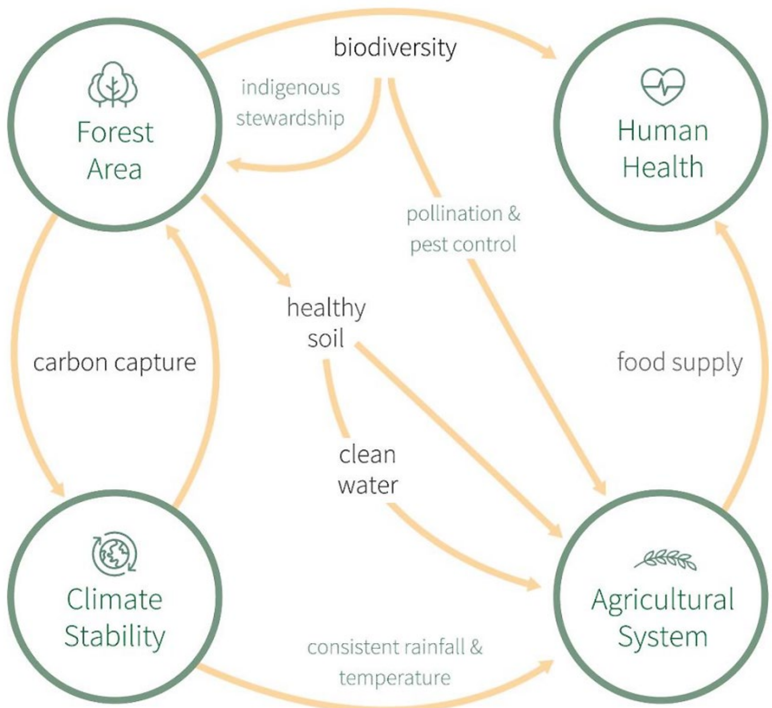
Wespath has published 38 unique public policy statements written between 2009 and 2022.[18] Included in these statements are independently authored letters to US agencies such as the Environmental Protection Agency and Securities and Exchange Commission as well as endorsed letters written by major investment groups such as the PRI, the Interfaith Center on Corporate Responsibility (ICCR), Council of Institutional Investors, and others. Topics covered by the public statements range from environmental protection and human rights to corporate governance and standard setting.

5. It is difficult to measure the impacts of system-level investing strategies.

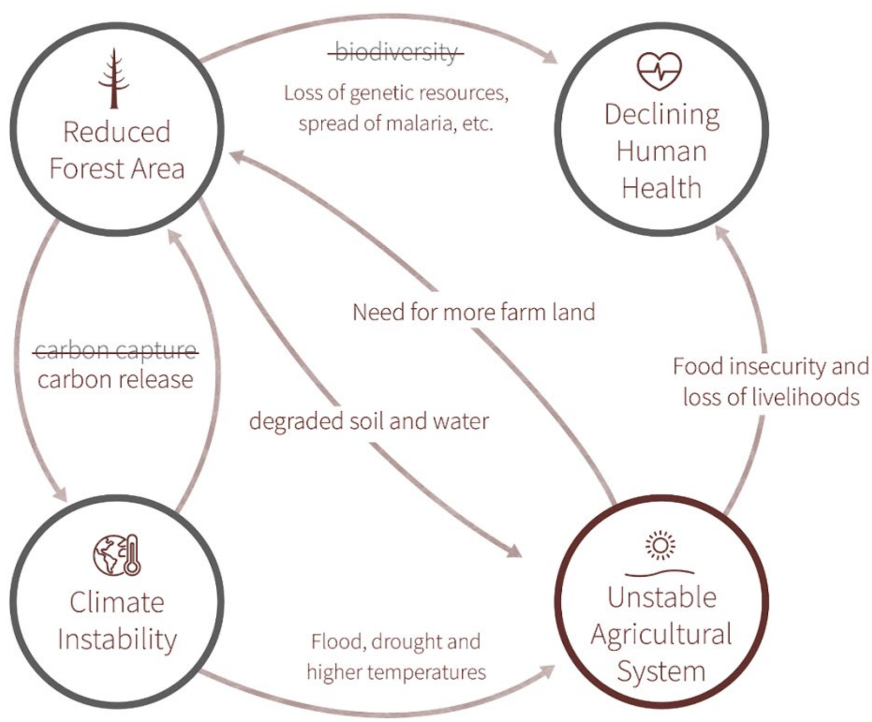
All five studied investors struggle with how to measure and report on the impacts that they are having on systems through their system-level investing approaches. This challenge is connected to the concepts of value extraction and value creation, concepts that Domini's Steve Lydenberg has woven into the firm's philosophy and highlighted during our interview for this project. An important differentiation between conventional and system-level investors is that the latter makes value creation *and* financial return central to their investment philosophies whereas the former maintains a focus on only financial return. Evaluating investment decisions from a purely financial standpoint is a straightforward process. Capturing and communicating the social or environmental value, for example, that a firm's investments create is the opposite. It is an incredibly complex process with no straightforward techniques, agreed upon metrics, or playbook to follow.

Figure 2. Domini system dynamics maps, value creation vs. value extraction

VALUE CREATING SYSTEM



VALUE DESTROYING SYSTEM



Source: Domini Impact Investments (2023). *Systems Dynamics Maps*, 2022. Domini Forest Project.

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As a consequence, while system-level investors continue examining how to measure the systemic value of their investments, they focus on measuring their progress against the commitments and standards that they have set. For example, all five case study investors have put considerable effort into designing and implementing criteria to guide their investment decision-making process:

CalSTRS integrates standards and frameworks set by the Taskforce on Climate-related Financial Disclosures (TCFD) into its corporate engagement strategy, utilizing proxy voting avenues to encourage adoption of TCFD-aligned reports.

Domini's investment due diligence is informed by the Forest Stewardship Council (FSC). The FSC's forestry certification supports Domini's security selection process and goal in maintaining a portfolio that adds rather than extracts value to forests.

SPMF has adopted the six Principles outlined in the UN's Principles for Responsible Investment. These principles support SPMF's responsible investment tracking system.

UPP applies a net-zero emissions criteria to its portfolio, filtering out assets that work against its climate strategy. This allows it to progress towards and track its progress on its net-zero commitment.

Wespath organizes its sustainable investing efforts through its Sustainable Economy Framework. The framework sets procedures for investing, engaging, and avoiding different assets.

6. It is crucial to have a "champion" for system-level investing within an organization for the strategy to succeed.

A commonality among the five firms has been the presence of at least one system-level "champion" within the company – that is, an outspoken, enthusiastic, and convincing advocate or a spokesperson for system-level investing. SPMF has Chief Investment Officer, Shannon O'Leary; Domini has Strategic Advisor, Steve Lydenberg; UPP has President and CEO, Barbara Zvan; CalSTRS has Investment Officer, Kirsty Jenkinson; and Wespath has Managing Director of Sustainable Investment Strategies, Jake Barnett. Without such champions inside of investment teams, the choice to expend extra effort on carrying out system-level practices might be foregone. The individuals listed above have advocated internally and externally for system-level techniques to be adopted. They serve on the boards of collective engagement bodies and have supported the creation of system-level tools to be used by the wider investment community.

Investor Case Studies

California State Teachers Retirement System (CalSTRS) With $315 billion in assets under management (AUM), CalSTRS is the largest teachers' retirement system and second largest public pension fund in the U.S. Established by law in 1913, CalSTRS' mission is to, "secure the financial future and sustain the trust of California's educators."[19] CalSTRS provides retirement, disability, and survivor benefits to California's more than one million public school educators and their families.

CalSTRS is administered by the Teachers' Retirement Board, which ensures that the nine CalSTRS Investment Beliefs are incorporated into all policies, procedures, and investment plans. CalSTRS considers environmental, social, and governance implications with a particular emphasis on **climate change** in all business and investment decisions. The CalSTRS fund includes investments in public and private portfolios. Investments are guided by an Investment Policy and Management plan, which ensures a long-term, ten-year investment horizon and dictates an annual return goal of 7%.[20]

System-level investing strategy

CalSTRS has twenty different policies that guide its investment strategy. It first published a Statement of Investment Responsibility in 1978 to help its investment team navigate the complex landscape of Environmental, Social, and Governance (ESG) issues. The CalSTRS investment philosophy takes a long-term patient capital approach, with an emphasis on the systemic challenge of climate change. In the early 2000s CalSTRS began formalizing and recording its commitment to system-level investing, culminating in its first ever sustainability report in 2015.

The CalSTRS Sustainable Investment & Stewardship Strategies Program and Portfolio Policy, approved by the Teachers' Retirement Board, governs the Sustainable Investment and Stewardship Strategies Portfolio (SISS), which comprises up to five percent of the CalSTRS Total Fund market value.[21]

Developing the strategy and ensuring successful adoption

- *Stakeholder feedback.* With the feedback of its members, the Teachers' Retirement Board (TRB) has taken measures to incorporate system-level values and techniques within its operations. Every three years, the Investment Committee, composed of the TRB, consults CalSTRS staff and surveys its members to publish a strategic plan paving the way for action on system-level investing techniques.

- *Investment beliefs and policies.* To maximize adoption, CalSTRS incorporates system-level values into its investment beliefs and guiding policies, informing its members of how their retirement is being funded and beholding its internal and external investment managers to incorporating system-level techniques.

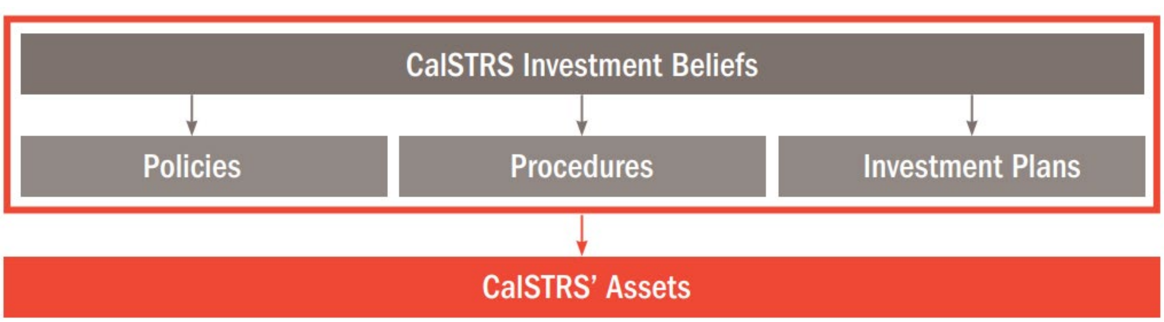
CalSTRS Policy Impact on Operations

1. Extending conventional techniques

a. Statement of investment beliefs

Last updated in 2020, The CalSTRS Investment Beliefs guide the CalSTRS' Board of Directors and investment team in developing appropriate policies, procedures, and investment plans for CalSTRS' assets.[22]

Influence of CalSTRS Investment Beliefs



Created by CALSTRS.

Highlights from the nine belief statements include:

- The management of ESG factors is material to generating long-term financial returns for CalSTRS members.
- Climate risks and the economic transition related to it materially impacts the value of CalSTRS' investment portfolio.
- Alignment between external advisors and managers and the CalSTRS investment approach is critical to meet its long-term goals.
- The climate risk belief statement was adopted in 2020 as part of the TRB's Low-Carbon Transition Workplan.

The CalSTRS Investment Belief guide has prompted the creation of policies that inject system-level strategies into the CalSTRS investment model. One example of such a policy is its Investment Policy and Management Plan (IPMP), last updated in 2023. The IPMP, which provides a framework for CalSTRS' investments, explicitly recognizes the importance of managing ESG risks and is equipped with an Investment Policy for Mitigating ESG Risks.[23] The policy explains that the success of CalSTRS' investments is tied to the success of the financial, environmental, and social systems that all investments live within. As a result, CalSTRS understands its fiduciary duty to be investing in entities that similarly pursue long-term sustainability in their operations. The policy goes on to make the following critical points:

- Managers of CalSTRS investments who do not strive for sustainability put its long-term expected rate of return at risk.
- The Investment team, CIO, and the Investment Committee (CalSTRS board) will take immediate action following any potential violation of the ESG policy.
- Sustainable returns over long periods are more important than short term gains.
- All investment managers will take into account the CalSTRS 25 ESG Risk Factors when making an active investment.

CalSTRS investments are also guided by its Sustainable Investment & Stewardship Strategies Program and Portfolio Policy (SISS). Last updated in 2021, and originating in 1999, the SISS program aims to, "be a catalyst in transforming the financial markets to focus on long-term value creation that fully integrates sustainability considerations and uses CalSTRS' influence as a significant global investor to promote sustainable business practices and public policies."[24]

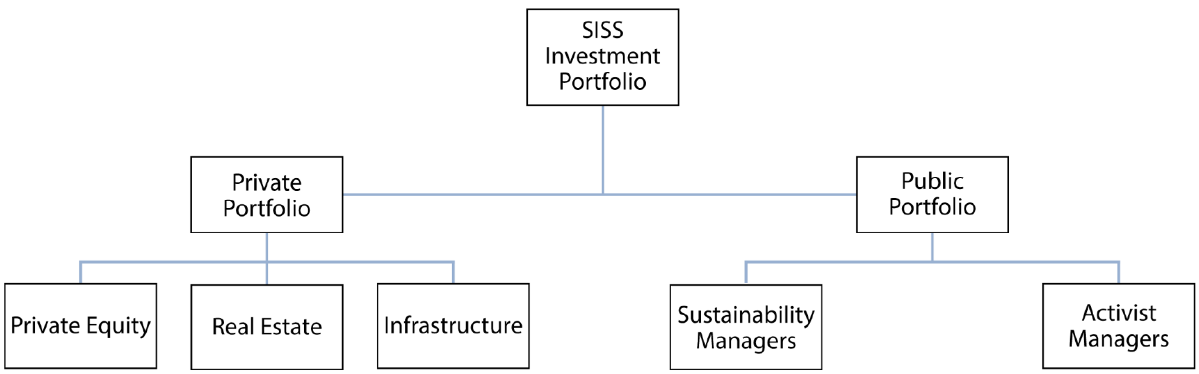
The SISS program includes guiding policies for: proxy voting, portfolio company engagement, regulatory advocacy, asset allocation for the SISS private and public portfolio (combined which comprise up to 5% of total CalSTRS AUM).[25]

b. Security selection & portfolio construction

The CalSTRS SISS portfolio is comprised of a public portfolio component and a private portfolio component.[26] The public portfolio aims to enhance returns of the total CalSTRS fund with the additional benefit of improving environmental, social, and financial systems. Strategies used to achieve this include: actively managing portfolios, investment partnerships in public securities, and passively managing portfolios. All strategies incorporate ESG considerations and ensure external managers follow suit with an activist and long-term value creation focus.

The SISS private portfolio is a critical growth engine for CalSTRS. Its investment scope is broad, but the portfolio's main goal is to be a source of long-term capital appreciation for the overall CalSTRS Fund (SISS policy). The private portfolio does not look to replicate investments present elsewhere in CalSTRS portfolios. Rather, it serves to expand investment opportunities in private equity, infrastructure, and real estate that align with the SISS program goal of creating long-term and sustainable value.

CalSTRS SISS Portfolio Outline



Created by CalSTRS

Importantly, the SISS program underscores an investment approach across asset classes that "focuses on structural shifts in the global economy linked to sustainability."[27] In 2019 CalSTRS adopted the Low-Carbon Transition Workplan, which aims to reduce climate-related investment risk and increase CalSTRS' ability to support climate-related solutions. The Workplan superseded a 2021 commitment by the Teacher's Retirement Board to achieve net zero greenhouse gas emissions across the entire CalSTRS investment portfolio by 2050 or sooner.

The net zero commitment has strengthened CalSTRS' ability to have a positive impact on climate via asset allocation, resulting in over $20 billion invested in low-carbon solutions as of 2021.[28] Key components of the pledge include:

- *Measurement and reporting.* CalSTRS uses MSCI's Climate Value-At-Risk service to measure its public market emissions exposure and reduction management. The tool allows for a comparison of CalSTRS portfolio emissions against potential representations of Earth's future climate. This has contributed to confident climate-related investment decisions including tying 20% of the CalSTRS public equity portfolio to a low-carbon public equities index and committing to an emissions reduction plan for its Fixed Income Portfolio that includes an initial 12% carbon reduction.[29]

- *Proxy voting.* In 2022 alone CalSTRS voted on 1,033 shareholder proposals. A focus of CalSTRS' proxy voting approach is aligning corporate behavior with the Paris Climate Agreement.

- *Corporate engagement.* CalSTRS leverages its leadership role with Climate Action 100+, working with likeminded investors to secure reduced emissions commitments from some of the world's largest companies.[30]

- *Policy engagement.* CalSTRS advocates at the state and federal level for policy that encourages emissions reductions. It has directed its policy engagement.

c. Engagement

Throughout its 100+ year history, CalSTRS has maintained a leadership role in public advocacy for system-level investing techniques. Guided by its Stewardship Priorities and its Corporate Governance Principles, engagement is a cornerstone of the CalSTRS system. Highlights of CalSTRS' engagement efforts include:

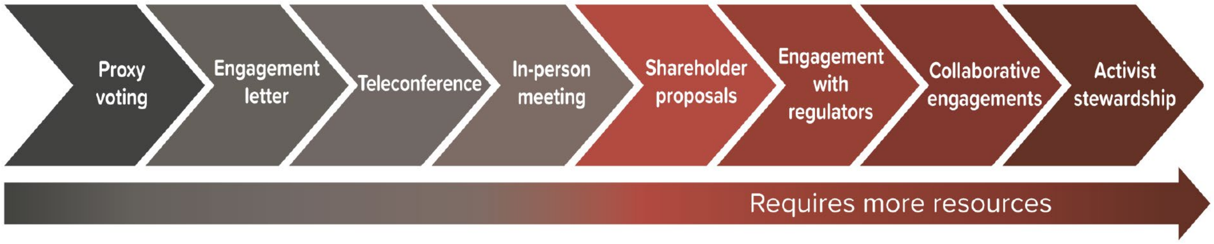
- Voting against directors that do not provide at minimum, disclosures, including financial reports that align with the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) and include, at a minimum, the company's direct emissions (scope 1) and indirect emissions (scope 2).[31]

- Take every reasonable engagement effort prior to taking a divestment stance.

- Voting against a board that does not include at least one woman and against a board's nominating and governance committee if at least 30% of its members are not women.

- Voting against the nominating and governance committees of U.S. companies that do not disclose information about the diversity of their board members.

Influence of CalSTRS Investment Beliefs



Recreated by TIIP, original created by CALSTRS.

Examples of CalSTRS stewardship efforts and their systemic importance include:

- **Phillips 66:** important global market actor; top 40 on the Fortune 500 list; market value of $46 billion.

  CalSTRS led a shareholder proposal and public campaign aimed at Phillips 66 to make emissions reduction commitments. As a result, in October of 2021, Phillips 66 published a lobbying activity report demonstrating how its new policy goals align with the Paris Climate Agreement.[32] The report also explained a growing focus on lower-carbon energy sources. CalSTRS led this engagement with the support of Climate Action 100+, making its leadership more credible with the support of fellow investors.

  By engaging Phillips 66 on its climate risk, CalSTRS presents itself as an owner interested in more than its asset's financial condition. CalSTRS' push to bring a major energy company in alignment with the Paris Climate Agreement signals to the broader industry that environmental systems should be considered to attract investment.

- **Duke Energy:** 2nd largest electric utility company in the US by revenue; serves 8+ million customers.

  CalSTRS led engagements with Duke Energy to secure reduced greenhouse gas emission commitments through filing a shareholder proposal and with repeated dialogue with the company. As a result, Duke agreed to accelerate the closing of its coal plants with a 2035 target year, retire old oil and natural gas generation units, and achieve net zero methane emissions by 2030 for its natural gas operations.[33] CalSTRS led this engagement with the support of Climate Action 100+, making its leadership more credible with the support of fellow investors.

  Like its approach with Phillips 66, CalSTRS is addressing climate risk that lacks a clear, immediate impact on the company's financial condition. By doing so, CalSTRS acts with a long-term and systemic lens, encouraging change that strengthens the underlying environmental system. This is directly in line with its belief that healthy environmental systems support a healthy financial system. A necessity to deliver long-term value for its members.

2. Adopting advanced techniques

a. Self-organization

By collaborating with the investment community, CalSTRS creates a stronger lever by which it can advocate for its beliefs. Given its size and age, CalSTRS has a unique ability to influence and add credibility to existing alliances. It has done so in the following ways:

- Playing a leading role in Climate Action 100+, an investor-led initiative to keep the largest greenhouse gas emitters accountable.
- Becoming an active member and Chair of the Board of the Council of Institutional Investors, an association of US asset owners advocating for effective corporate governance and policies that enhance long-term value.
- Supporting Ceres on multiple workstreams including the Ceres Investor Network on Climate Risk and Sustainability. CalSTRS supported Ceres' advocacy for the passing of California's 2023 climate disclosure bill. SISS Investment Director, Kirsty Jenkinson, also serves as a Ceres board member.
- CalSTRS Chief Investment Officer, Christopher Ailman serves on the leadership team of the ISSB's Investor Advisory Group.

b. Polity

A significant element of the CalSTRS stewardship strategy is influencing regulatory policy and legislation. CalSTRS maintains a high level of transparency in its policy efforts by publishing all of its public submissions with clear statements on its policy positions.[34] The following actions highlight the CalSTRS approach to influencing public policy:

- Advocating for regulation ensuring good governance and the safety and transparency of the market.[35]
- Engaging state, federal, and global actors to improve disclosure standards.
- Identifying and opposing legislation that would weaken shareholder rights.
- CalSTRS engages with: the Federal Trade Commission, the International Sustainability Standards Board, the US Securities and Exchange Commission, the European Supervisory Authorities, and many more.[36]

CalSTRS' decision to influence public policy aligns with its system-level approach as it goes beyond single-entity or single-industry engagement and targets matters indirectly related to an assets' financial performance. By engaging with governmental bodies, supporting certain regulatory efforts that increase market transparency and opposing other efforts that weaken corporate governance, CalSTRS aims to strengthen the *system* in which its assets operate in.

c. Standards setting

Historically, CalSTRS has advocated for clear, effective, and global disclosures to support the system-level investing community. CalSTRS Chief Investment Officer, Christopher Ailman, served as the inaugural chair of the SASB Investor Advisory Group and maintains a seat on the ISSB advisory group's leadership committee.[37] The advisory group represents leading asset owners and managers in improving the quality and comparability of sustainability-related financial disclosures. By dedicating energy to improved global disclosures, Ailman and CalSTRS are investing in a tool that can support global systems.

A Deeper Dive: CalSTRS & ISSB – Supporting global sustainability reporting standards

International Sustainability Standards Board The founding of the ISSB in 2021 brought the world a step closer to globally consistent sustainability reporting standards. ISSB standards were developed with the guidance of numerous stakeholders including its Investor Advisory Group, where CalSTRS plays a leading role. Throughout the ISSB's standards development process, CalSTRS provided detailed recommendations on how standards can be most effective for investors, giving feedback for each disclosure draft published by the ISSB.[38]

Ailman has continued to publicly comment on the importance of having a body like the ISSB, recommitting CalSTRS to advising ISSB leadership and promoting the global uptake of ISSB standards.

Supporting reliable and comparable standards for non-financial corporate disclosures may not have an immediate financial benefit to CalSTRS and its members, however it does have long-term consequences in shaping global corporate behavior and capital allocation. A part of this exact community, CalSTRS is responding to increasing investor demand for quality, non-financial information, by influencing and supporting standards that align with its mission of achieving a net-zero portfolio. As a result, the recent creation of the International Sustainability Standards Board and its incorporation of multiple reporting frameworks was a milestone that CalSTRS celebrates as a step closer to a global standard.

Domini Impact Investments Domini Impact Investments is a women-led investment adviser that focuses exclusively on impact investing. Domini leverages finance to drive positive outcomes for people and planet while seeking competitive financial returns. Domini manages five funds, each guided by the same standards, but with a slightly different focus:

1. **Domini Impact Equity Fund:** Universal human dignity and ecological sustainability focus
2. **Domini International Opportunities Fund:** Global sustainability focus
3. **Domini Sustainable Solutions Fund:** General sustainability focus
4. **Domini Impact International Equity Fund:** International corporate responsibility focus
5. **Domini Impact Bond Fund:** Additionality focus, directing capital where it is needed most

Domini has always incorporated environmental and social factors into its investment approach. In 2018 it decided to focus on **forests and land use.**[39] Domini has taken a particular focus on researching the implications of deforestation and agricultural land use for the companies in its funds and identifying climate and biodiversity-related risks and opportunities. A driving force behind Domini's system-level philosophy is Steve Lydenberg, a foremost figure and leading thought-leader of system-level investing and Strategic Advisor at Domini.

System-level investing strategy

Since it was founded in 1991, Domini has invested under the belief that strong financial markets are only possible with healthy supporting environmental and social systems. In 2016, Domini committed to taking a system-level approach and introduced the concept and accompanying techniques to the firm.

Between 2016 and 2018, Domini developed its Investment Beliefs Statement and began issuing public reports on its system-related activity. Its investment process is guided by its two over-arching goals:

1. **Universal Human Dignity** *"Domini seeks investments that promote universal values of fairness, equality, justice and respect for human rights."*
2. **Ecological Sustainability** *"Domini seeks investments that promote long-term environmental sustainability."*

Alongside Domini's goals are the systemic issues that it has chosen to focus on. Initially, Domini chose nine areas of focus. From 2016 to 2018, Domini realized that tackling nine systemic issues was too wide of a scope, as each focus area demanded more attention than anticipated. In an effort to increase its potential impact on a given system, Domini chose to focus exclusively on forests and land use. It used a framework developed in partnership with The Investment Integration Project to justify its new singular focus on forests and land use.[40] The framework addressed themes of consensus, relevance, effectiveness, and uncertainty.

Consensus

There is general global consensus among scientists, investors, corporations, policymakers, and the public about the need for effective action to halt deforestation. Such consensus was reflected in a 2014 pledge by national and subnational governments and multinational companies, indigenous communities, and nongovernmental organizations to end forest loss, and in the United Nations Sustainable Development Goals which highlight the importance of sustainable forest management and reversing deforestation.

Relevance

To determine its exposure to, or dependency on forests, Domini calculated the percentage of its holdings linked to forests (see image below). Its analysis showed multiple types of links to forests within its holdings. The two most noteworthy being holdings with a direct link, a link that demonstrates a need for forests while simultaneously contributing to their destruction; and holdings with a macro link, a link describing companies that will be meaningfully impacted by the loss of forest ecosystem services, particularly with regard to climate change. Domini views a focus on forests as a prudent financial decision that supports its goal of sufficiently monitoring risk and creating value for its investors.

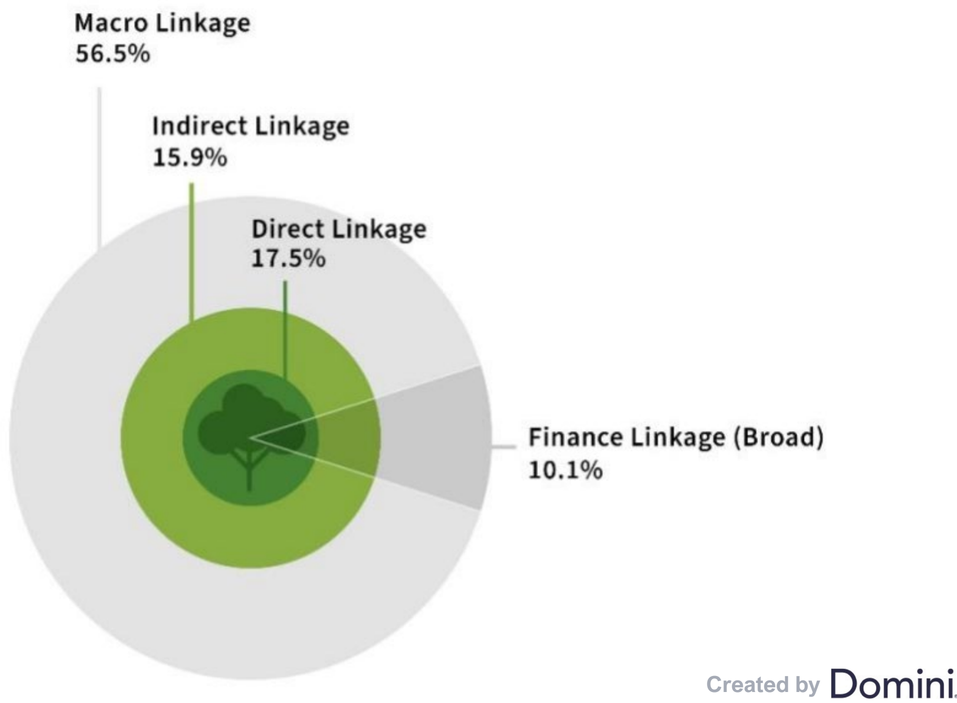
Effectiveness

Domini has identified global commodity sourcing as the primary driver of deforestation. It asserts that investors have an outsized influence on commodity sourcing practices, making it an effective lever in the push to end deforestation. Domini has also observed a lack of attention being given to forests by investors, encouraging the firm to act on the need for investor action.

Uncertainty

Although there is consensus regarding deforestation's negative impact on the planet, the exact scope and scale of this impact vis a vi differing levels of deforestation is unclear. With the potential to be extremely dire, pushing the Earth past its planetary boundaries, the lack of certainty in deforestation's consequences provide Domini with another justification for narrowing its focus.

Domini Holdings Linked to Forest Health



Source: Domini Impact Investments (2020). *Domini Forest Project – Justification for our Forest Work.*

1. Extending conventional techniques

a. Statement of investment beliefs

In 2017, Domini formalized its Statement of Investment Beliefs (SIB). Different from an investment policy statement or a mission statement, the SIB communicates a firm's views on financial markets and the principles it applies to security and manager selection. Domini's original SIB consisted of three beliefs:[41]

1. Investments have systems-level impact on finance, society and the environment. Investors have an ethical obligation to acknowledge these consequences.
2. Investors that strengthen the resilience and integrity of these critical systems create lasting value. Investors that fail to do so cause harm.
3. Long-term investment performance depends upon the above principles.

Between 2018 and 2022, after it chose to focus on forests, Domini developed a forest-specific SIB and a corresponding set of Forest related Effectiveness Principles. Over time, the principles evolved to focus on regenerative agriculture, biodiversity, and indigenous peoples. The combination of its beliefs and principles sets the tone for *why* Domini is taking its unique approach and *how* Domini plans to execute its strategy.

Domini Forest-related Investment Beliefs

- Societies and economies, and therefore businesses and investments, are built on stable and healthy environmental systems with respect to climate and biodiversity.
- Forests and related lands provide substantial value to investors and corporations with regard to stable and healthy environmental systems.
- Investors' policies and practices can impact forests and related lands either positively or negatively.
- Corporations and investors can act effectively to preserve, measure, and enhance the value they derive from these lands.

Domini Forest-related Effectiveness Principles

- Base our investments, engagements, and other investment-related decisions on a holistic understanding of corporations' and investors' dependence and impact on the long-term value and services of forests and related lands.
- Work to create a positive systems dynamic that enhances the value of forests and related lands.
- Identify, monitor, and report on our direct and indirect impacts on forests and related lands, with an emphasis on climate, biodiversity, and Indigenous peoples.
- Share our principles and processes with investors, investees, and the financial community to promote holistic, long-term policies and practices regarding forests and related lands.

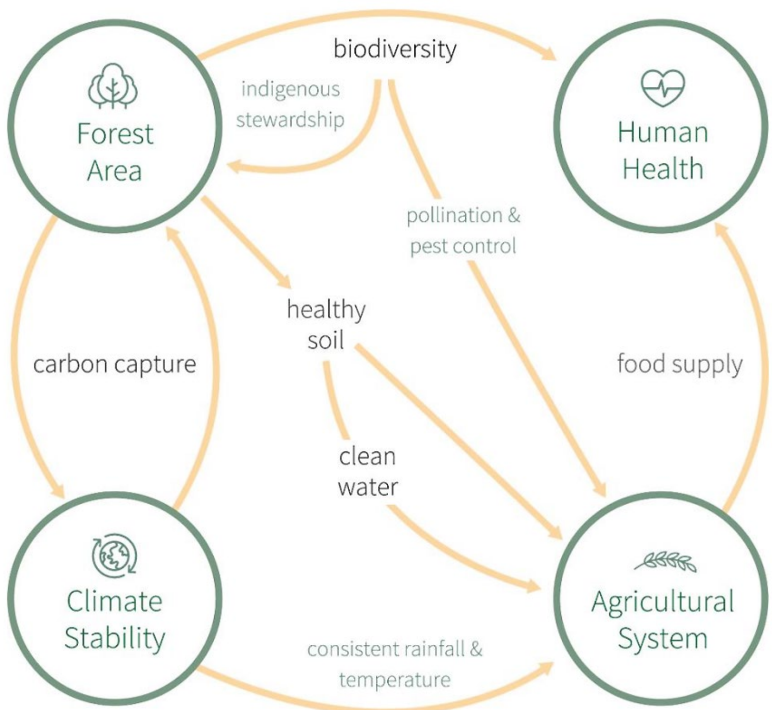
By stating its belief that a healthy financial system is dependent on healthy environmental and social systems, Domini's SIB demonstrates a system-level focus. Contrary to the SIB of a more conventional investor, which may state a belief that financial markets are naturally efficient, or that it seeks added value through ESG consideration, Domini's SIB commits the firm's investment process to system-level considerations. Domini's investment principles and beliefs put guardrails on the firm's investment practice, nudging it to strengthen value creating systems rather than investing in value destroying systems.

The system dynamics maps below, developed by Domini, demonstrate how systems are interrelated and can be value creating or value destroying. Domini seeks to add value to the forest system, with the benefit that by doing so, value will be added to the systems of human health, agriculture, and climate stability.

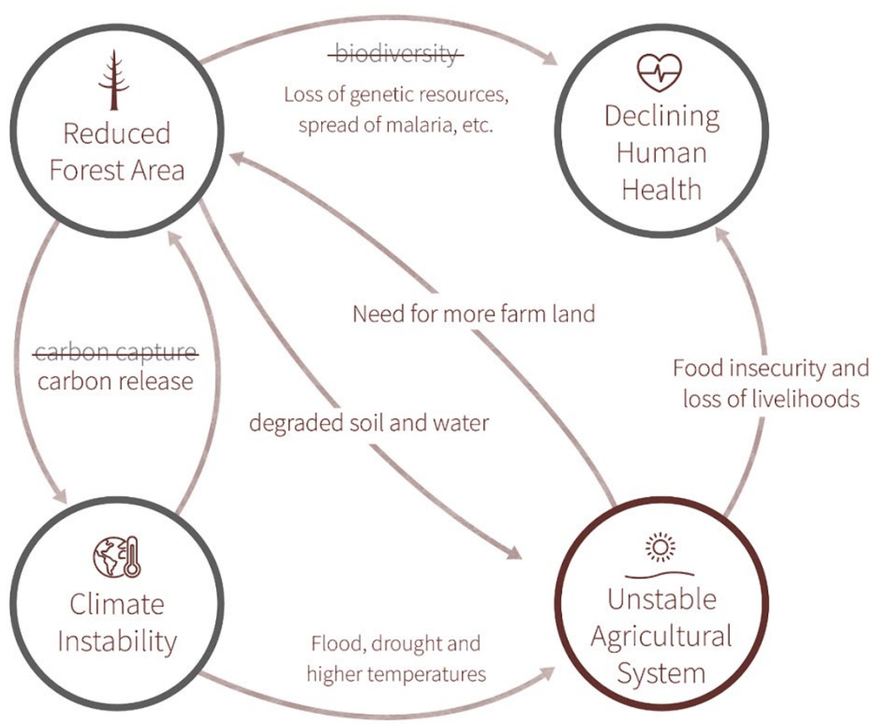
Domini System Dynamics Maps

Forest connection to three foundational social and environmental systems that investors rely on

VALUE CREATING SYSTEM



VALUE DESTROYING SYSTEM



Source: Domini Impact Investments (2023). *Systems Dynamics Maps*, 2022. Domini Forest Project.

Created by Domini

b. Engagement

An objective of Domini's focus on forests is to promote forest-positive business model transitions. The firm works to achieve this by engaging with companies, issuers, civil society organizations, and policymakers.

Examples of Topics Pursued

- Improved use and development of voluntary standards
- Sustainable palm oil sourcing
- Action on human rights abuses
- Action against deforestation
- Adoption of regenerative agriculture

Examples of Methods Used

- Direct dialogue with companies
- Filing of shareholder proposals
- Proxy voting
- Participation and leadership in collaborative initiatives (UN PRI, Interfaith Center on Corporate Responsibility, Finance for Biodiversity, Nature Action 100)
- Public statements on policy issues (supporting the passage of the national FOREST ACT, the New York Tropical-Deforestation Free Procurement Act, the California Deforestation Free Procurement Act)

Source: Domini Impact Investments (2023). *Forest Engagement Overview*. Domini Forests Project. June 2023.

Domini has taken particular engagement interest in Indonesia, where its investment principles and beliefs regarding the protection of forests, indigenous communities, and biodiversity are coexisting. Indonesia is home to some of the world's largest intact forests, which provide shelter for endangered species and are home to many indigenous and local communities.

For more than a decade, Domini has engaged with Indonesian companies at the intersection of palm oil production and deforestation. Its engagement with one major food company in the region has been over ten years in the making, resulting in the company's first ever sustainability report, responsible palm oil sourcing commitment, and climate transition plan. Recently, as a result of government intervention, activism, and better corporate behavior, deforestation rates in Indonesia have gone down substantially. However, because deforestation risk still exists in many of Indonesia's rich biodiverse ecosystems, Domini has committed to further engagement work, pushing companies to consider action in order to prevent land grabs, end deforestation, and ensure respect for indigenous and local communities.[42]

c. Security selection & portfolio construction

Between 2019 and 2021, Domini developed and incorporated forest and biodiversity-related key performance indicators (KPIs) to use in company evaluations. Domini's KPIs are aligned with its Impact Investment Standards, which is a 70-page document developed to put the firm's principles into action.

In its Impact Investment Standards report, Domini lays out its process for determining which stocks and bonds are eligible for investment by Domini Funds.

- **Stocks and corporate bonds:** First, Domini asks "Is the company's business model aligned with Domini's firm's commitments to universal human dignity and ecological sustainability?" If not, the company is excluded from Domini's investment portfolios. Next, Domini considers how the company interacts with its stakeholders, including customers, employees, suppliers, investors, communities, and the natural environment. Companies that mismanage these relationships can generate financial, social, and/or environmental risk by mismanaging these relationships.

- **Non-corporate bonds:** Domini focuses on three outcomes when assessing non-corporate bond opportunities. Each outcome stems from the Domini Investment belief. The first is, will the issued bond increase access for populations underserved by the conventional financial community? The second is, will the issued bond create public goods for vulnerable populations? The third outcome Domini looks for is, will the issued bond fill capital gaps that have been created by current financial practice?

2. Adopting advanced techniques

a. Self-organization

Alongside its internal operations, Domini has made it a point to collaborate with likeminded investors to push systems-level thinking and responsible investing forward. It has done so by co-creating and joining industry-led organizations such as the following two examples.

In 2020, Domini joined 25 global financial institutions in signing the Finance for Biodiversity Pledge. By signing the pledge, Domini has committed itself to: collaborate and share its knowledge; engage with companies; assess impact; set targets; report publicly on its commitments by 2025.[43] Since joining, the pledge has grown to include 153 signatories that represent $22.7 trillion in AUM across 23 countries. In addition, Domini is a member of the Finance for Biodiversity Foundation's Advisory Board, where 11 representatives advise on how to best achieve the foundation's goal of reversing nature loss by 2030.[44]

In 2022, Domini and ten other investment firms announced the launching of Nature Action 100. Domini and its partners joined forces with the Institutional Investors Group on Climate Change, the Finance for Biodiversity Foundation, Planet Tracker, and Ceres to help organize Nature Action 100's operations.

The initiative aims to drive corporate action on tackling nature and biodiversity loss through means of corporate engagement.[45]

Through the Finance for Biodiversity Foundation and Nature Action 100 Domini has helped create a clear, consistent, and actionable set of recommendations for how companies can prevent biodiversity loss. Additionally, it has provided investors with an opportunity to organize themselves and build leverage, in order to more effectively promote corporate behavior that prevents biodiversity loss. In June of 2023, Nature Action 100 published the Investor Expectations for Companies, outlining six key focus areas and eight key industries. It plans to finalize a list of companies by the end of 2023 for Nature Action 100 members to begin engaging with via its published expectations.

A Nature Action 100 Focus Areas

Ambition

Publicly commit to minimize contributions to key drivers of nature loss and to conserve and restore ecosystems at the operational level and throughout value chains by 2030.

Assessment

Assess and publicly disclose nature-related dependencies, impacts, risks, and opportunities at the operational level and throughout value chains.

Targets

Set time-bound, context-specific, science-based targets informed by risk assessments on nature-related dependencies, impacts, risks and opportunities. Disclose annual progress against targets.

Implementation

Develop a company-wide plan on how to achieve targets. The design and implementation of the plan should prioritize rights-based approaches and be developed in collaboration with Indigenous Peoples and local communities when they are affected. Disclose annual progress against the plan.

Governance

Establish Board oversight and disclose management's role in assessing and managing nature-related dependencies, impacts, risks, and opportunities.

Engagement

Engage with external parties including actors throughout value chains, trade associations, policy makers, and other stakeholders to create an enabling environment for implementing the plan and achieving targets.

Source: Nature Action 100 (2023). *Nature Action 100 releases investor expectations to support urgent corporate action on nature loss.* June 26, 2023.

b. Polity

As mentioned above, Domini seeks to influence public policy in line with its goals of universal human dignity and ecological sustainability. It does so by identifying likeminded associations to engage with, supporting legislation at the federal and state level, and submitting comments to relevant government agencies. Below are three examples demonstrating Domini's efforts:

- Domini is an active member of the Investors Policy Dialogue on Deforestation (IPDD), where investors around the world convene to engage governments on stopping deforestation. Through the IPDD Domini is engaging the government of Brazil, calling for public policy that leads to a long-term halt of deforestation.[46]

- In 2023, Domini led a group of investors representing $2.3 trillion in AUM in dialogue with New York State legislators. On behalf of the investor group, Domini submitted a letter outlining the value of a well-designed forest policy that prohibits deforestation in state purchases. As a result of its lobbying efforts in Albany, New York's Tropical Deforestation-Free Procurement Act was passed by the State Assembly. If the bill is signed by the Governor, it will require companies doing business with the state of New York to have a transparent supply chain that does not contribute to tropical deforestation. The impact Domini can have by supporting the passage of the bill involves a wider scope than conventional corporate engagement methods, a key feature of system-level investing.[47]

c. Standards setting

Domini has set its own exclusionary standards, outlining five categories of business that are fundamentally misaligned with its goals of universal human dignity and ecological sustainability: weapons and firearms; nuclear power; fossil fuels; for-profit prisons and immigration detention centers; and alcohol, tobacco, and gambling.[48] Domini evaluates companies on a case-by-case basis but typically looks at its percentage of revenues, and market influence (leadership), and environmental and social track record in order to make a decision.

Domini Exclusion Categories

Created by Domini

In addition to developing its own exclusionary standards, Domini has incorporated credible external standards into its investment process. Standards developed by the Forest Stewardship Council (FSC) are a prime example. The FSC standards have a unique ability to identify companies in forest-product-intensive industries that are making changes to source more responsibly. Its credibility among nonprofit organizations and other firms in the space as the most effective forestry certification make FSC methods an integral part of Domini's research process. At the same time, Domini has voiced critical feedback to strengthen FSC's certification in areas of observed weakness.[49]

3. Evaluating Results

Domini has been reporting on and evaluating its results internally and externally since 2016. In addition to Quarterly and Annual Impact Reports that communicate the impacts of its forest and land use focus, Domini has conducted an internal self-assessment on the effectiveness of its investment approach and its influence on the forest system. Domini's goal for evaluating its results has been to map the relative impacts of its initiatives, determining which can be attributed to progress towards the forest project's goals and to what extent.

Saint Paul & Minnesota Foundation (SPMF) With approximately $2 billion in assets under management (AUM), the Saint Paul & Minnesota Foundation (SPMF) is the largest community foundation in Minnesota. Founded in 1940, SPMF's mission is to create "an equitable, just and vibrant Minnesota where all communities and people thrive."[50] It aims to do so through three core strategies: inspiring generosity by facilitating and amplifying individual philanthropic giving; advocating for equity – and racial equity in particular – through grantmaking and other activities, and; investing in community-led solutions to the challenges faced by local communities across Minnesota. SPMF's investment goal is to create a diversified portfolio that exceeds the foundation's annual 5% spending policy plus inflation.[51]

System-level investing strategy

SPMF launched its system-level investing strategy in 2019, under the leadership of Shannon O'Leary, the foundation's new Chief Investment Officer. It initially incorporated environmental, social and governance (ESG) themes, broadly speaking, with a highly intentional focus and deep engagement on diversity, equity, and inclusion (DEI) and **racial and gender equity**.

SPMF's motivations for developing the strategy were:

- Aligning SPMF's investments with the foundation's values and mission and ensuring that SPMF's investment portfolio was not propagating problems that the foundation was otherwise trying to solve (e.g., racial equity), either directly or indirectly.
- Investing for impact alongside financial return and leveraging the foundation's approximately $2 billion in AUM to amplify SPMF's approximately $100 million in annual grantmaking.
- Increasing alpha and better managing downside risk management by working with investment managers with strong commitments to ESG and DEI, which research indicates outperform their peers without such commitments.
- Responding to increasing demands from the foundation's donors to adopt such a strategy and giving SPMF a competitive edge when it comes to attracting additional donor funds.
- Influencing a marked increase in the racial and gender diversity of the financial industry, broadly speaking.

Developing the strategy

- **Stakeholder management.** Establishing SPMF's system-level investing strategy required obtaining buy-in from stakeholders including the foundation's executive leaders, board of directors, and investment committee. The investment team met individually with these stakeholders over the course of about six months throughout 2019, helping them to understand how the investment team managed the foundation's portfolio, explaining the motivations for the system-level investing strategy, and gaining their buy-in for the approach.

- **Audit of existing practices.** Throughout 2020, SPMF's investment team reviewed the foundation's existing ESG, DEI, and racial/gender equity focused investment policies, producers, and materials (e.g., manager surveys), identified ESG and racial/gender equity data providers for use in developing comprehensive and replicable manager assessment processes, and established initial benchmarks of SPMF's investments related to ESG, DEI, and values alignment for use in tracking investment managers' progress over time. The investment team also looked to the principles established by the U.N.-backed Principles for Responsible Investment (PRI) to guide development of the system-level investing strategy.[52]

Ensuring successful adoption of the strategy

SPMF describes the following as critical to facilitating the successful launch of its system-level investing strategy, and as important to its ongoing implementation and overall effectiveness:

1. Use of simple, straightforward language to explain investment concepts to stakeholders and to generate their buy-in.	All stakeholders were generally supportive of the strategy given SPMF's overall focus on racial and gender equity and the investment team's commitment to investing the foundation's assets in alignment with its values (rather than in conflict with them). The investment team describes their use of simple, straightforward language to explain potentially intimidating investment concepts with stakeholders as crucial to obtaining this buy-in (e.g., "we have an obligation to know if there are investments in our portfolio that are causing the problems we are trying to solve with our grants").

2. Focus on engagement and improvement over time.	Instead of requiring managers to meet minimum thresholds for investment managers' ESG and DEI performance, SPMF focuses on encouraging progress over time – progress related to both their commitment to ESG and DEI and to their adoption of related policies and practices. System-level progress is not achieved, according to SPMF, through "canceling" – or divesting from – managers with poor ESG and DEI scores. Rather, system-level progress is best achieved through meeting managers where they are in terms of ESG and DEI, generating their buy-in for the advantages of improving across both fronts, and engaging with them one-on-one to learn about their successes and challenges and to provide related encouragement and support.

1. Extending conventional techniques

a. Statement of investment beliefs

A firm's interest in managing systemic risk and opportunity is often communicated via their SIB. However, firms will communicate this intent through other statements, including, for SPMF, an Investment Policy Statement. SPMF updated its Investment Policy Statement in 2020 to reflect its commitment to aligning its investment activities with the foundation's values and mission, and to specify how it will integrate ESG considerations into investment decision-making and how it will address DEI and racial/gender equity in its investment portfolio. According to the policy, SPMF believes that material ESG factors impact investment performance and are critical to long-term sustainability – as are DEI and racial/gender equity – and, accordingly, will:

- Align its investment practices with PRI principles and integrate ESG considerations throughout all investment decision-making and across all asset classes.
- Instruct investment managers to consider ESG factors when sourcing investments for SPMF and to integrate ESG factors into proxy voting and shareholder and other engagement.
- Regularly monitor the ESG performance of asset managers.

- Conduct periodic surveys of managers to assess their racial/gender equity policies and practices.

- Consider racial equity goals when hiring new managers, including identifying candidates that represent an upgrade in DEI and ESG alignment for required return/risk than currently in portfolio, including BIPOC-owned businesses in searches, and reviewing candidates' racial/gender equity policies and practices.

Present within its Investment Policy document, the Saint Paul & Minnesota Foundation has published an Investment Philosophy. It cites directly from the organization's mission statement and commits the investment team to following a strategy that only amplifies its mission. For example, the investment team is committed to investments that align with the Foundation's grantmaking in the community it serves. The investment team is also committed to evaluating its investments for ways that it does or does not, "inspire generosity, advocate for equity, and invest in community-led solutions."[53]

b. Manager due diligence

Central to SPMF's system-level investing strategy is its manager due diligence activities. Research cited by SPMF suggests that asset owners can increase alpha and better manage downside risk by working with investment managers with strong commitments to ESG and DEI, which research indicates outperform their peers without such commitments. Specifically, the research indicates that (a) homogeneous leadership teams are less innovative, more susceptible to harmful "group think", and perform worse than racially and gender-diverse decision-making teams; and that (b) diverse investment teams are consistently over-represented in the top quartile of performers.

With this research in mind, SPMF conducts annual assessments of its investment managers' commitment to ESG and ESG performance, and bi-annual (every two years) assessments of their commitment to DEI and DEI performance. SPMF bases its ESG assessments on data from four sources:

- Third-party ESG data provided by Sustainalytics.[54]

- Data reported by managers (ESG policies and procedures [including integration of ESG into investment decisions], proxy voting details, and ESG reporting).

- Observations by the SPMF investment team and discussions with managers (is the manager comfortable with the discussion itself? can they provide examples of how they have integrated ESG on a deal-by-deal basis?).

- Investee-reported data (e.g., things like LEED certification).

The foundation collects information for its bi-annual DEI assessment via its investment manager diversity survey that asks about firm-wide gender, ethnic, and racial diversity. The survey asks about diversity at all personnel levels but focuses on the diversity of the firm's ownership and investment decision-makers.

SPMF supplements its annual ESG assessments and bi-annual DEI assessments with one-on-one discussions with managers about their ESG and DEI commitment and performance, noting that such meetings are critical to fully understanding managers' ESG and DEI practices and challenges that might be hindering progress. One manager, for example, scored poorly on their DEI assessment despite their increasing commitment to DEI. It was only because of a follow-up discussion that SPMF learned that the manager was intentionally recruiting women and people of color to participate in internships, allowing the manager to then write interns recommendation letters to get into the requisite training programs, with the goal of offering them regular employment after they receive the training.

SPMF uses the results of these ESG and DEI assessments and one-on-one meetings to engage with managers to drive improvement over time.[55] SPMF focuses on "meeting managers where they are" and eliciting their commitments to improve and further integrate ESG and DEI going forward. According to SPMF, managers' willingness to engage with SPMF related to improving their ESG and DEI performance is as important, if not *more* important, than the performance metric itself. SPMF has, however, terminated relationships with three managers due to a combination of underperformance, lack of diversity, and unwillingness to commitment to ESHG and DEI improvement over time. SPMF's investment team noted that most, if not all, of its investment managers are staffed by generally high-performing and high-achieving individuals that are not used to getting "bad grades" and are therefore very motivated to improve their ESG and DEI performance if they score poorly on the related assessments. SPMF's transparency with managers on both the raw scores and how the scores were developed is a critical catalyst for managers' willingness to adjust their practices. 100% of the managers in the SPMF portfolio indicated that SPMF is the only organization that provides complete transparency on ESG and DEI assessments.

SPMF summarizes managers' ESG, DEI, and racial equity performance and progress over time via a proprietary scorecard that it shares with its investment committee each year. Depending on whether the manager is in the public or private markets, the scorecard, excerpted below, includes some combination of:

- An ESG Risk Exposure score (asset's exposure to industry-specific, material ESG risk);
- An ESG Risk Management score (how well an asset is managing identified risk exposure);
- An ESG Risk Rating (degrees of unmanaged ESG risk of an asset);

- An ESG Risk Rating (degrees of unmanaged ESG risk of an asset);
- ESG management practices of each fund as determined by SPMF; and
- ESG performance of the underlying industries of each fund, using industry averages;
- SPMF's custom values alignment index, which combines DEI survey information with ESG performance information to measure the degree to which assets advance or inhibit SPMF's strategic priorities.

2. Adopting advanced techniques

a. Self-organization

SPMF became the first U.S. community foundation signatory of the Principles for Responsible Investing (PRI) in 2022, enabling SPMF's investment team to connect with "like-minded institutional investors who are also trail blazers in this field."[56]

SPMF's decision to join PRI provides it with a globally recognized and highly credible standard, which further demonstrates its system-level investing commitment. In this effort, SPMF is going beyond the typical firm-level engagement that investors allocate resources towards and supporting a community of asset owners and managers that want the allocation of their capital to generate positive outcomes.

SPMF is a member of the Institutional Allocators for Diversity, Equity, & Inclusion (IADEI). This organization is a consortium of asset owners that seeks to drive DEI within institutional investment teams and portfolios in investment management. Significant areas of focus include directing capital toward diverse fund managers, enhancing the efforts of other nonprofits with similar goals, engaging with influential market participants, and facilitating access to research related to DEI in asset management. SPMF benefits from this network as a source of diverse-led managers across asset classes and a venue to recommend SPMF-sourced diverse-led managers utilize for promotion of their fund offerings.

b. Standards setting

SPMF contributed to the development of PRI's Diversity, Equity, and Inclusion Due Diligence Questionnaire (DDQ) in 2022[57] as part of its efforts to "more intentionally use [its] investment dollars to drive change in the investment industry… [and to] make it easier for other foundations and endowments to join [the foundation in] initiating this change in their portfolios."

By contributing to the DDQ, SPMF is providing a standards resource to all asset managers investing in fixed income, public equities, hedge funds, private equity, real estate and infrastructure assets. Cutting across asset classes and sectors, the DDQ has the potential to systematically raise the bar by which asset managers can track their DEI impact.

University Pension Plan Ontario (UPP) is a jointly sponsored defined benefit pension plan created by and for Ontario's university sector. UPP manages $10.8 billion in pension assets and proudly serves over 39,000 working and retired members across 16 participating universities and sector organizations.

System-level investing strategy

Following its launch in July 2021, UPP established a three-year strategic plan to guide its operations from 2022 to 2025.[58] To develop its strategic plan, UPP engaged various stakeholder groups, including members and Plan Sponsors (which include university employers, faculty associations, and unions). The plan enshrines purpose and systems resilience into its investment approach.[59]

As part of its 'Lean into ESG' pillar, UPP recognizes that, as a long-term investor, its ability to fulfil its generational responsibilities to derive and protect sustainable value to current and future members rely on "a healthy, functioning market, society, and environment."[60] This language publicly signals UPP's incorporation of systemic risks into its investment practices.

Developing the strategy

In March of 2022, UPP conducted a survey and a series of discussion forums with plan members on responsible investing priorities and approaches as an important input to its holistic strategy.[61] The survey established a baseline understanding of member opinions and beliefs, an ongoing component to UPP's member engagement and strategic development practice.

UPP Strategic Plan 2022 - 2025

Created by UPP University Pension Plan Ontario

A majority of respondents said UPP should prioritize responsible investing as a means for building long-term, sustainable value, with combatting climate change identified as their top priority. UPP's proactive engagement helped it establish a base understanding of its members' viewpoints, guided the development of its strategies, and helped build trust with members early in the organization's journey.

Following its member engagement, UPP announced its Climate Action Plan in mid-2022, committing to a net-zero portfolio by 2040 or sooner, with interim targets, and an emphasis on decarbonizing the real economy.[62]

1. Extending conventional techniques

a. Statement of investment beliefs

UPP partnered with The Investment Integration Project and Sinclair Capital to develop a statement of investment beliefs that communicates the *why* of its investment program.

The eight specific beliefs[63] (outlined below) guide its strategies and decision-making processes. These acknowledge that long-term sustainable growth depends on action grounded in strong, clear values, and recognize that UPP has a responsibility to promote the health of the capital markets and the financial, social, and environmental systems on which capital markets rely.

Its investment beliefs are also embedded into its Statement of Investment Policies and Procedures, where a Responsible Investing section states UPP's recognition of its responsibility to "consider the plan's stakeholder interests and real-world impact, as well our contribution to a just, sustainable society and economy."[64] In this section, ESG factors are described as essential to creating long-term value and managing risk. UPP's Responsible Investing Policy[65] further details UPP's approach to ESG integration, stewardship, and reporting.

The Responsible Investing Policy, which is informed by UPP's Investment Beliefs, defines responsible investing as "the integration of ESG considerations into investment management processes and stewardship practices, focused on those factors that could have a material impact on financial performance and the environmental, social, and financial systems upon which capital markets rely."[66]

UPP's guiding investment beliefs:

- UPP invests with a purpose: to fulfill the pension promise to members, now and in the future.
- As a long-term investor, UPP has a responsibility to promote the health of the capital markets and the financial, social, and environmental systems on which capital markets rely.

- Creating value and managing risk involve exercising UPP's voice to influence outcomes related to material issues through active ownership, policy advocacy, and collaboration with other investors and stakeholders — all of which must be approached with the same intention and rigor as selecting investments.

- All aspects of investing should be forward-looking and intentional. Successful investing requires rigorous research and analysis, alignment with UPP's capabilities, and focused innovation

- Culture is an essential investment input. How we invest should reflect UPP's culture of collaboration and forward vision.

- UPP embraces partnership as a foundation for enhanced performance and impact.

- Costs are an asset that should be treated as judiciously as any other plan asset. The goal is neither to reduce costs to the lowest possible level, nor squander a plan asset. Rather, the goal is to employ costs wisely in delivering a secure pension promise.

- Transparency engenders trust. Our investment of members' pension earnings has bearing on their retirement security; they have a right to know how we approach and perform that responsibility.

UPP's Investment Beliefs emphasize the importance of healthy financial, social, and environmental systems to achieve sustainable, long-term investment returns, and to ensure its current and future members can retire well. By integrating a systems-level approach to its investing, UPP is better positioned to manage risk, derive and protect value, and contribute to healthy, resilient, and sustainable capital markets.

UPP's Investment Beliefs also articulate the need to actively engage with companies, advocate with policymakers and regulators, and partner with peer investors and others for enhanced performance and impact. Such actions receiving attention in an investment belief statement instruct UPP to act as a systems-level investor and set an expectation for the adoption of advanced techniques described below.

b. Security selection & portfolio construction

In 2022, UPP published its Climate Action Plan, outlining the steps it will take to a net-zero portfolio by 2040 – a decade earlier than many others. The Climate Action Plan acknowledges that UPP's ability to achieve investment returns and provide retirement benefits depends on a stable climate; and in turn, its investments affect the stability of the climate. It also acknowledges the materiality of climate change on its investments, stating that, "UPP's ability to realize adequate investment returns and provide retirement benefits depends on a stable climate; and UPP's investments affect the stability of the climate."[67]

UPP's security selection is directly impacted by its view of climate as material to its investments. The Climate Action Plan[68] outlines four overarching commitments that will structure UPP security selection:

1	2	3	4
Evaluate climate-related risks, opportunities, and impacts of our current and prospective investments at the total fund and investment mandate levels.	**Invest** in climate solutions in line with the transition to a net-zero world and reduce the GHG intensity of our assets.	**Engage** with portfolio companies and market actors, including asset managers, to encourage a transition to a resilient, low-carbon, net-zero world, and sufficient-climate disclosure.	**Advocate** for public policy and market systems that support limiting the global average temperature rise to 1.5 degrees Celsius.
Commitments: • Implement a climate transition investment framework and evaluate our portfolio. • Integrate climate risk and opportunity assessment into investment strategy and processes.	**Commitments:** • Invest only in new mandates and assets that align with the transition to a net-zero world. • Reduce our portfolio's carbon footprint by 16.5% by 2025 and 60% by 2030 from a 2021 baseline. • Set a target for new investments in climate solutions and selectively exclude investments in companies that present significant climate risk.	**Commitments:** • Engage with at least 20 companies through collective and direct engagement. • Engage with external investment managers to encourage their engagement with companies and emissions reductions.	**Commitments:** • Participate in direct and collective advocacy with policymakers. • Join the UN-convened Net-Zero Asset Owner Alliance and support industry initiatives that advance climate action.

UPP hopes for its strong public climate commitments to send a signal to all companies demonstrating the importance of decarbonization and the heavier flow of capital to those who take it seriously.

c. Engagement

UPP believes that collaborative engagement is an integral part of value creation, risk management, and improved corporate behavior. The following examples demonstrate how UPP approaches collaborative engagement:

1. With the support of the Shareholder Association for Research and Education (SHARE), UPP is able to broaden its engagement with public companies on the topics of climate action, reconciliation, and human rights.[69] UPP joined the University Network for Investor Engagement, a SHARE initiative that brings together some of Canada's most prominent universities. The strengthened voice of the university network led to successful negotiations with a Canadian bank to measure and report on carbon risk in its lending portfolio.[70] This sets the stage for enhanced accountability and the potential raise the bar on climate reporting for all Canadian banks.

2. UPP is a member of the 30% Club, which collectively engages companies to improve gender diversity at the board and executive level. Through its membership of the 30% Club Canadian Investor Group, UPP has joined 20 other Canadian institutional investors in engaging Canadian companies on gender and racial diversity, and is currently leading engagement with two large companies. UPP is calling for improved DEI disclosures at both companies, including published policies and targets to ensure accountability and progress.

3. UPP is a member of the Canadian Coalition for Good Governance (CCGG), which collectively engages company boards to improve their corporate governance practices. A key focus of this collective engagement effort has been enhanced disclosures. Between 2020-2022, CCGG engaged 16 companies on their environmental and social disclosures, and 15 companies implemented CCGG's requested improvements.[71]

As demonstrated in the above examples, UPP is committed to improving the long-term performance of its assets, to support its purpose of long-term value creation for members today and for generations to come. Each engagement example demonstrates that UPP is encouraging companies inside and outside of its portfolio to fundamentally improve their environmental, social, and governance practices. These engagements extend past the individual firm-level, and to collaborative market-wide and public policy engagement. Furthermore, by partnering with peer investors and other organizations, UPP is able to enhance the impact of its stewardship, while also gaining access to global tools, research, networks, training, and other resources which help to advance best practices within its own operations.

Through its involvement in the 30% Club, in particular its Canadian chapter, and in CCGG, UPP is leveraging its unique knowledge and expertise of Canadian challenges, opportunities, and other relevant information and relationships to strengthen systems in its own backyard.

Proxy voting is another key tool that UPP leverages in its engagement activity, to support long-term value creation for its beneficiaries by exercising its voting rights and responsibilities, articulating its environmental, social and governance (ESG) oversight expectations. It has established a Proxy Voting Policy, reviewed annually, that states its positions on a number of issues it recognizes as relevant to enhancing the long-term economic interests of shareholders.[72] UPP has made its Proxy Voting Policy and its votes and rationale public, to ensure transparency about its voting on issues including executive compensation, climate disclosures, DEI, lobbying, and more. The policy is directly linked to UPP's Responsible Investing Policy, which embeds a system-level investment approach throughout UPP's investment management activities.

d. Manager due diligence

In addition to evaluating managers on their track-record of long-term sustainable performance, UPP aims to partner with fund managers that are aligned with UPP's Investment Beliefs and responsible investing ambitions. UPP partners closely with external managers to encourage and support their progress on integrating responsible investing factors and approaches into their operations, recognizing that building long-term relationships is essential to long-term value creation.

For example, UPP's external manager due diligence includes assessing a prospective partner's approach to equity, diversity, inclusion, and reconciliation, including the manager's policies, roles, responsibilities, targets and progress and against them, and representation throughout the company. Furthermore, UPP assesses the way potential partners integrate diversity through the investment lifecycle and their stewardship activities,[73] including the manager's own engagement, proxy voting, and advocacy work.

2. Adopting advanced techniques

a. Self-organization

In the two years since its launch, UPP has joined strategic partnerships and associations[74] in order to advance its commitment to systems resilience. At an international level, UPP is a member of the Principles for Responsible Investment, the Net Zero Asset Owners Alliance (NZAOA), Climate Action 100+, and a participant of the Ceres Investor Network on Climate Risk and Sustainability. At a domestic level, UPP is actively involved in Climate Engagement Canada.

Climate Engagement Canada was created, with UPP as a founding member, in order to lead a nation-wide engagement program with high-emitting Canadian issuers across multiple sectors on climate risk governance, disclosure, and the transition to a low-carbon economy in Canada. CEC's steering committee, which is chaired by UPP's CEO Barbara Zvan, drives its strategic approach to convening finance and industry.[75]

A key CEC outcome is the CEC Net Zero Benchmark. It provides a set of common standards for investors to evaluate corporate issuers' progress towards aligning with the Paris Agreement. In total, CEC has brought together 38 participants with $4.6 trillion in AUM, all pledging to promote a just transition to a net zero economy.[76]

CEC has selected a focus list of Canadian companies to engage. Their common characteristic is an identified opportunity to accelerate the low-carbon transition and act as an industry leader on climate.

By choosing not to focus on a particular industry and by encouraging improved reporting and accountability standards across the Canadian economy, CEC is attempting to have a systemic impact on climate.

b. Polity

UPP recognizes it has a responsibility to advocate for sustainable public policy in order to ensure healthy markets that are capable of driving long-term value for its members. UPP communicates with regulators and policymakers, both independently and together with peer investors and other organizations. UPP publishes its statements and submissions on its website, for added transparency about its advocacy.

In 2022, UPP issued 10 public submissions to agencies, including the Ontario Securities Commission, the U.S. Securities and Exchange Commission, and the International Sustainability Standards Board. In most cases, UPP called for improved regulation of corporate disclosures of environmental, social, and governance risks and opportunities across industries,[77] demonstrating its focus on systems.

A Deeper Dive: UPP and Canada's Sustainable Finance Action Council

The Sustainable Finance Action Council (SFAC) brings together the Canadian government and the country's 25 largest financial institutions, along with official sector representatives such as the Bank of Canada and the Office of the Superintendent of Financial Institutions. It serves as a center of expertise, partnership, and dialogue to foster the growth Canada's sustainable finance market and mobilize investment toward the net-zero transition.

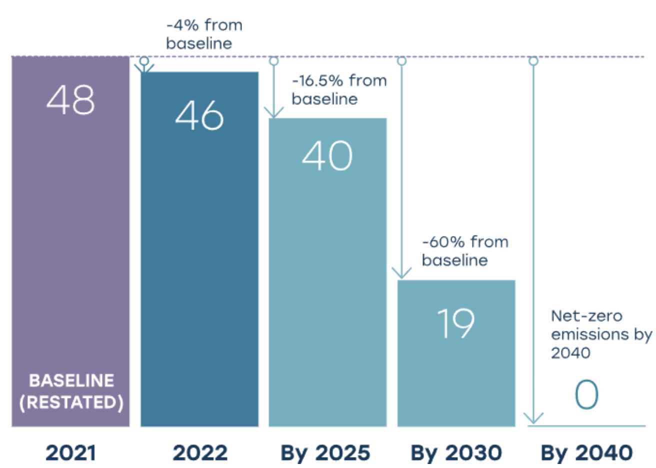
In early 2023, SFAC published a Taxonomy Roadmap Report with recommendations for a uniquely Canadian framework for developing a green and transition taxonomy, with standardized, science-based definitions. UPP's CEO, Barbara Zvan, led the report's development as chair of SFAC's Taxonomy Technical Expert Group, alongside UPP Board Trustee, Kathy Bardswick, in her role as SFAC Chair.

Providing clarity on the definition of green and transition investments is a foundational act to allowing for systemic improvements on climate. By standardizing what a climate-compatible investment may entail, various actors from investors to corporations to municipalities may speak a common language. UPP's backing of the taxonomy report adds credibility to and further promotes its system-level efforts.

c. Standards setting

UPP's Climate Action Plan details the frameworks and measurements UPP will use to assess investments, and incorporates the work of credible target-setting bodies such as the NZAOA, TCFD, and Paris Aligned Investment Initiative to ensure its disclosures and approach to decarbonizing are in line with best practices.[78]

UPP Carbon Footprint Goals



Created by UPP UNIVERSITY PENSION PLAN ONTARIO

In order to report transparently, UPP has published its methodology for assessing its carbon footprint, which is aligned with the Greenhouse Gas Protocol, ensuring a high level of transparency into its calculated carbon emissions which will keep track of UPP's progress towards a net-zero emissions portfolio.

UPP developed a Climate Transition Investment Framework that enables it to systematically evaluate the transition alignment and readiness of its portfolio and new investment opportunities, set targets for climate solution investments, and refine its approach to climate-related investment exclusions.[79]

UPP also has public standards for its investment exclusions. Its Investment Exclusion Policy is updated every two years and is approved by the Board of Trustees. It includes general parameters such as industry exclusions, approved by the Board of Trustees, in addition to specific entity exclusions, approved by the Management Investment Committee. The policy holds UPP's CEO accountable for its implementation and UPP's Chief Investment Officer, Investments team, and Responsible Investing team accountable for adhering to the policy. UPP's Investment Exclusion Policy considers global and regional frameworks, as well as other relevant factors, including the Paris Agreement, the OECD Guidelines for Multinational Companies, and potential for financial and reputational loss due to ESG issues.[80]

The public nature of this policy, as well as its detailed accountability framework, sets a clear expectation for investees and a clear tone for other institutional investors.

Wespath Benefits and Investments is a nonprofit pension fund and a general agency of the United Methodist Church (UMC). Created by the UMC's legislative body, the General Conference, Wespath provides over 100,000 UMC members with pension and benefit programs. Additionally, it provides investment services to 150 UMC-related institutional investors. With over $24 billion in assets under management (AUM), Wespath is one of the largest faith-based pension funds in the world.

Wespath's mission is for its investments to have a positive financial, social and environmental impact, while abiding by UMC values. The Wespath Fiduciary Committee approves the Investment Policy, which sets the structure and purpose of the investment program. It also approves new investment funds, asset classes and investment strategies; monitors investment performance and fund risks; and ensures that fiduciary duties and a commitment to UMC Social Principles are carried out in its sustainable investment program.

System-level investing strategy

Wespath takes an "invest, engage, avoid" approach to its investment strategy.[81] This approach combines conventional and sustainable investing techniques with advanced, system-level techniques in an effort to manage risk and abide by the Wespath investment philosophy (expanded upon below).

The Wespath Sustainable Economy Framework has an important influence on its investment strategy. The framework outlines a vision of "long-term prosperity for all, social cohesion and environmental health." Wespath believes that achieving this framework will result in the creation of healthy financial markets, resilient companies, and ultimately greater market returns.

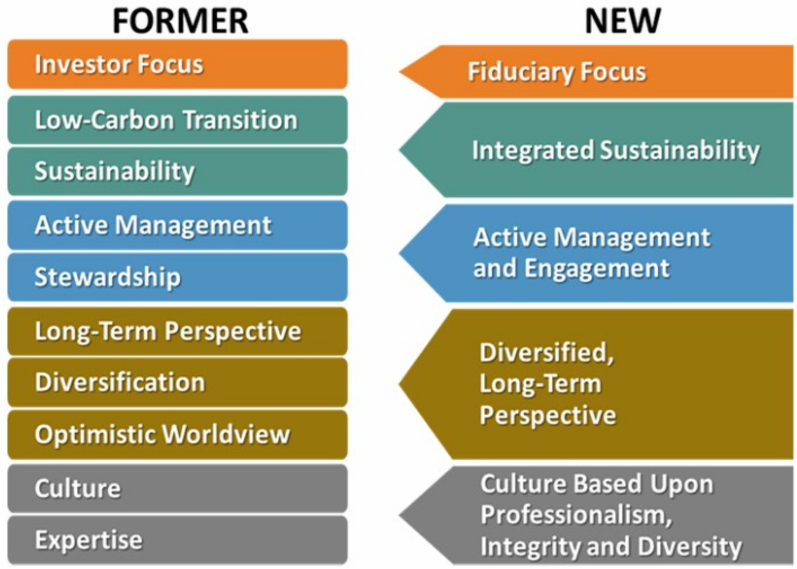
1. Extending conventional techniques

a. Statement of investment beliefs

Wespath first published a set of 10 investment beliefs in 2016. In early 2023, Wespath's Investments division, senior leadership team, and its Board of Directors collaborated to consolidate its 10 previous beliefs into five investment beliefs.[82]

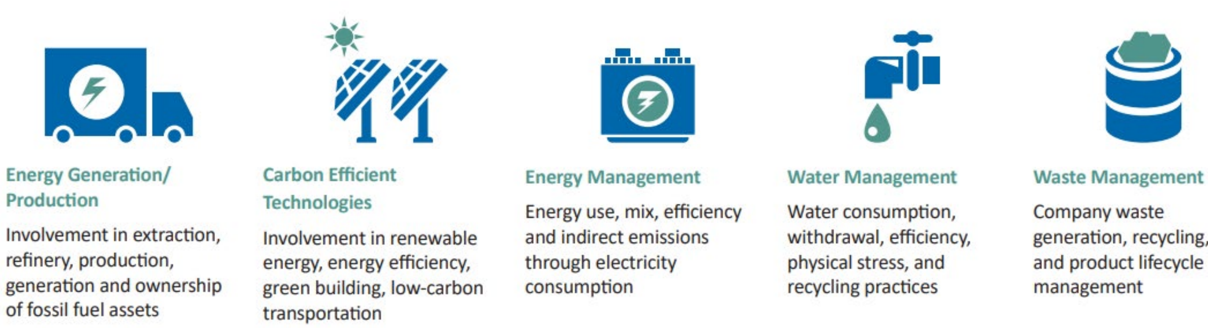
Wespath refines its beliefs on an ongoing basis as it identifies new values and specific ways to communicate its investment approach. For example, Wespath added a Low-Carbon Transition belief and accompanying Climate Action Plan in 2018 to reflect its view that climate change is a systemic risk. This led to a partnership between Wespath and BlackRock, the largest asset manager in the world, who together produced the Wespath Transition Ready Strategy. The strategy identifies business models that are most prepared for the low-carbon transition, generating confidence for Wespath to invest 6% of its total assets in low-carbon strategies.

Wespath Investment Beliefs 2016 ➡ 2023



Created by Wespath

Wespath's five pillars used to evaluate company Transition Readiness



Created by Wespath

In addition to its five investment beliefs, Wespath follows a Sustainable Economy Framework (SEF), which provides the foundation for its sustainable investing program and a lens by which to identify new investment opportunities. The SEF specifies Wespath's definition of a sustainable global economy, which it considers necessary to create healthier financial markets and more resilient companies. The SEF includes the following three pillars and corresponding goals:[83]

1. Long-term prosperity for all: achieve equal opportunity for advancement and access across gender, race, and economic background.

2. Social cohesion: achieve reliable access to basic necessities including sustainable food and water, clean energy, and affordable housing.

3. Environmental health: develop resilient ecosystems by combatting climate change, biodiversity loss, plastic waste, and other polluting activities.

b. Security selection & portfolio construction

Multiple initiatives allow Wespath to act on its belief that climate change is a systemic risk. Its Transition Ready Investment Strategy provides an enhanced passive investment approach, overweighting companies that are carbon-efficient (investing in carbon technologies, reducing carbon emissions, using natural resources sustainably) and underweighting companies that are poorly positioned for a low-carbon economy. As a result, Wespath's portfolio has had a 50% reduction in carbon emissions intensity and a 40% increase in climate technology exposure relative to its performance benchmarks (Russell Top 200 Index and the MSCI World ex USA IMI Value Index).[84] Since its initial commitment of $750 million to the launch of the Transition Ready strategy, Wespath has more than doubled its investments into low-carbon ready securities.

In addition to targeting specific investment opportunities, Wespath utilizes a Management of Excessive Sustainability Risk (MESR) policy to identify for exclusion investments that do not align with its climate action beliefs. The MESR describes two types of exclusions:[85]

1. **Ethical exclusions:** When a company's revenue is more than 10% reliant on the production, sale, distribution, and/or marketing of alcohol, tobacco products, adult entertainment, weapons, gambling, privately-operated correctional facilities.[86]

2. **Sustainability-related financial risk exclusions:** When a specific issue or set of companies or industries expose investors to higher levels of financial risk, the Wespath board of directors creates a set of guidelines for the particular issue. To date, guidelines have been set for two issues:

   a. The **climate change** guidelines focus on the extraction or mining of thermal coal, excluding with 64 exclusions having been made since its inception.

   b. The **human rights** guidelines exclude companies operating in, and sovereign debt from countries with a track record of, human rights violations. Since its inception, 35 companies and the debt of 12 countries have been excluded.[87]

c. Engagement

Although Wespath has a formal exclusion policy, its investment philosophy prioritizes engagement. Written within Wespath's investment beliefs include the conviction that shareholder engagement adds long-term value to its funds.[88] The UN Principles for Responsible Investment (PRI) serves as a foundation for Wespath engagement work, allowing for greater potential for collective engagement opportunities.

In 2021 and 2022 Wespath recorded over 120 engagements with asset managers and companies on topics related to climate change, human rights, and diversity and inclusion. Outcomes of Wespath shareholder engagement activities include:

- Incorporating legal settlement charges in pharmaceutical executives' compensation (related to the opioid crisis).
- Agreement from Tripadvisor and Booking Holdings to engage on the development of a human rights policy following a shareholder resolution.
- The publishing of climate risk reports by Oxy and Chevron following Wespath shareholder resolutions and executive team meetings.
- A commitment by Cummins Inc to align its lobbying activity with the Paris Agreement.[89]

A notable element of Wespath's shareholder engagement activity is its proxy voting approach, which is approved by its Board of Directors and outlined in its Proxy Voting Guidelines. Wespath uses the expertise of Institutional Shareholder Services (ISS) and other data sources to execute on its proxy voting strategy. Some examples of Wespath engagement activity across themes includes:[90]

1. **Environmental:** In 2020, Wespath joined the hedge fund Engine No. 1 in getting three board members with expertise on the low-carbon economy elected onto Exxon Mobil's Board of Directors. Since the new appointments have joined, Exxon has continued to be accused of expanding its oil and gas production. However, it has also introduced net-zero targets as well as investment into carbon capture and clean energy technologies such as hydrogen-based energy. Although there are contrasting opinions on the total impact the new board members have had thus far, it must be acknowledged that a healthy environmental system is now of interest at the board level of one of the world's largest oil and gas companies.

2. **Social:** In 2021, Wespath supported a shareholder resolution for JP Morgan to perform a racial equity audit to examine how its $30 billion dollar commitment to supporting black, indigenous and people of color communities has been allocated. As a result, in November of 2022 JP Morgan published a *Racial Equity and Commitment Audit Report* outlining where its committed resources have gone thus far.[91] This is a step in the right direction for increasing accountability as the publication of such an audit report, at the very least, allows the public to determine whether JP Morgan's activities are in line with its commitments. It is important to note that many stakeholders found the report lacking in detail and progress. However, it remains an important example of how shareholder engagement can lead to iterative improvements by companies.

3. **Governance:** In 2022, Wespath supported a shareholder proposal for Netflix to produce a lobbying report that would codify its lobbying policies and procedures; disclose all expenditures; and explain all the company's decision-making practice for its lobbying activity.[92] While Netflix has yet to produce such a report, this is an important example of Wespath's engagement process targeting systems-level change. With this engagement, Wespath presents itself as an owner who corporate transparency to political risk, raising the standard by which it expects its holdings to report against.

With its headquarters in Illinois, Wespath has made a targeted effort to practice its shareholder engagement activities in the American Midwest. This has been done through the Midwest Investors Diversity Initiative (MIDI), which engages companies on board diversity.

In 2019 and 2020, MIDI engaged 22 companies that subsequently added, or committed to add, at least one diverse board member. The number of MIDI-engaged companies adopting board diversity practices has increased over time, going from 13 in 2020 to 18 in 2022. This cross-industry initiative is setting improved standards for corporate governance practices, a step in the right direction for making a systemic impact on DEI.[93]

d. Manager due diligence

Wespath's Investment Policy includes a requirement that the Wespath board ensure its external asset managers consider environmental, social, and governance (ESG) factors across asset classes. The policy also outlines a Women and/or Minority Owned Manager Program, which aims to retain high quality firms that are owned by women or members of a minority group.

As part of its external manager selection process, Wespath applies an internal ESG Appraisal to assess and monitor manger policies and practices.[94] Wespath has been iterating on its appraisal process since 2014 and it now includes the following:

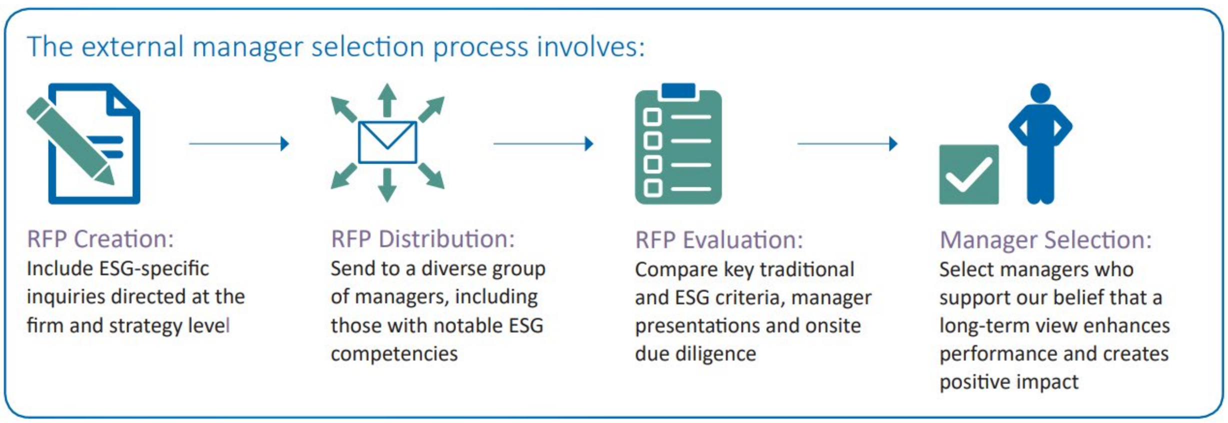
- **ESG Integration Reporting Questionnaire** that mangers complete with their annual reporting requirements. The questionnaire covers ESG integration at the organizational, or firm-level and at the individual strategy, or mandate-level.

- **Guidance Document** highlighting the degree of detail that should be included in the questionnaire.

- **Performance Snapshot** uses manager responses to provide general feedback to each external manager.

- **Individual Manager Assessment** uses manager responses to provide individualized feedback to each external manager, encourage progress, and increase alignment with Wespath expectations and beliefs.

Wespath external manager selection process



Created by Wespath

2. Adopting advanced techniques

a. Self-organization

Wespath has made self-organization techniques a key part of its investment activities through leadership positions in specific asset-owner alliances as well as through active engagement in other strategic partnerships. Its leadership positions are the following:

- **Principles for Responsible Investment (PRI).** Wespath was a co-author and founding signatory to the UN-backed PRI. It currently serves on the UNPRI's Stewardship Advisory Committee, where it recommends expectations to be set regarding PRI signatories' active ownership practices.

- **Investors for Opioid and Pharmaceutical Accountability (IOPA).** Wespath is co-chair of the IOPA, where it convenes investors to produce better governance structures at opioid producing companies. As a result of IOPA engagements, Wespath has helped achieve the appointment of independent board chairs at major pharmaceutical companies, increased the publication of opioid risk reports, expanded disclosure on pharmaceutical lobbying practices, and has aligned executive compensation with better opioid practice.[95]

- **Net-Zero Asset Owners Alliance (NZAOA).** Wespath is co-leading the engagement and communications working groups at the NZAOA. The engagement group is tasked with developing relationships with sector companies and asset managers while the communications working group ensures that NZAOA is publicly communicating its initiatives and progress.[96]

A Deeper Dive: Wespath & The Net Zero Asset Owners Alliance (NZAOA)

A key outcome from Wespath's work with the NZAOA's engagement and communication working groups has been a 2022 report called *The Future of Investor Engagement: A call for systematic stewardship to address systemic climate risk.*

The report lays out limitations to, and recommendations for expanding, conventional corporate engagement strategies. Cited limitations highlight the significant resources needed for effective corporate engagement and the lack of scaling that happens with most investor corporate engagement strategies. Most commonly, investors are engaging with individual, publicly listed companies as they are typically the largest holdings in a given portfolio. This results in a given investor missing a system-level engagement opportunity, for example via regulation that would affect all publicly listed companies, as its resources become committed to influencing a single large company's behavior.[97]

The report's recommendations educate investors on how existing corporate engagement strategies can be altered in order to positively affect systems rather than exclusively individual companies. Recommendations focus on three themes:

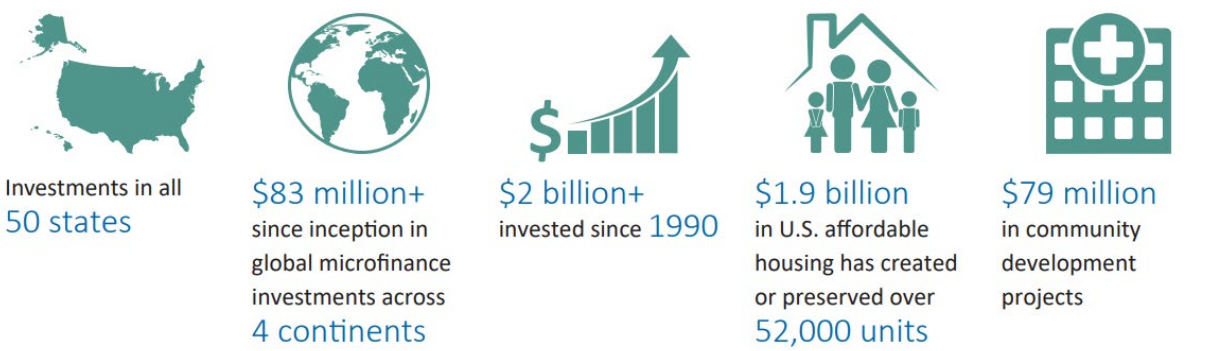
1. **Sector/value chain engagement** Investors can redirect their engagement efforts towards the development of incentives and frameworks that positively impact entire sectors or value chains.
2. **Policy engagement** Investor engagement efforts can support mandatory corporate disclosures as well as improved corporate lobbying behaviors in order to manage systemic social and environmental risk.
3. **Asset manager engagement** Asset owners can engage with the asset managers that select their holdings and exercise voting responsibilities on their behalf to ensure they properly understand how to make systemic value-creating choices rather than value-extracting choices.

By helping the development and dissemination of system-level engagement strategies for investors, Wespath is making a system-level contribution to the investment community it is a part of.

b. Additionality

Wespath's Positive Social Purpose (PSP) Lending Program aims to achieve market-competitive returns by being a source of long-term capital in historically underserved lending markets.[98] By taking a collaborative approach with local Community Development Financial Institutions, the PSP program supports intermediaries in making larger loans with less risk. Project examples include: multifamily housing, homeless shelters, senior and special-needs housing, health care and day care centers supporting low-income communities, charter schools, and international microfinance loans.

Wespath external manager selection process



Created by Wespath

Conventional investors may pass on the investments found in the PSP program due to their typically lower financial returns. The PSP program sets Wespath's investment approach apart, demonstrating an interest in more than financial return, but in social return as well. This is in line with Wespath's Sustainable Economy Framework which states that healthy financial systems cannot be had without long-term prosperity for all and social cohesion, two cornerstones of the PSP program.

c. Polity

Wespath uses public policy statements to engage policymakers and advocate for its beliefs. Wespath has published 38 unique public policy statements written between 2009 and 2022.[99] Included in these statements are independently authored letters to US agencies such as the Environmental Protection Agency and Securities and Exchange Commission as well as endorsed letters written by major investment groups such as the PRI, the Interfaith Center on Corporate Responsibility (ICCR), Council of Institutional Investors, and others. Topics covered by the public statements range from environmental protection and human rights to corporate governance and standard setting. For example:

Date	Engagement	Significance
June 14, 2022	Comment letter to the Securities and Exchange Commission on “Enhancement and Standardization of Climate-Related Disclosures for Investors”	The letter outlines Wespath’s support for the SEC’s proposed integration of the Task Force on Climate-related Financial Disclosures and the inclusion of greenhouse gas emissions reporting into the SEC’s proposal for investor disclosures.[100] The system-level significance of this polity action is that by showing support for climate-related disclosures, Wespath is encouraging the formation of investment industry guardrails that keep system health, in this case the climate system, at the forefront.
November 15, 2018	Comment letter to Securities and Exchange Commission Addressing Proxy Adviser Regulation and Opposing Potential Changes to Rule 14a-2(b)	In the letter, Wespath describes how active ownership, including proxy voting, is a crucial element of its investing strategy. It raises concerns that the SEC’s rule amendments will make it harder for proxy advisors to do their job, thus increasing the barrier for entry for new proxy advising firms which works against the industry’s pursuit of transparency. The system-level significant of this polity action is in Wespath’s advocating for transparency in the investment community, via the importance of proxy advising firms.[101] Wespath argues that the amendment will put its ability to generate long-term value creation at risk, citing a loss in ESG considerations that drive systemic health of environmental and social systems.

Conclusion

Although sustainable investing techniques have been around for some time, system-level strategies are new. While their newness can make it difficult to properly evaluate and analyze their implementation and effectiveness, we can clearly see the ways in which early adopters are integrating these new strategies.

System-level investors start with adapting conventional investment techniques to support their system-level focus. This comes up first and foremost in their SIBs and investment policy documents, where a system-level approach is clearly communicated. From there, system-level investors adapt advanced techniques, notably collaborating with likeminded firms to generate needed leverage for cross-industry engagement and amplify their influence.

The type of advanced techniques that firms choose to utilize will differ depending on their size, capabilities, and thematic focus (forest, climate change, social equity, etc.). A critical throughline is the internal presence of system-level champions. These individuals play crucial roles in making their teams and boards aware of system-level investing and its merits.

Implications for future investment practice and process

Using these five investors as examples, a roadmap begins to form, charting a path for investors to incorporate system-level techniques. It is a significant commitment that requires attention, however the five firms studied in this report provide a starting point and a model to follow.

What our case studies and analysis show is a replicable order of operations and necessary set of ingredients that support system-level investing. To start with, we can confidently say that identifying an internal champion is essential in any meaningful approach to system-level investing. All five firms had tremendously dedicated individuals with the ability to ensure decision-makers above, below, and adjacent to them were aware of the importance of a system-level approach. From there, we know that firms rely on a set of investment beliefs and policy documents that further weave a system-level approach into the fabric of the firm's culture and investment making process. This is the entry point into the remaining conventional and advanced techniques that firms will adopt with varying degrees of resources directed at each.

TIIP's new SAIL platform provides an in-depth roadmap for how investors can approach their journey to becoming or strengthening their system-level beliefs and techniques. SAIL provides guidance to firms at every step of the process to minimize the uncertainty of joining a new field of investing and maximize the impact an investment firm can have as they integrate system-level techniques.

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Acknowledgements

We want to thank the five firms profiled for this report – California Teachers Retirement System (CalSTRS), Domini Impact Investments, Saint Paul and Minnesota Foundation, and Wespath Benefits and Investments – for their time and transparency. A special thank you goes to the following individuals for taking extra time out of their schedules to ensure this report was as accurate and robust as possible: Steve Lydenberg, Kirsti Jenkinson, and Shannon O'Leary.

About The Investment Integration Project (TIIP)

The Investment Integration Project's (TIIP) mission is to help investors understand how healthy social, environmental, and financial systems can benefit their portfolios. TIIP provides consulting services, applied research, and a subscription-based SaaS platform that supports investors' pursuit of system-level investing, an advanced approach to sustainable and impact investing that focuses on managing systemic risks and investing in solutions to systemic problems. Learn more at https://www.tiiproject.com

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