

RESPONSIBLE INVESTING REPORT

2016



UNIVERSITY OF TORONTO
ASSET MANAGEMENT CORPORATION



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MESSAGE FROM UNIVERSITY OF TORONTO'S PRESIDENT

In March 2016, I released the report “Beyond Divestment: Taking Decisive Action on Climate Change”. This report built on the recommendations of an advisory committee that had been struck in response to a petition calling on the University of Toronto to divest from fossil fuel-producing companies. The goal, common to each of these initiatives, is to help meet the challenges posed by climate change.

As both my report and the advisory committee’s recommendations make clear, the University’s most valuable and effective contributions to the global effort to avert or mitigate the consequences of climate change will flow from our fundamental role as an institution of research and education. U of T is continuing to make important contributions in climate science research and education, and we have implemented or are facilitating many of the advisory committee’s recommendations in this regard.

At the same time, a comprehensive approach to the challenges posed by climate change will also include a systematic assessment of environmental, social, and governance (ESG) factors as they relate to the University’s investments. Considering ESG-based factors – including those linked to climate-related risk – as they pertain to all sectors of our economy offers the best chance of success in addressing climate change from the perspective of our investments, while simultaneously allowing us to fulfill our



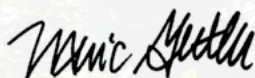
fiduciary duties to the University's Pension and Endowment Fund beneficiaries.

Accordingly, in "Beyond Divestment" I called on our Pension Committee to incorporate ESG factors into its Statement of Investment Policies and Procedures (SIPP) – a change that was implemented by the Committee in June 2016. I also called on UTAM management to expand significantly their application of ESG analysis. I directed them to enhance transparency and build a rigorous and systematic approach to integrating ESG factors into their investment decisions. I set several specific goals and suggested particular initiatives for UTAM to consider. I also requested that UTAM report annually on their progress. It was an ambitious agenda.

I am delighted that UTAM, with leadership and initiative from Daren Smith and his entire team, has responded enthusiastically. As this report clearly demonstrates, UTAM has

embraced the importance of applying ESG analysis alongside other investment tools and practices in an effort to make better-informed and ultimately more responsible investment decisions. UTAM has made remarkable progress in the past year. Of course, as they would be the first to point out, more remains to be done, especially in the context of a complex and constantly evolving investment landscape. But, as you will see in this report, we have made a major new commitment to responsible investing and we are further ahead in this endeavour than at any point in our institution's history.

Let me congratulate Daren and his team on an impressive report and an excellent start.




Merik Gertler
President, University of Toronto



MESSAGE FROM UTAM'S PRESIDENT AND CHIEF INVESTMENT OFFICER

I am proud to present our inaugural responsible investing report. As the asset manager for the University of Toronto's Pension Fund, Endowment, and short-term working capital fund (EFIP), UTAM is committed to being a responsible investor on behalf of the University while fulfilling our investment mandate and fiduciary duty.

As part of being a responsible investor, we believe that material Environmental, Social and Governance (ESG) factors should be considered as part of the investment decision-making process along with other material factors. I am pleased to report that we made great strides in 2016 in enhancing our investment approach, so that it now more fully incorporates ESG factors into our investment decision-making process. As just a few examples, I would highlight that we became a signatory to the United Nations-supported Principles for Responsible Investment (PRI), implemented a system that allows us to

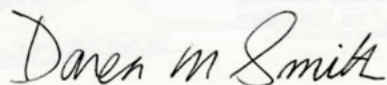


identify and evaluate ESG risks for equity securities held by our equity managers, and enhanced our manager selection and monitoring process so that it now more fully takes into account ESG considerations. We believe that implementing these changes is not only consistent with our fiduciary duty but that it also allows us to make better-informed decisions and ultimately makes us better investors.

UTAM employs a “manager of managers” approach to investing, meaning that we do not buy and sell individual bonds and stocks ourselves, but instead seek out best in class managers to do that on our behalf. This is a different approach than that used by many large pension plans and other institutions. I point this out because best practice for ESG integration depends on whether assets are managed in-house or by external managers. Our goal is to implement a best in class approach to ESG integration for a manager of managers.

Our commitment to integrating ESG factors into our investment decision-making process, and continuing to improve how we do this, is a top priority for UTAM’s senior management. To that end, during the first quarter of 2017, we established an internal responsible investing committee composed of the President & Chief Investment Officer, Chief Operating Officer, Chief Risk Officer, and the Senior Portfolio Manager, Investments to oversee the implementation of ESG integration and to provide strategic direction for UTAM’s responsible investing efforts.

UTAM has been fortunate to benefit from the wisdom and insights of many of Canada’s large pension plans. We are constantly seeking out thought leaders so we can stay on top of evolving trends and developments. While we believe we have achieved a great deal in a short period, we are committed to enhancing our processes as new information, metrics, data, and best practices emerge. We recognize that this will be a long-term journey and look forward to sharing our progress with you in future Responsible Investing reports.



Daren M. Smith, CFA
President & Chief Investment Officer

UTAM'S RESPONSIBLE INVESTING PRINCIPLES

Consistent with the United Nations-supported Principles for Responsible Investment (PRI), UTAM defines Responsible Investing as an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions to better manage risk and generate sustainable, long-term returns.

We believe that considering material ESG factors as part of our investment decision-making process, with respect to both direct and indirect investments, along with other material investment factors is consistent with our fiduciary duty.

Environmental, Social and Governance factors are defined as follows:



Factors that relate to a company's interaction with the physical environment (e.g. climate change, greenhouse gas emissions, air and water pollution, water scarcity, deforestation)



Factors that relate to a company's practices that have a social impact on a community or society (e.g. working conditions including slavery and child labour, labour relations, health and safety, human rights, impact on indigenous communities)



Factors that relate to how a company is governed (e.g. executive compensation, board independence and composition, shareholder rights, transparency)

In December 2016, UTAM became a signatory in support of the PRI, which are a set of six aspirational principles designed to encourage and assist investors in integrating ESG into their investment processes. In becoming a signatory, we have committed to the following statement from the PRI and its six Principles for Responsible Investment, which we have adopted as our own.

"As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time).

We also recognize that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the six PRI principles."

The PRI will guide UTAM's approach to responsible investing. On the following pages, we have listed the six Principles for Responsible Investment and some of the actions we are taking, and intend to take, in support of these principles. We expect our actions to evolve over time as best practices emerge and as we enhance our processes.

Signatory of:



PRI PRINCIPLE

UTAM ACTIONS

PRINCIPLE 1

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

1. Evaluate ESG related risks across all portfolios.
2. Integrate consideration of ESG factors into our investment and operational due diligence policies, and into other policies where relevant and material.
3. Integrate ESG considerations into our manager selection process, where relevant and material.
4. Support development of ESG-related tools, metrics, and analyses.
5. Encourage academic and other research on this theme.
6. Provide ESG training for investment professionals.

PRINCIPLE 2

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

1. Adopt a proxy voting policy that is ESG focussed and apply this, where possible, to all direct public equity investment mandates (i.e. where public equity securities are held in the name of Pension or Endowment), and to public equity pooled funds in which Pension and Endowment are the only investors (i.e. where pooled funds are held in the name of Pension or Endowment and these pooled funds, in turn, hold public equity securities).
2. Encourage managers to adopt ESG focussed voting policies, where relevant.
3. Support corporate and regulatory proposals which contribute to improved governance practices and more effective boards.
4. Participate in collaborative engagement initiatives.

PRINCIPLE 3

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

1. Discuss ESG risks in manager portfolios and in relation to particular securities held.
2. Ask managers to undertake and report on ESG-related engagements with companies.
3. Support collaborative initiatives promoting ESG disclosure by companies.

PRI PRINCIPLE

UTAM ACTIONS

PRINCIPLE 4

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

1. Encourage managers to become signatories to the PRI.
2. Communicate ESG expectations to managers.
3. Support the development of tools for benchmarking ESG integration.
4. Support regulatory or policy developments that enable implementation of the Principles.

PRINCIPLE 5

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

1. Support and participate in networks and information platforms to share tools and pool resources.
2. Collectively, with other asset owners and managers, address relevant emerging issues.
3. Identify and support appropriate coalitions whose beliefs are aligned with the Principles.

PRINCIPLE 6

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

1. Disclose how ESG issues are integrated within our investment practices.
2. Disclose active ownership activities (e.g. voting, engagement, and policy dialogue).
3. Communicate with stakeholders on ESG issues and the Principles.
4. Report on progress and achievements relating to the Principles.
5. Make use of reporting to raise awareness among a broader group of stakeholders.

Where the words “relevant” and “material” are used they are intended to reflect the view that ESG factors are not equally important across all managers and strategies. For example, the expected holding period of an investment (e.g. time horizon) often has an impact on the relevance and materiality of ESG factors, with a shorter holding period generally implying less importance.

OUR APPROACH

TO INTEGRATING ESG FACTORS INTO THE MANAGER SELECTION AND MONITORING PROCESS

INTEGRATING ESG FACTORS INTO OUR MANAGER SELECTION AND MONITORING PROCESS IS A RESPONSIBILITY SHARED BY ALL OF OUR INVESTMENT STAFF. WHILE WE HAVE PREVIOUSLY CONSIDERED ESG FACTORS WHEN EVALUATING MANAGERS, WE ARE NOW MUCH MORE RIGOROUS AND SYSTEMATIC IN OUR APPROACH. THE ACTIONS LISTED BELOW DESCRIBE ELEMENTS OF OUR CURRENT PROCESS THAT WILL BE UNDERTAKEN FOR ALL MANAGERS, WHERE POSSIBLE AND RELEVANT.

SELECTION OF MANAGERS

1. Issue ESG due diligence questions, review responses and follow-up where appropriate.
2. Review manager's responsible investing policies.
3. Meet with responsible investment focussed staff and assess their skills and competence.
4. Discuss the manager's governance and management of responsible investing activities.
5. Discuss the manager's involvement in collaborative initiatives and direct engagements with company management.
6. Review the manager's voting policy and processes (where UTAM would not direct the voting).
7. Ask whether the manager is a signatory to the PRI and/or other relevant organizations.
8. Review responsible investing reporting to clients and/or the public.
9. Communicate the type of ESG reporting we expect.
10. Evaluate the quality and coverage of ESG research used.
11. Assess the manager's ESG incorporation strategies and ability to identify and manage ESG issues.
12. Review ESG characteristics of the portfolio.
13. Discuss how ESG issues have impacted specific investment decisions and, where relevant, stock and portfolio performance.
14. Discuss securities that appear to have material ESG risks.
15. Include a section on ESG in our internal manager investment recommendation memos.

A large, leafy tree with vibrant green foliage stands in the foreground, partially obscuring a multi-story stone building with a blue-tiled roof. The building features numerous windows, some with white frames. The scene is set outdoors on a sunny day, with shadows cast on the ground.

MONITORING OF MANAGERS

1. Issue ESG due diligence questions annually, review responses and follow-up where appropriate.
2. Include responsible investment as a standard agenda item at annual performance review meetings.
3. Highlight examples of good responsible investment practices by other managers.
4. Encourage consideration of joining responsible investing initiatives/organizations or participation in collaborative projects with other investors.
5. Review the manager's responsible investing reporting.
6. Meet with responsible investment focussed staff and discuss any changes since the last meeting and current areas of research.
7. Review ESG characteristics of the portfolio.
8. Request information on ESG incorporation in specific investment decisions.
9. Discuss securities that appear to have material ESG risks.
10. Include a section on ESG in our internal manager review reports.

PROACTIVE AND DELIBERATE VOTING

In the past, for all public equity securities held directly by the Pension Fund and the Endowment, UTAM delegated proxy voting to its external managers according to each manager's own proxy voting policy. Although we reviewed these policies and each manager's voting record annually, this was a more passive approach. We have determined that the best way we can vote proactively and deliberately is by taking back voting responsibility from our managers and by engaging a third-party proxy voting service provider to vote according to our beliefs. This allows us to better respond to shareholder proposals related to ESG, including those aimed at reducing climate-related risks. Accordingly, in September 2016 we engaged Institutional Shareholder Services (ISS) for proxy voting services and adopted their Sustainability policy and guidelines, where possible, to all direct public equity investment mandates (i.e. where public equity securities are held in the name of Pension or Endowment), and to public equity pooled funds in which Pension and Endowment are the only investors (i.e. where pooled funds are held in the name of Pension or Endowment and these pooled funds, in turn, hold public equity securities).



ISS DESCRIBES THEIR SUSTAINABILITY VOTING GUIDELINES AS FOLLOWS:

"The ISS Sustainability voting guidelines represent an approach to corporate governance and proxy voting that aligns with the perspectives of mainstream investors that wish to incorporate ESG considerations in their investment decision-making processes to a greater extent. The Sustainability guidelines focus on long-term economic value preservation/enhancement through promotion of corporate governance best practices that mitigate risks to shareowners, but also reflect the recognition that ESG factors could present material risks to portfolio investments.

The Sustainability guidelines were specifically formulated to meet the growing need by mainstream institutional investors to account for ESG elements in their voting practices, including signatories to PRI looking to fulfill their obligations to the PRI from a proxy voting perspective. ISS liaised with the UN PRI Secretariat to help inform the development of the Sustainability guidelines."

ADVOCACY AND COLLABORATION

UTAM believes that there is strength in numbers and that by joining together with other like-minded investors we can achieve together what might not be possible individually. The list on the following page shows the external organizations supporting advocacy and collaboration to which we currently belong. We intend to sign the Montréal Carbon Pledge in 2017 and will continue to seek out other organizations that would be beneficial to join or align with.



UTAM has also worked with the University's Responsible Investing Committee (RIC) since its inception in 2009. This committee discusses and expresses opinions on principles related to responsible investing and has been a helpful sounding board to the University and UTAM.



**INSTITUTIONAL
LIMITED PARTNERS
ASSOCIATION**

The ILPA is a member-driven organization dedicated exclusively to advancing the interests of private equity investors through education programs, independent research, best practices, networking opportunities and global collaborations. UTAM has endorsed ILPA's Private Equity Principles that state that private equity managers should provide investors with portfolio company and fund information on material risks including "Extra-financial risks, including environmental, social and corporate governance risks".

<https://ilpa.org/>

MEMBER SINCE 2002



Formerly known as the Carbon Disclosure Project, CDP is a non-profit organization that runs the global disclosure system that enables companies, cities, states and regions to measure and manage their environmental impacts. CDP has built the most comprehensive collection of self-reported environmental data in the world. Over 5,600 companies responded to CDP's climate change, water, forests and supply chain questionnaire in 2016.

<https://www.cdp.net/en>

SIGNATORY SINCE 2016



**Pension Investment
Association of Canada**
Association canadienne des
gestionnaires de caisses de retraite

The Pension Investment Association of Canada has been the national voice for Canadian private and public pension funds since 1977 in matters related to pension investment and governance. PIAC evaluates and promotes sound pension and corporate governance standards and practices.

<http://piacweb.org/>

MEMBER SINCE 2004



Responsible Investment Association

The Responsible Investment Association is Canada's membership association for Responsible Investment (RI). Members believe that the integration of environmental, social and governance (ESG) factors into the selection and management of investments can provide superior risk adjusted returns and positive societal impact.

<https://riacanada.ca/>

MEMBER SINCE 2016

**Canadian Coalition for
GOOD GOVERNANCE**

THE VOICE OF THE SHAREHOLDER

The CCGG is the pre-eminent corporate governance organization in Canada and is uniquely positioned to effect change as the voice of Canadian institutional shareholders. Representing the interests of institutional investors, CCGG promotes good governance practices in Canadian public companies and the improvement of the regulatory environment to best align the interests of boards and management with those of their shareholders, and to promote the efficiency and effectiveness of the Canadian capital markets.

<http://www.ccg.ca/>

MEMBER SINCE 2008



The UN-supported Principles for Responsible Investment (PRI) works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

<https://www.unpri.org/>

SIGNATORY SINCE 2016







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