



# Memorandum

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**TO:** Board of Governors

**FROM:** Committee to Advise on Matters of Social Responsibility (CAMSR)

**SUBJECT:** Approval of CAMSR Report Implementation Plan

**DATE:** April 23, 2020

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At its meeting of April 15, 2020, CAMSR approved the submission of the CAMSR Report (GD19-50) to the Board of Governors.

CAMSR recommends that the Board of Governors approve the implementation plan contained in the CAMSR Report.

The CAMSR Report is attached as Appendix A.

Motion for approval:

*Be it resolved that the Board of Governors, on the recommendation of the Committee to Advise on Matters of Social Responsibility (CAMSR), approve the implementation plan contained in the CAMSR Report (GD19-50) supporting the operationalization of the CAMSR recommendations, approved by the Board of Governors on December 5, 2019.*





**McGill**

**COMMITTEE TO ADVISE ON  
MATTERS OF SOCIAL  
RESPONSIBILITY (CAMSR)**

**REPORT TO THE BOARD OF  
GOVERNORS**

GD19-50 APPENDIX A  
APRIL 23, 2020

## Context, Process and Acknowledgement

At its meeting of December 5, 2019, the Board of Governors (“Board”) approved the recommendations contained in the CAMSR Report (GD19-29), with the understanding that an implementation plan, including quantifiable targets and timelines would be developed by CAMSR, in consultation with the Investment Committee, and presented to the Board at its meeting of April 23, 2020. CAMSR’s Report is available [here](#).

Since the Board’s decision, CAMSR held three meetings (January 16, March 24, and April 15, 2020) and the Investment Committee held two meetings (February 7 and March 18, 2020). In addition, the Committees held a joint working session on February 18, 2020. The Investment Committee’s recommendations with respect to the operationalization of CAMSR’s recommendations one through six were approved by CAMSR, along with the remaining last two recommendations (seven and eight) on March 24, 2020.

The result of this work is an implementation plan that takes into account the mission of the University and the fiduciary duties of the Board; the plan presents actions, which serve to fulfill, in a meaningful and ambitious manner, the Board’s decision of December 2019. The plan fully supports McGill’s priorities in socially responsible investing and sustainability, and promotes the sound governance and trusteeship of the University’s endowment.

CAMSR expresses its gratitude to the Investment Committee and to all the members of the University community and the community at-large, who participated in CAMSR’s activities and whose advice and expertise was valuable in helping CAMSR bring forward to the Board responsible and implementable actions that are needed to support collective efforts in the fight against climate change.

## Implementation Plan Related to the CAMSR Report Recommendations (GD19-29)

The implementation plan presents the eight recommendations approved by the Board in December 2019 and, for each recommendation, proposes an implementation approach for the Board's consideration.

### Recommendation #1, with respect to Decarbonization:

At its December 2019 meeting, the Board of Governors committed to:

“Reduce the overall carbon emissions of the endowment portfolio, by a percentage to be set against a determined reference index or benchmark.

This percentage should be commensurate with McGill's ambitions to be a leader in sustainability, while having due regard to the portfolio's risk and return objectives and the Statement of Investment Policy's goal to provide a dependable and optimal source of income for endowment beneficiaries and to cover the annual operating costs of the MIP.

This commitment will involve a reduction of exposure to the highest carbon intensive companies in the portfolio, including some within the fossil fuel industry. CAMSR notes that a carbon footprint target needs to be supported by an analysis that will help to establish metrics and a timeline according to which progress will be measured. CAMSR, in collaboration with the Investment Committee, is committed to working on this analysis and developing a plan (including the proposed target, metrics, and timeline) for the overall commitment in regard to the carbon emission of the portfolio, which will be presented to the Board by its meeting of April 2020.”

In response to this commitment, CAMSR recommends the following reduction target and timeline:

CAMSR recommends a reduction of the carbon emissions of the McGill Investment Pool (“MIP”) public equity portfolio in order to achieve and sustain, by 2025, a 33% carbon emissions reduction of the MIP public equities relative to the MIP public equities benchmark, with the understanding that the majority of the reduction is to be achieved within the first two years.

*Note:* Considering the portfolio as at September 2019, this approach results in a reduction of the MIP carbon emissions by 38 tons of CO<sub>2</sub> per million dollars invested. It will lead to divesting from highly carbon intensive companies, including those within the fossil fuel industry. In comparison, the elimination of the Carbon Underground 200 from the equity holdings as at September 2019 would have reduced the carbon footprint by 18 tons of CO<sub>2</sub> per million dollars invested, which is far less than what the proposed plan recommends.

Please see Appendix 1 for a description of the analysis that the Investment Committee and CAMSR considered in order to establish this target and timeline.

**Recommendation #2, with respect to Impact Investing:**

At its December 2019 meeting, the Board of Governors committed to:

“Invest in low-carbon funds and funds that contribute to decarbonization (impact investments) of the MIP and set global allocation objectives, which may include the following asset classes:

- Fixed income (ex: green bonds)
- Private investments (ex: new clean technologies in auto parts, solar equipment, light fixtures)
- Real assets [renewable energy infrastructure (ex: wind, solar, hydro, waste, bioenergy)]”

In response to this commitment, CAMSR recommends the following target and timeline:

CAMSR recommends, by 2025, to commit 5% of the MIP to low-carbon funds and funds that contribute to decarbonization of the MIP.

*Note:* Based on the MIP’s current assets, this target represents a \$77 million commitment, which will grow as the MIP’s assets are expected to increase over time. Please see Appendix 2 for a description of the analysis that the Investment Committee and CAMSR considered in order to establish this target and timeline.

**Recommendation #3, with respect to Screening**

At its December 2019 meeting, the Board of Governors committed to:

“Increase the amounts invested in the fossil-fuel-free fund (established in 2017 with a \$5 million commitment) and promote it among the donor community.”

In response to this commitment, CAMSR recommends the following actions:

As part of McGill’s Bicentennial Campaign, the University will actively promote the Endowment’s fossil-free fund and seek the interest of the donor community to increase allocations to it. Based on the response from the donor community, the University will propose to the Investment Committee, within two years, a target allocation and an appropriate mechanism for implementation. Donor allocations of MIP funds will be used to meet this target allocation.

#### **Recommendation #4, with respect to Engagement**

At its December 2019 meeting, the Board of Governors committed to:

“Exercise, to the extent possible, active stewardship through investor engagement opportunities with investment managers.”

In response to this commitment, CAMSR recommends the following actions:

The Investment Committee will continue to increase the number of managers who adhere to ESG Policy and/or are signatories of the UNPRI (at 93% as at January 2020). The Investment Committee will ensure that the University follows-up with these managers on an annual basis to assure itself that they still adhere to an ESG Policy and/or that they are still signatories of the UNPRI.

The University will encourage managers to monitor the carbon footprint of their portfolio using MSCI ESG research or a similar measurement tool. The University will also use the ESG Impact Monitor system of MSCI to identify, assess and question the involvement of MIP companies in practices which go against ESG and/or UNPRI norms.

The Office of Investments will increase its knowledge base on socially responsible investment practices through training, attendance at conferences or other similar activities.

Progress in the actions noted above will be reported to the Investment Committee on an annual basis and will form part of the Investment Committee’s annual report to CAMSR and the Board of Governors.

#### **Recommendation #5, with respect to ESG Integration**

At its December 2019 meeting, the Board of Governors committed to:

“Review the Statement of Investment Policy of the MIP to reflect ESG goals and objectives, including modifying the Investment Objective section to consider ESG commitments.”

In response to this commitment, CAMSR is recommending the following actions:

Following the Board’s consideration of the CAMSR Report in April 2020, the Office of Investments will propose amendments to the *Statement of Investment Policy* (SIP) to the Investment Committee at its meeting in June 2020. The amendments will aim to implement the proposed CAMSR recommendations, which are presented to the Board of Governors for consideration.

### **Recommendation #6, with respect to Annual Reporting**

At its December 2019 meeting, the Board of Governors committed to:

“Present to the Board and publish, annually, a report on SRI, including:

- % of assets managed by managers with an ESG policy and/or as signatories of the UNPRI
- MIP carbon emission absolute and relative measures
- Impact investment exposures
- Such other initiatives as may be relevant to SRI activities”

In response to this commitment, CAMSR is recommending the following actions:

The Investment Committee will present to CAMSR and to the Board of Governors, and publish annually, a report on SRI beginning in Spring 2021, following the MIP’s year-end (December 31, 2020).

### **Recommendation #7, with respect to SRI Review**

At its December 2019 meeting, the Board of Governors committed to:

“The Board commit to reviewing the current SRI practices on a five-year basis in order to determine the need for any adjustments or further SRI actions, as may be advisable, in relation to the University’s endowment fund.”

In response to this commitment:

The review has been added to the Board’s calendar of business and is planned to take place in the spring of 2025.

### **Recommendation #8, with respect to Institutional Leadership**

At its December 2019 meeting, the Board of Governors committed to:

“The University, in line with its mission, take a leadership role to evaluate and promote, in collaboration with peer (U15) universities, policies and best practices in the area of SRI.”

In response to this commitment, CAMSR is recommending the following actions:

The University is proactively taking a leadership role in order to inform peer institutions of its evaluation of actions to promote policies and best practices in the area of SRI. In the recent past, representatives of the University have met with representatives of other universities in order to engage in discussion on best practices in the area of SRI that are applicable to universities. The University will continue these discussions and seek further opportunities to collaborate with peer universities and will report its activities to CAMSR.



## APPENDIX 1

### Analysis supporting Recommendation #1, with respect to Decarbonization:

The analysis undertaken in respect of the decarbonization target and timeline supports the University's objective to establish meaningful and concrete actions needed to achieve the sound implementation of the recommendations approved by the Board in December 2019. With that objective in mind, the University's development of the proposed target and timeline was informed by the following considerations:

- a) the University's ability to effectively implement portfolio changes required to meet different target scenarios with the current asset mix and managers;
- b) the possibility that a manager's preferences (with an important underweight in carbon intense sectors) might change going forward;
- c) the cost of implementation (transitional and ongoing); and
- d) the long-term impact of different constraints.

The possibility that the carbon footprint of the overall equity market might reduce naturally in the future as well as the possible upward fluctuations associated with an increase of the weights of the 3 sectors (i.e. Energy, Materials and Utilities) that contribute the most to the MIP's total carbon emissions have been considered. As a result of the uncertainty related to the overall market future carbon emissions, a target measured relative to an Equity market benchmark, rather than an absolute target, is proposed.

MSCI was used to provide objective data on CO<sub>2</sub> emissions. Data, which are available for most public equity issuers, include data related to: the direct emissions from owned or controlled sources (Scope 1), the indirect emissions associated with the generation of purchased energy (Scope 2) carbon emissions, but not the data that would be related to the indirect emissions from the generation of purchased energy (Scope 3). Currently, there is no objective measure for Scope 3 emissions as company reports include partial Scope 3 emissions only.

#### Additional Considerations:

##### **Achieve and sustain a 33% carbon emissions reduction of the MIP public equities relative to the MIP public equities benchmark**

Carbon emissions of the MIP benchmark as at September 2019 were 163 tons CO<sub>2</sub> per million dollars invested. Carbon emissions (as at September 2019) of the MIP were 148 tons CO<sub>2</sub> per million dollars invested. A target of being at least 33% below the benchmark and a reduction from 148 to 110 will cause an estimated expected Tracking Error (i.e. variance to benchmark) of no more than 0.4% measured over a 5-year period.

##### **Limits on the attainable level of carbon emission reduction levels**

Selling all MIP investments in the 3 sectors with the highest carbon emissions (i.e. Energy, Materials and Utilities), would require a complete overhaul of most of the investment manager mandates. As most managers do not offer substitute investment vehicles, the hard and soft costs would be significant, and the resulting portfolio would dramatically breach materiality thresholds. Furthermore, even if the MIP's investments

in all 3 sectors were to be sold, the MIP would still retain a Carbon Footprint, as calculated in September 2019, of 31 tons per million invested.

### **Elimination of the Carbon Underground 200 Equity Holdings**

The elimination of the Carbon Underground 200 equity holdings would reduce the Carbon Footprint from 148 to 130 – far less than would be achieved by the recommended changes. The operational impact would be almost as significant as the complete elimination of the 3 most carbon intense sectors. An investment of just one of the Carbon Underground 200 securities in a manager's fund would be problematic as all assets of the MIP would need to be redeemed from most of the current pooled fund investments, even when the portfolio carbon footprint is minimal. There would be a loss in flexibility to select the changes that achieve the largest carbon footprint reduction with the least cost and impact on returns and risk.

### **Reducing Allocation to Carbon Intensive Geographic Markets (Canada and Emerging Markets (EM))**

The Canadian market index carbon emissions (tCO<sub>2</sub>/\$million invested) is 143; EM is 334 vs. the overall MIP benchmark emissions of 163. A reduced allocation from Canada and/or EM could conceivably reduce carbon footprint. However, McGill's managers in Canada and EM have Carbon Emissions well below the benchmarks so a reallocation away from the managers would actually have an adverse impact on the carbon footprint and require significant changes to portfolio construction. Hence, it is an inefficient solution to reduce the carbon footprint.

### **More Aggressive Reduction Targets Beyond the Recommended 33% Relative to Benchmark**

At this time, the 33% reduction target relative to benchmark touches the 0.4% tracking error Materiality Threshold. Higher targets would surpass it and put at risk the capacity of the Investment Committee to adapt to a reasonable range of changes to market conditions (both the practical ability to implement changes and the impact on tracking error). Higher targets will also impose additional costs, require terminations of manager mandates and potentially impair McGill's ability to participate in important markets such as EM – which currently account for 20 % of MIP public equity allocation and could potentially continue to grow. There are very few EM managers who commit to low carbon emissions. This may change in the future but today it is a constraining factor.

The Investment Committee is confident (at an 84% confidence level) that the changes considered will not produce a negative variance from our benchmarks of more than 0.4% per annum over a five-year period. The variance could be greater over a shorter timeframe such as one quarter or one year but as an endowment fund with a long-term time horizon, the Investment Committee is less concerned about short-term fluctuations.

## APPENDIX 2

### *Analysis supporting Recommendation #2, with respect to Impact Investing:*

Current allocation into renewable and clean technology private debt, low carbon real estate and listed impact equities is estimated at 2% of the total MIP assets.

Based on the MIP's current assets, the target represents an \$77 million commitment, which will grow as the MIP's assets increase over time. Impact investments that will be included in this commitment will aim to generate specific beneficial environmental effects in addition to financial gains. They will take the form of numerous asset classes and will address environmental issues. Funds that incorporate sustainability principles into their value creation strategies will be considered, including real estate funds, infrastructure funds and listed impact equity funds that are highly exposed to decarbonization. Equity and Fixed Income securities could also be included if the company or the debt of the company contributes to potential climate change solutions. Lastly, this approach would include, among others, companies in alternative energy, energy efficiency, green building, pollution prevention, and sustainable water.

Taking into account the relatively limited resources in the Office of Investments, the preference will be to invest in strategies belonging to asset classes with similar risk-return characteristics as the ones already contemplated by the internal team.

Given the emergence of impact investments in many asset classes and the absence of a proper long-term track record, it is difficult to assess the historical performance of these specific investments. Information was gathered on future expected return and volatility measurements from assumptions given by investment manager experts in each field. It is expected that a 5% commitment to selected strategies would have minimal impact on MIP returns (8 to 10 basis points) and almost no impact on risk characteristics if not a little on liquidity.

With a portion of the impact investment strategies dedicated to private funds, it is estimated that sourcing, due diligence, investment selection and capital deployment could likely take 5 years to fully reach the target.