CHAPTER 9
INVESTMENT MANDATES, PORTFOLIO ANALYTICS AND CLIENT REPORTING

This chapter attempts to draw the threads of the earlier ones together in the ways that these topics are given effect in practice:

- through the mandates and expectations set by clients; and
- how fund managers communicate their environmental, social and governance (ESG) work to their clients.

It notes how the challenges of the agency problem can occur within the investment chain as well as between investors and corporate management, and how the core corporate governance precepts of accountability and alignment can also be used to derive appropriate answers to these challenges in the investment sphere. Designing mandates to deliver investment processes focused on the long-term horizons typically sought by asset owners is key, though delivering this in practice is complex.

The chapter also discusses requests for proposals (RFPs), which are evaluation documents for consultants and asset allocators to conduct initial due diligence on prospective asset managers, and an important mechanism for identifying potential providers of fund management services. If done well, the RFP process enables asset managers to provide useful information to consultants and asset allocators, by which they can be compared and evaluated. More broadly, the chapter considers the assessments that clients and their advisors use to identify appropriate fund managers and gain assurance that they are continuing to deliver the investment processes that have been agreed.

Finally, this chapter covers the screening and portfolio analytics tools that are emerging to assist asset owners and their advisers to assess ESG, or to provide them with an appropriate basis for raising questions about fund manager approaches to ESG.

CHAPTER 9
INVESTMENT MANDATES, PORTFOLIO ANALYTICS AND CLIENT REPORTING

1 ACCOUNTABILITY TO CLIENTS AND ALIGNMENT WITH THEM

The veteran founder of Vanguard, John Bogle, called our society a 'double-agency' one – namely, a society in which corporate agents (as a practical matter, corporate CEOs) "who are duty-bound to represent their shareholders face money manager/agents who are themselves duty-bound to represent their mutual fund shareholders and their other clients, often pension funds."[1]

According to Bogle, there is a similarity between the agency problem that corporate governance is designed to address and the agency problems that occur within the investment chain. As with corporate governance, these investment chain agency problems can be addressed (though not completely solved) by careful alignment and accountability:

- **Alignment** should be designed so that the timeframes and structures of portfolio manager assessment and remuneration closely reflect both the performance experienced by the clients they serve and the timeframes over which they need performance to be delivered.
- **Accountability** should mean that portfolio managers respond to the clearly expressed intentions of their clients and report as fully as required.

Client mandates can deliver these two elements if they are designed well. There are a number of steps to good design of mandates, and also to the oversight and monitoring process that assesses whether the mandates have in fact been delivered in practice. These steps can be characterised as follows:

A. Clarifying client needs: defining the ESG investment strategy

The first step in the effective design of a mandate is that the client should be clear about their needs and set them out in a clear statement of ESG investment beliefs. Doing so will require them to define their investment goals and beliefs. Institutional clients will typically be keenly aware of the goals that they are trying to achieve (their risk-adjusted return target over the appropriate time horizon), but may find it harder to define their investment beliefs. Nevertheless, it is these beliefs that will help them to define how they believe they will create value and to set their investment approach. The investment beliefs – that might be expressed in a Statement of Investment Principles – ought to guide the overall approach towards ESG (and investment more generally), and will help to frame any mandate agreed with an investment manager.

B. Fully aligning investment with client ESG beliefs

Once the client's investment beliefs are clarified, the next challenge is to ensure that they are reflected operationally within the fund manager's investment approach. This can require a clear framing of basic expectations, including such issues as appropriate ESG screening approaches.

As suggested by a Principles for Responsible Investment (PRI) report, asset owners should ensure that mandates align investment across asset classes (while the text implies an equities mandate, the intent of its ambition is to expect integration and engagement, as appropriate, across all asset classes) with their beliefs and strategies:

"Attention should be paid to aligning timeframes through fees and pay structures, ensuring that ESG issues are fully integrated into investment decision-making, and ensuring that the investment manager engages with companies and issuers, and votes shareholdings."[2]

C. Developing client-relevant ESG-aware investment mandates

Ensuring that the mandate is fully operational is typically done through a detailed request for proposals (RFP) process. Typically this takes the form of a detailed questionnaire to a long-list of potential managers. Reports suggest that there are now always at least some ESG questions included in these questionnaires, though for the least ESG-aware clients, these are likely to be few and somewhat superficial. For those asset owners that take ESG more seriously, the questions will be detailed and challenging and form a significant element of the RFP decision-making process. The questionnaire is used to sift providers to develop a shortlist of potential managers, and then there is usually a so-called 'beauty parade' series of meetings between appropriate representatives of the asset owner (sometimes the investment committee of the board, executive team members or just an investment consultant, depending on the scale of the mandate or the asset owner and their internal resources) and a number of potential fund managers (typically there are around three managers included at this stage of the process).

D. Tailoring ESG investment approach to client expectations

Different sorts of clients have very different expectations across ESG issues and the rest of their investment approach. Responding to those different expectations may require entirely different investment approaches and indeed, different fund types. It is vital to find ways to ensure that the client and fund manager are aligned in their approach and have a full understanding of their appropriate expectations. This may be done outside the legal mandate as well as within it.

E. Holding managers to account

Once the mandate is agreed, the client will then wish to assure itself that the fund manager is indeed delivering in accordance with the mandate. This is unlikely just to be narrowly in terms of delivering financial performance in line with expectations, though if performance differs notably from what might be expected in given markets, then no doubt questions should be asked just as often about striking outperformance of expectations as happens in relation to notable underperformance. However, this is not often the case. And for ESG mandates in particular, the assessment is likely to be across a broader range of issues. There are two forms that this work will take:

- monitoring meetings between the client and the fund manager; and
- the manager's measurement and reporting of its ESG performance.

Each of these areas is explored in more depth through the rest of this chapter.

2 CLARIFYING CLIENT NEEDS: DEFINING THE ESG INVESTMENT STRATEGY

9.1.1 Explain why mandate construction is of particular relevance and importance to the effective delivery of ESG investing: linking sustainable investing to the mandate; defining the sustainable investment strategy.

In order to incorporate the longer-term perspective discussed in **Section 1** and an ESG mindset into the mandates that asset owners give fund managers, asset owners need to have developed a clear understanding of their own views on ESG and investment more generally. It has become common now for asset owners to set out their investment beliefs – namely, a philosophy of what the institution believes will drive returns and deliver value over the relevant time-horizon. Most asset owners these days incorporate a perspective on ESG factors.

The Pensions and Lifetime Savings Association (PLSA) produces a **Stewardship Checklist** for its members, which encourages just such a development of a broader philosophical approach.[3]

Example

PLSA Stewardship checklist

In this checklist (useful not just to pension schemes but for all asset owners), there are three key requirements.

To ensure an effective and meaningful stewardship strategy, investors should:

✓ Be clear about how stewardship fits within their investment strategy, policy and how it helps meet their investment objectives. This should include:

- A clear and agreed understanding of the trustee board and relevant organisations' (e.g. the employer's) overall mission, purpose and objectives.
- A defined set of agreed investment beliefs – including on ESG issues – at a level which ensures everyone is comfortable but which is also sufficiently granular to meaningfully inform and guide the investment strategy and objectives.
- A robust framework for deciding and monitoring a scheme's investment policies – including on ESG issues – and the role which acting as an engaged steward of members' assets plays in this. This can either be a stand-alone policy or fully integrated into a scheme's investment policies.
- A strategy for how stewardship fits into the manager selection process and ongoing relationship monitoring.

✓ Seek to ensure that fund managers and other service providers deliver effective integration of long-term ESG factors into their investment approach. Using due diligence and the fund manager appointment process, pension schemes will gain a clear understanding of the ESG integration and stewardship approaches of prospective fund managers. Schemes should ensure that these approaches are fully consistent with the scheme's investment strategy, policy and objectives over the appropriate time horizon.

✓ Work with their advisers to consider the level of resource available for stewardship activities, which assets are covered and what the appropriate structure is. Some schemes will have the resource for an in-house stewardship team. Others will need to outsource stewardship either to their existing asset manager or to a specialist stewardship 'overlay' provider. It should be noted that delegating stewardship activities does not absolve schemes of responsibility. Instead they should take ownership of the stewardship approach and ensure they have a clear understanding of work taken on their behalf.

As the PLSA indicates, the investment philosophy is often shaped by the overall purpose of the organisation, set by its founding documents. For many asset owners now, it is vital that ESG is integrated within that purpose. Not least because, since October 2019, changes to the UK's *Occupational Pension Scheme Investment Regulations (2005)* have required pension schemes to set out in their *Statement of Investment Principles (SIP*) their policies on how they consider financially material ESG factors within their investment approach, as well as the extent to which they undertake stewardship, including engagement and voting. New reporting requirements, in line with European Union's (EU) *Shareholder Rights Directive II*, will reinforce the same sort of approach across the EU. Many other markets around the world have established similar expectations. The starting point for the investment process is often how ESG is viewed in the context of an overall investment philosophy or purpose.

Two reasonably representative examples of how such purposes are articulated by major global asset owners are shown below:

From CPP Investment Board (Canada):

> *"CPP Investments invests the assets of the CPP with a singular objective – to maximise returns without undue risk of loss taking into account the factors that may affect the funding of the CPP. Our investment strategy is designed to capitalize on our comparative advantages while ensuring we maintain our commitment to responsible investing".*[4]

From AustralianSuper:

> *"We work hard to maximise investment returns over the long term, so members can enjoy a better future. As long-term investors, we focus on investing in a mix of quality assets that can grow members' savings over time. We balance this with an understanding of the risks we need to take to achieve this objective and deliver competitive returns against our peers.*
>
> *Our four core investment beliefs are the foundation of our investment approach. A rigorous governance framework and disciplined investment process help us allocate and manage members' savings and maintain our position as one of Australia's leading super funds.*
>
> *Our four investment beliefs:*
>
> 1. *We return all profits to members.*
> 2. *We believe in active management – both asset allocation and stock selection.*
> 3. *We use our scale to reduce costs and better structure investments.*
> 4. *We're aware of our responsibility to the broader community, consistent with our obligations to maximise benefits to members."*[5]

How the purpose and investment beliefs and philosophy see ESG impacting investment performance – whether as risk factors or value creators – will shape how ESG is integrated into mandates and what the asset owner will expect of its fund managers. This is well-articulated in a McKinsey article from October 2017.[6] The article provides a framework for considering how to develop a policy and philosophy, and then how it can practically be implemented. It states that:

> *"A sustainable investment strategy consists of building blocks familiar to institutional investors: a balance between risk and return and a thesis about which factors strongly influence corporate financial performance."*

Responding to these two building blocks, McKinsey suggests that there are two fundamental questions that asset owners need to ask in developing their ESG investment philosophy:

1. **Are ESG factors more important for risk management or value creation?**

> *"If the mandate focuses on risk management, then the strategy might be designed to exclude companies, sectors, or geographies that investors see as particularly risky with respect to ESG factors, or to engage in dialogue with corporate managers about how to mitigate ESG risks. If value creation is the focus, on the other hand, investors might overweight their portfolios with companies or sectors that exhibit strong performance on ESG-related factors they believe are linked to value creation."*

2. **What ESG factors are material?** McKinsey notes that this is much less straightforward than the simple statement of the issue might make it seem, and that there are substantial reporting projects dedicated to identifying what is material at a sector level, let alone at an individual company level. The nature of the investment portfolio also adds a layer of complexity. The firm argues:

> *"The selection of material factors is often influenced to some extent by exposure to asset classes, geographies, and specific companies. For example, governance factors tend to be especially important for private equity investments, since these investments are typically characterised by large ownership shares and limited regulatory oversight."*

3 FULLY ALIGNING INVESTMENT WITH CLIENT ESG BELIEFS

9.1.2 Explain how ESG screens can be embedded within investment mandates/portfolio guidelines to: generate investment returns; manage portfolio risk.

Once the asset owner client has developed its investment philosophy and beliefs, this then needs to be translated into the specifics of the mandates that it awards to its fund managers. As McKinsey indicates, there are two key questions which will frame how this is delivered in practice:

1. Is ESG a risk management tool or a source of investment advantage?
2. Which aspects of ESG most matter from the perspective of the asset owner?[6]

Determining the answers to these questions will be the starting points for shaping the mandates awarded. Furthermore, in shaping the detailed expectations, the answers will need to be reflected in the terms of the individual mandates themselves.

The answers will also help shape the overall **strategic asset allocation (SAA)** of the asset owner – the long-term exposures that it chooses to have in terms of asset classes and geographies. They may also inform decisions around the asset owner's **tactical asset allocation (TAA)** or the short-term variations around the SAA to respond to nearer-term market and other circumstances.

Example

Pension fund concerned about climate change

A pension fund has strong beliefs regarding the impending impacts of climate change.

- The fund might establish multiple mandates investing in new technologies, including renewable energy generation.
- The fund's mainstream equity and debt mandates may well include screens that exclude fossil fuel investments.
- The fund may require that any sovereign bond mandate includes an active ESG overlay that seeks to limit exposure in countries where the physical impacts of climate change are likely to be most acute.

Example

Foundation investment portfolio concerned about human rights abuses

A foundation investment portfolio, where the investment beliefs feature major concerns regarding human rights abuses, might be more likely to:

- apply a screening approach across portfolios requiring the exclusion of any investment facing significant allegations; and
- screen out exposures to certain countries where human rights abuses are perceived to be a frequent occurrence or where human rights standards are deteriorating at a rapid rate.

Naturally in practice, the investment beliefs, and the mandates that are created to reflect them, are rarely as one-dimensional as the two examples above might imply. Furthermore, the client will always have an expectation of investment returns being generated alongside delivery of whatever broader expectations it places on the investment approach.

The McKinsey article also provides a helpful framework for understanding the different ways in which ESG considerations can be reflected in an asset owner's investment approach, and so be fully operationalised in the work of its fund managers. This is shown in **Table 9.1**.

Table 9.1: LEADING INSTITUTIONS APPLY SUSTAINABLE INVESTING PRACTICES ACROSS SIX DIMENSIONS OF THEIR INVESTMENT PROCESS AND OPERATIONS

DIMENSION OF INVESTING	ELEMENTS OF SUSTAINABLE INVESTING
Investment mandate	• Consideration of ESG factors, including prioritisation. • Targets.
Investment beliefs and strategy	• Rationale for ESG integration. • Material ESG factors.
Investment operations enablers:	
✓ Tools and processes	• Negative screening. • Positive screening. • Pro-active engagement.
✓ Resources and organisation	• ESG expertise and capabilities. • Integration with investment teams. • Collaborations and partnerships.
✓ Performance management	• Review of external managers (screening and follow-up). • Follow-up on internal managers (including incentives).
✓ Public reporting	• Accountability. • Transparency.

Source: McKinsey.[6]

Fund managers themselves, hoping to win mandates that reflect ESG concerns, will seek to develop their own policies that fully integrate ESG approaches into their portfolio management. This is both an element of marketing their approach and differentiating themselves in a crowded investment marketplace. An overarching policy also helps to train and shape the mindset of the investment teams themselves. An ESG policy should formally outline the investment approach and degree of ESG integration within a firm.

Such an ESG policy is an opportunity for a fund manager to highlight the relevance, or in some cases the lack of relevance, of responsible investment norms and principles (like those issued by the PRI) to a firm's investment strategy or strategies. A number of investment strategies face inherent challenges, some of which may be due to:

- the lack of ESG data within their scope; or
- a relative scarcity of methodologies and best practices to apply ESG integration within an asset class.

In each case it is worth noting that the ESG market is developing very rapidly and new offerings are being brought to the market all the time, meaning that there are increasingly fewer gaps in supply. Whether these new offerings meet their needs will be for the asset owners to decide.

Example

Multi-strategy investment firm

It is in the interests of a multi-strategy investment firm that manages both fundamental and quantitative ESG strategies to highlight the fact that active ownership activities (like engagement) are more relevant to more concentrated, fundamental strategies, rather than more diverse quantitative portfolios. The application of ESG to certain asset classes – such as commodities or money market funds – is in its infancy.

Here are two examples of ESG philosophies from leading fund management firms.

RBC Global Asset Management:

> *"We invest in sustainable great companies at attractive valuations and steward them for the long term. We use intangible, ESG and business assessment combined with strong risk analysis to achieve this. Financial analysis and ESG assessment are intertwined in judging a business. Businesses thrive over the long term when they invest in ESG intangible factors that lead to stronger more sustainable financials.*
>
> *We consider ESG factors as non-traditional sources of risk and opportunity which we believe should form part of every company assessment… The relevance of particular ESG issues varies from industry to industry, which is why we believe it is important to integrate ESG into the company assessment … rather than as a pre-screen or overlay. It facilitates engagement and ensures ESG risks and opportunities are incorporated into the fundamental valuation analysis driving financials."*[7]

Generation Investment Management:

> *"Our investment process underpins our differentiated thinking about the dynamics that drive and influence the performance of companies. We construct portfolios of sustainable companies with the confidence derived from our deep research and analysis.*
>
> *A sustainable company is:*
>
> *(1) one whose current earnings do not borrow from its future earnings;*
>
> *(2) one whose sustainability practices, products and services drive revenues, profitability and competitive positioning; and*
>
> *(3) one that provides goods and services consistent with a low-carbon, prosperous, equitable, healthy and safe society."*[8]

These philosophical statements then need to be operationalised into ESG policies that cover a range of practical issues. Regardless of the investment strategy or asset class, such an ESG policy needs to address the manner in which the portfolio manager:

- addresses ESG issues at portfolio reviews;
- establishes the rationale and methodology for ESG portfolio-level assessment;
- assesses exposure to ESG risk within the risk management function;
- determines ESG impacts to the portfolio;
- responds in the investment decision-making process to ESG implications; and
- discloses ESG exposure to the fund's investors.

Portfolio managers should also find ways to embed ESG information within annual or interim reports alongside financial information and manager commentary to fund investors. Annual reports may include:

- ESG activities across the portfolio;
- frequency of engagement; and
- highlighted activities and their outcomes.

Portfolios with private or unlisted securities exposure may choose to report portfolio performance against **key performance indicators (KPIs)** over a given investment period and relative to peers.

Reporting ESG information with consistency and continuity helps ensure compliance with the portfolio's ESG policy, responsiveness to ESG-related portfolio issues and effective portfolio oversight.

4 DEVELOPING CLIENT-RELEVANT ESG-AWARE INVESTMENT MANDATES

9.1.3 Explain the most common features of ESG investing that asset owners and intermediaries, including pension consultants and fund selectors, are seeking to identify through request for proposal (RFP) and selection processes: voting; engagement; examples of decision-making; screening process.

The International Corporate Governance Network's (ICGN) *ICGN Model Mandate Initiative: Model contract terms between asset owners and managers* provides a helpful framework and proposes best practices for ESG-aware investment mandates around:

- the monitoring and use of ESG factors;
- the integration of ESG factors into investment decision-making;
- adherence to good practice around stewardship; and
- voting and reporting requirements.

As the document states:

> *"As important as setting standards within fund management contracts is how clients can effectively call their fund managers to account in respect of these mandates. The intended standards will most effectively be delivered where managers are made accountable on a regular basis for their delivery against them."*[9]

According to a 2016 PRI report on *How asset owners can drive responsible investment*, investment mandates should require investment managers to:

- Implement the asset owner's investment beliefs and relevant investment policies.

- Integrate ESG issues into their:
  - investment research;
  - analysis; and
  - decision-making processes.
- Invest in a manner consistent with the asset owner's time horizons, understanding the key risks that must be managed to achieve the asset owner's portfolio goals.
- Implement effective stewardship processes, including:
  - engagement with companies and issuers on ESG issues; and
  - for listed equities, voting all shareholdings.

  This engagement should align with the asset owner's responsible investment and related policies.
- Engage constructively and proactively with policymakers on responsible investment and ESG-related issues. This engagement should align with the asset owner's responsible investment and related policies.
- Report on the actions taken and outcomes achieved. The reporting should enable the asset owner to:
  - assess the manner in which the investment manager has implemented the asset owner's investment beliefs and policies; and
  - understand how this has affected investment performance and ESG outcomes and impacts.[10]

Different asset managers adopt different responsible investment strategies because their investment philosophy and investment processes may fundamentally differ. For instance:

- some active investors focus on fundamental company-specific research, while others may emphasise quant models;
- some will be more event-driven, while others are more focused on identifying companies with a long-term track record of delivering superior financial performance;
- passive investment approaches need to build ESG priorities into the design of the mandate and the way in which investment assets are selected – typically, this is either by:
  - excluding certain investments (e.g. the fossil fuel sector, or particularly carbon-intensive aspects of it), or
  - applying a 'tilt' to a broad index (so that, to pursue the climate change example, the least carbon-intensive companies are chosen in each sector meaning that the overall portfolio has a reduced intensity).

As a result, different managers will integrate ESG in different ways:

- as a threshold requirement before investment can be considered;
- as a factor that informs the valuation or provides a quant basis for adjusting (or tilting) exposures;
- as a risk assessment that offers a level of confidence in the valuation;
- as a basis for stewardship engagement; or
- as a combination of two or more of these methods, which is very often the case.

An alternative form of classification has been proposed by CFA Institute, in its proposed *ESG Disclosure Standards for Investment Products* (under review at the time of writing, following a public consultation).[11] This highlights six main categories of products (not all of them mutually exclusive so that they might be offered in combination by some providers), as shown in **Table 9.2**.

Table 9.2: CFA INSTITUTE PROPOSED ESG PRODUCT FEATURES

PROPOSED FEATURE NAME	BRIEF DESCRIPTION OF FEATURE FUNCTION
ESG integration	Explicitly considers ESG-related factors that are material to the risk and return of the investment, alongside traditional financial factors, when making investment decisions.
ESG-related exclusions	Excludes securities, issuers or companies from the investment product based on certain ESG-related activities, business practices or business segments.
Best-in-class	Aims to invest in companies and issuers that perform better than peers on one or more performance metrics related to ESG matters.
ESG-related thematic focus	Aims to invest in sectors, industries or companies that are expected to benefit from long-term macro or structural ESG-related trends.
Impact objective	Seeks to generate a positive, measurable social or environmental impact alongside a financial return.
Proxy voting, engagement and stewardship	Uses rights and position of ownership to influence issuers' or companies' activities or behaviours

Source: CFA Institute Proposal for ESG-Related Features (2020).[12]

These variations in style should be readily apparent to asset owners (and the investment consultants that advise them). Therefore, they should help determine which is the most appropriate provider of services to fulfil the client's needs, consistent with their investment beliefs and philosophy. A further part of CFA Institute's proposal offers an indication of how this tailoring of styles of investment product to the needs of particular clients might occur (some of these imply a retail investor market, but the needs and what they might imply are nevertheless insightful for institutional products as well) (see Table 9.3).

Table 9.3: CLASSIFICATION OF ESG-RELATED FEATURES ACCORDING TO ESG-RELATED NEEDS

	ESG-RELATED FEATURES					
ESG-RELATED NEEDS	(A) ESG INTEGRATION	(B) ESG-RELATED EXCLUSIONS	(C) BEST-IN-CLASS	(D) ESG-RELATED THEMATIC FOCUS	(E) IMPACT OBJECTIVE	(F) PROXY VOTING, ENGAGEMENT AND STEWARDSHIP
(1) "I want to know that the ESG factors that are material to the risk and return of my investments are explicitly considered."	●					●
(2) "I don't want to violate my personal beliefs or the mission, principles or beliefs of my organisation."		●				
(3) "I want to make investments that I believe have relatively fewer negative effects, and more positive effects, on the people and things I care about and the world in which I live."		●	●		●	●

	ESG-RELATED FEATURES					
ESG-RELATED NEEDS	(A) ESG INTEGRATION	(B) ESG-RELATED EXCLUSIONS	(C) BEST-IN-CLASS	(D) ESG-RELATED THEMATIC FOCUS	(E) IMPACT OBJECTIVE	(F) PROXY VOTING, ENGAGEMENT AND STEWARDSHIP
(4) "I want to capitalise on investment opportunities related to long-term environmental or social trends."				●		
(5) "I want to invest in specific solutions that intend to make a measurable contribution to a defined environmental or social need, problem or goal."					●	●

Source: CFA Institute (2020).

The usual way that consultants and clients seek to understand and test fund managers' capabilities and approaches is through an RFP process (an invitation to pitch for potential business; see the following section for more details on this), usually followed up with interviews of short-listed candidates. Naturally, the client wants to gain confidence that the fund manager can deliver satisfactory financial returns while staying within relevant risk parameters. In addition, with regard to ESG considerations, the client wants to understand:

- whether the approach to integration is sufficiently robust to deliver an appropriate portfolio structure;
- that the fund manager is capable of delivering with certainty any hard constraints on the portfolio (such as negative screens);
- that the manager can deliver appropriately effective engagement to preserve and enhance value;
- that the manager actually delivers in practice what it sets out as its approach in these respects in its policy documents and other assertions; and
- there is often an overarching concern that the client is seeking confidence that the fund management firm genuinely has a solid ESG philosophy underpinning its actions, because that gives greatest confidence that the ESG activity is genuine and robust and will be delivered consistently over time.

Unless the fund manager can deliver all these necessary requirements (with the last two being perhaps the most important), it is unlikely to make it through the due diligence process.

The RFP process

The RFP process is a formalised one, and a little formulaic in most cases. The questions asked are generally high level, and although they sometimes ask for examples of delivery to ensure that the fund manager can demonstrate the truth behind its assertions, the resulting information will rarely reveal much of the substance of what is going on. The questioning now typically goes deeper than the basic question of whether the fund manager is a signatory to PRI (which for a period of time in many RFPs was the sole ESG question), but this is often still the starting point.

The larger fund managers have RFP teams that deal with the flow of questions and hold a bank of answers, which builds and extends over time with input from practitioners, but this may occasionally come at the detriment of tailoring of responses. The result is that clients will only be able to ask the second- and third-level questions that actually get closer to the truth of the underlying processes in the face-to-face interviews of the short-listed candidates, which are typically the second part of a manager due diligence process. The RFP questioning process does at least have the benefit of narrowing the field to a shortlist of potential providers.

The following table (marginally adapted from the PLSA original) sets out what might be the major ESG considerations for a pension fund, or other asset owner, when seeking to allocate a new mandate across the full range of potential asset classes. These are elements that may need to be reflected in the RFP process to ensure that ESG issues are appropriately delivered by the relevant mandate.

Table 9.4: POSSIBLE ROUTES TO INCORPORATING ESG BY ASSET CLASS

	MANDATE CHOICE	INVESTMENT INTEGRATION	ENGAGEMENT
Passive/index tracking	Trustees should consider the index benchmark and any ESG tilts.	No, or limited, manager discretion in stock selection.	Managers can exert influence on companies through engagement and voting. There is also scope for influence on market- and system-wide issues.
Active equity	Trustees could invest in ESG-oriented mandates, such as sustainable equity.	Managers should consider financially material ESG factors and their impact on future profitability in company evaluation. Traditionally, data availability and quality has limited the ability to do this in quantitative analysis, though this is changing.	Managers can exert influence on companies through engagement and voting.
Active fixed income	Some assets (such as green bonds) could be considered by trustees, but probably only as part of a broader fixed income mandate.	Managers should consider the potential for ESG risks to impact credit ratings and borrowers' future ability to make repayments.	It is possible for managers to have engagement with borrowers on material ESG risks, particularly at the time of initial issuance.
Real estate	Some real estate strategies could have E and/or S objectives, and appropriate assets may be targeted to achieve these.	Managers should consider material environmental and social risks during acquisition and development, and manage resource use during occupation.	Managers can engage with tenants and the local community to address potential issues and drive change.
Infrastructure	Trustees can consider portfolios biased towards infrastructure that supports a sustainable future.	Managers should assess the physical and societal risks arising from infrastructure assets. Longevity of investment means that systemic issues need to be considered.	Managers can exert influence on underlying companies or asset management through governance arrangements (e.g. board seats).
Private debt	Trustees could consider mandates that target lending at certain sustainable activities.	Managers should identify and seek mitigation of potential ESG risks during due diligence on loans.	Managers should have ongoing dialogue with borrowers to ensure that emerging and identified ESG risks are managed.

	MANDATE CHOICE	INVESTMENT INTEGRATION	ENGAGEMENT
Private equity	Trustees can assess which companies the manager may target and the potential for unwanted or desired ESG exposures to arise.	The longevity of the investment means that systemic risks need to be considered. Managers should assess potential ESG risks during due diligence and ongoing ownership.	Managers would be expected to have a high level of influence over company management and ensure that governance structures are effective.

Source: Based on Engaging the Engagers, PLSA/Investor Forum 2020.[13]

As the PLSA and Investor Forum explain in their *Engaging the Engagers* report (the text refers just to pension schemes, but the same is true for all asset owners; similarly, the focus of the report is on engagement but the thinking extends to ESG issues more generally):

> *"The appointment process for a new asset manager offers a key opportunity for pension schemes to thoroughly assess the market for a manager whose approach to stewardship, engagement and (where relevant) voting aligns with the scheme's own. Where a pension scheme is looking to hire a new asset manager through a tender and due diligence process, the statement of expectations with regard to stewardship should form a part of the contractual relationship with the manager. The due diligence process is likely to include some assessment of whether the manager can fulfil the pension scheme's expectations in the asset classes and geographies in question."*[13]

The document goes on to offer a series of potential questions to ask a fund manager as part of the due diligence process before appointment of a manager. As it states, not all questions will be suitable to every situation (for example, different asset classes or natures of mandate will demand different assessment criteria), and all will need to be tailored to the circumstances of the specific mandate. Nonetheless, the following provides a good basis for asset owners to seek to test potential service providers, and for fund managers to demonstrate the value that they can bring through their ESG work:

1. Understanding how the manager sees stewardship and engagement and what its main drivers for action are. This includes how consistently that philosophy is applied across asset classes and geographies.
    - How long term is the fund management firm's investment mindset? Is this reflected in the portfolio exposures, turnover and approach to engagement? How do these approaches vary across different teams and portfolios?
    - How does the manager decide on the resourcing given to stewardship? How is this overall resource shared across the firm's portfolios, asset classes and geographies? What plans are there for changing the resourcing of stewardship?
    - For which portfolios and asset classes does the manager believe it most needs to improve its approach to stewardship and engagement currently? What is being done to bring those up to the standards in the wider organisation?
2. Seeking confidence in the processes by which the manager's objectives are set and progress against them is monitored.
    - What systems does the fund manager have in place to capture engagement objectives systematically and to measure progress against those objectives?
    - What differences do those systems reveal about the nature and effectiveness of engagement between different asset classes, portfolios or geographies?
    - If different teams within the fund management firm have investment exposure to the same company or asset, how does the firm seek to have a concerted approach to stewardship and engagement? How does it leverage different perspectives and understandings of a business from those different teams?

3. Understanding how the manager allocates its engagement efforts between the different forms of engagement.
   - What form of engagement takes the majority of the manager's engagement resource? Why?
   - Are different forms of engagement more relevant in different asset classes, portfolios or geographies? Explain how.
   - What is the process for agreeing to escalate an engagement? What are the range of escalation tools available?
   - How does the application of escalation vary between different asset classes, portfolios or geographies? Are these differences appropriate?[13]

The aim of these questions is to provide a basis for assessing how robust each fund manager's approach to the area of stewardship and engagement is and so, a framework for effective differentiation between providers. The focus of the PLSA and Investor Forum report is largely on engagement, and so the focus of these questions is also. It is, however, relatively straightforward to broaden the coverage of the questions to encompass ESG integration as well (or instead).

Investment integration

Asset owners have their own investment philosophies and preferred investment styles so as clients, they will seek to test whether the responsible investment strategy adopted by the fund manager is coherent with their broader investment strategy and aligned with their preferences:

- some clients might be more interested in investing with a quant-fund manager running a smart beta product; while
- others might prefer a fundamental stock-picking fund manager with a concentrated portfolio of companies.

The important thing is that both strategies integrate ESG issues in a relevant and value-adding way, given the specificities of their respective investment processes.

Therefore, clients' key questions in this regard will always be around the investment decision-making process. Typically this operates on two levels:

1. An analysis of the formal process and in particular, how ESG is integrated. This will usually also incorporate an assessment of the portfolio as it stands (perhaps using some of the available analytical tools) to take a view as to whether it is consistent with the assertions as to ESG integration.
2. A discussion of the process as it has been applied to individual assets, usually framed by the client identifying one or more assets that are questionable from an ESG perspective, and testing how it was that the asset(s) in question were deemed to be appropriate to be included within the portfolio.

It is this systematic approach of assessing the overall portfolio and testing hard cases that usually reveals whether there is any real substance to the ESG element of the investment process.

The client is attempting to get under the skin of the fund manager's decision-making processes, to understand what actually determines whether an asset will be included in a portfolio or not, and the decisions that lead to different weightings within the portfolio. It is only through highlighting the factors that may lead to these concrete investment decisions that the fund manager can genuinely demonstrate that its ESG integration approach:

- is real and robust; and
- can be replicated effectively over time.

Furthermore, it is only through understanding how these factors drive concrete investment decisions that the client will begin to have confidence in the robustness of the way ESG is integrated in practice. Should the fund manager be appointed, future dialogue (the regular review meetings, typically annually, though sometimes more frequent) will again focus on assessing the overall portfolio for consistency with the asserted ESG integration and testing individual investment decisions to assess whether the investment process remains as promised and continues robustly to integrate ESG into decision-making. It is consistency of investment approach that an asset owner tends to be seeking.

→ *See Section 6 of this chapter for some sample questions of the sort of style that a client might ask a fund manager as part of ongoing monitoring; some of these might also be useful, or could be adapted, for due diligence discussions.*

As well as testing the investment process with hard cases, clients will usually look at metrics – notably portfolio turnover and Sharpe and other ratios – to see if these are consistent with what they understand of the investment process.

Increasingly, there are now also ESG portfolio assessment tools to help facilitate the assessment of the portfolio as a whole. These look at the overall ESG assessment of the portfolio constituents (typically an overview of the portfolio assessed against each category of E, S and G) and identify outliers within the portfolio, comparing these to the benchmark. While these assessments are subject to the challenges around the ESG analysis (most notably they are typically highly dependent on the disclosures made by individual companies, which are of variable quality and detail), they at least offer a basis for clients to test and challenge the effectiveness of ESG integration.

→ *For further detail on challenges in ESG analysis, see Chapter 7.*

Clients might also request that the fund manager provides them with an ESG performance attribution analysis, providing some insights into the value added by ESG factors on stock selection.

Clients can use these insights to test and challenge whether the portfolio manager continues to invest in line with the method that they were hired to deliver.

→ *This is considered in more depth below in Section 6.*

Engagement and voting

The other key area of client expectation lies around effective stewardship delivery. Clients will probe and test the effectiveness of fund manager voting and engagement approaches – both policy and delivery.

There are two crucial bases of assessment for any asset owner:

1. Who does the stewardship work: specifically, is it outsourced, delivered by a specialist stewardship team or is it the portfolio managers (or how do these individuals successfully work together)?
2. The closely connected issue of: how significant are the resources assigned to stewardship?

It should be no surprise that resourcing poses a real challenge to the effectiveness of engagement. As a recent study by the Institute of Chartered Secretaries and Administrators (ICSA) (now the Chartered Governance Institute) states:

> *"One factor mentioned by both issuers and investors were investors' resource constraints. With many major investors often holding thousands of firms in their portfolios it is only natural that their resources are stretched to engage meaningfully with all companies."*[14]

While teams are being expanded, this challenge remains – certainly company chairs believe that limited investor resource is a major limitation on effective engagement, and it is a repeated frustration for them. The ICSA study suggests that there has been an increase in the quantity of engagement but companies perceive that this growth in activity was 'not always accompanied by an increase in the quality of engagement'.

As discussed in depth in Chapter 6, prioritisation of engagements is a key way for fund managers to respond to resource constraints. Asset owners will want to understand how the fund manager prioritises engagements, both in terms of focusing on individual assets and in terms of prioritisation of particular issues for engagement. Part of a responsive fund manager's approach to prioritisation will be to understand what are clients' key priorities and how these might best be reflected in the fund manager's programme of activity. An asset owner will seek to understand through the due diligence process how they can best influence their fund manager and how responsive to their priorities the chosen fund manager is likely to be.

Concentrated portfolios are more easily resourced from a stewardship perspective, and those firms that most pride themselves on being active stewards tend to be genuinely concentrated and so can commit significant resources to these activities. This leads to one way of addressing the resourcing issue: portfolio managers themselves becoming more actively involved in stewardship. This is natural for fundamental active equity managers who hold concentrated portfolios of stocks and would typically maintain a constant dialogue with management. This is particularly true in markets with low liquidity (such as small caps or emerging markets) where the option for larger investors to exit is less available, but stewardship becomes challenging with larger portfolios of many stocks where managers may not have a direct dialogue with all the companies. Fund management houses with more diversified portfolios are more likely to develop larger, more stand-alone stewardship teams.

The alternatives to building specialist stewardship resource internally are **outsourcing** and **collective action**.

Outsourcing

Outsourcing is done by almost all investors in the area of voting, where proxy advisers are hired to provide:

- a voting platform and the pipework; and
- advice on how to vote.

Different investors lean to different extents on such advice, but few ignore it entirely – not least because of that issue of the breadth of portfolios and the difficulty of addressing all votes in a concentrated period especially for a potentially long tail of small investments. Voting service providers are somewhat controversial because companies tend to believe that they have too much influence on voting decisions and thus, press for higher standards of conduct; increasingly investors ask these providers to apply their own voting templates but few investors reveal the extent to which their voting differs in practice from the voting recommendations of their advisers. In turn, investors may express frustration that companies often seek more dialogue with the proxy advisory firms than they do with investors themselves.

Some asset owners take control of voting directly; others ask their fund managers to reflect their policies; but the majority tend to leave voting decisions entirely in the hands of their fund managers. They tend to do this having assessed the alignment between the fund manager's voting policies and approaches and their own as part of the due diligence process, with this alignment playing a part in their choice of manager. They will also seek to assess the quality of voting decision-making over time as part of the ongoing monitoring process. As with monitoring of the investment process and investment decision-making, this is best done by talking about hard cases that the client itself identifies.

Collective action

The other way in which investors can share resources is through collective engagement approaches.

→ *See Chapter 6 on engagement and stewardship for more on collective vehicles, and engagement and voting more generally.*

Assessing the quality of engagement and voting

Since resources are always limited, clients should always ask how the fund manager ensures that the use of its resources is most effective. Fund managers should be able to set out a thought-through structured approach to targeting engagement and delivering change for the benefit of clients.

Example

Fund manager and direct engagement

A fund manager might undertake direct engagement with a few of the larger holdings in the portfolio where concerns on material ESG issues have been identified. This might be complemented with broader engagement on a number of issues with a larger number of companies through specialist providers.

Finally, the fund manager might identify one key issue (e.g. climate risk disclosure) where systemic change is required and which might best be addressed through collaborative engagement initiatives.

It is likely that any structured approach to resource efficiency will always need to encompass some form of collective body, as such organisations assist both in terms of effectiveness and in efficiency.

Voting is also considered by clients as a key aspect of stewardship. Voting often gets more attention in client assessments because the datapoints on voting are clearer, for example:

- How does the fund manager vote in general?
- By what process does the manager reach its decisions?
- How did the manager vote on specific controversial matters?

The most sophisticated clients seek to discuss specific votes at individual companies as the basis for testing whether the policy and process actually lead to justifiable results in practice. This enables more granular discussion, which reveals more of the substance of the fund manager's approach and avoids the fund manager selecting individual cases that put their work in the best light.

Assessing engagement is harder. Because engagement is nuanced and long-term, it is hard to have a clear view of its effectiveness. It occurs in private meetings so the visibility of even the activity itself is low, but the difficulty goes further than this: effectiveness is largely invisible even for the engager. Any investor that asserts with certainty that they have made a change happen at a company is most likely overstating their case: in almost every case this simply cannot be known. There may be a correlation between what an investor sought and what happened, but correlation is not the same as causation. After all, it is not shareholders who make decisions about the strategies of companies but company boards; shareholders can influence and persuade but it will always be the board that actually decides.

This is reflected in the performance measurements that investors themselves place around engagement. Mostly developed by the stewardship overlay providers, these tend to be schemes to reflect the changes made by companies as engagement progresses. Expressed as either milestones or objectives, the engagers measure progress towards concrete change or better practice over the three or more years typical of the engagement process. It is these metrics that clients can assess and challenge, as well as having direct dialogue with the engagement team to gain some confidence in the robustness and sense that lies behind the measurements.

5 TAILORING ESG INVESTMENT APPROACH TO CLIENT EXPECTATIONS

9.1.4 Explain the different client types and their objectives which influence the type of ESG investing strategy selected.

Different clients (institutional, retail or private) have different investment objectives, risk/return profiles and drivers. These will influence the type of ESG investing strategies they will consider most attractive.

Table 9.5 provides a (highly) simplified and generalised insight into the likely primary drivers towards ESG investing and so the relevant risk/return profiles and implied favoured ESG approach, for broad groupings of investors. As with all generalisations, there will be many individual exceptions to these indicative and broad-brush characteristics.

Table 9.5: OVERVIEW OF INVESTOR DRIVERS

Investor	Defined benefit (DB) pension scheme	Defined contribution (DC) pension scheme	General insurer	Life insurer	Sovereign wealth fund	Foundation	Individual investor
Investment time horizon	10–70 years	10–70 years	1–2 years	10–50 years	30–150+ years	50–250+ years	1–50 years
Primary driver for ESG investment	Fiduciary duty	Fiduciary duty, personal perspectives of beneficiaries	Awareness of financial impacts of climate change	Recognition of implications of lengthy investment time horizons	Reputational risk	Reputational risk, investment consistent with founding or charitable aims	Personal ethics and per-spectives
Risk mindset	Long-term perspective should permit higher risk tolerance	Where individual beneficiaries are permitted to switch providers, greater risk aversion than time horizon might otherwise imply	Loss aversion	Long-term perspective typically permits higher risk tolerance	High tolerance for illiquidity and short-term under-performance	High tolerance for illiquidity and short-term under-performance	Loss aversion
Implied favoured ESG approach	ESG integration	Some exclusions, ESG integration	ESG integration	ESG integration	Some exclusions, ESG engagement approach often most important	Exclusions likely, to ensure investment is consistent with founding or charitable aims	Screened funds, strong ESG integration

Within the institutional investment community, clients generally expect that ESG will be genuinely applied across the approach so that the asset owner can invest across the asset classes and benefit across all of them from the integration of ESG factors and effective stewardship engagement. This expectation is increasingly true whatever asset class the asset owner is investing in (the scale of the membership of PRI emphasises the scale of the commitment to ESG overall), and questions about the overall ESG philosophy and approach of the investment house are usually built into the discussions.

As discussed earlier, often these expectations are written into the mandate – the contract between the fund manager and the client. On occasions, however, the specific ESG (or other) requirements of a client are not included in the contractual mandate itself, but in a side letter, which also has contractual status. An insight into this model is provided by the *Brunel Asset Management Accord*.[15] This document sets out a pension manager's approach to long-term investment and ESG factors, but in a form of words that it believes is less-suited to the hard legal language of a specific contract, but more to a softer form of agreement whereby the fund managers are enabled more clearly to understand the client's perspective and so, align to it. For the purposes of this chapter, we talk about mandates in a way that encompasses side letters or any other legal documents that frame the agreement between a client and a fund manager.

The issue of time-horizons of the asset owner, and the overall investment philosophy, incorporating the institution's understanding of ESG factors and their impact on value over those time-horizons, goes to the core of delivering mandates that actually encourage fund managers to respond appropriately to ESG risks and opportunities. As the ICGN's *Model Mandate* puts it:

> "*The time horizon of most asset owners is considerably longer than that of fund managers. Thus for long-term portfolios, the factors and risks which matter to the asset owner are somewhat different from those typically considered within fund management processes. But as these factors and risks will impact their long-term returns, many asset owners are keen to see more effective integration of these longer-term factors into investment processes*."[9]

Even where an asset owner is seeking to invest in a particular ESG fund (for example, a bond fund tilted away from CO_2-intensive industries and towards businesses less likely to be disrupted by carbon taxes and constraints), asset owners are unlikely simply to ask regarding the approach within that specific fund. Rather, the overall mindset and philosophy of the fund manager are important because they provide a context of confidence that the specific fund has backing and will be resourced long term. Engagement is often an integrated activity across the investment house, meaning that there may be an opportunity to leverage off activity on behalf of other portfolios and asset classes.

To take the example of a carbon-tilted bond fund, there might be direct stewardship in relation to the fixed-income investments, but the fund could also benefit from the investor's broader engagement approach. This means that the fund could be informed by engagement on equity portfolios. Thus, the bond fund could benefit from the changes that equity engagement can deliver at holdings within the bond portfolio also.

Fund managers that integrate ESG across their funds and genuinely join up their activities find that engaging with firms with the perspective of equity and bond investment (and potentially other exposures also, for example through property portfolios) is often the most productive route of all. The investment house's overall approach to ESG thus matters to large asset owners, which will tend to probe whether this collaboration across the investment house happens effectively.

The same is true for retail investors as well, but often these investors are looking more for a product. Inevitably, they are constrained by the investment vehicles that they can invest in, but also, they are more likely to be seeking out an investment fund that suits their personal ethics and perspective on the world. Therefore they may seek out funds that exclude 'sin stocks' or avoid particularly carbon-intensive businesses. In fact, this approach is often mirrored by some institutional investors (such as foundations or religion-linked asset owners) where they have a moral constraint on their freedom to invest. For these investors, the ability to deliver exclusions and effectively screened portfolios is often more important than the broader philosophical approach of the investment house. Stewardship engagement is typically important to these investors, but may also get less challenge and focus in discussions.

Growing fields (such as impact investing) have developed from offerings to high-net-worth individuals and foundations into more mainstream investment vehicles. They are at times offered to mainstream asset owners although there are issues around the scalability of such investments. In many cases, it is difficult for large asset owners to take an interest in such opportunities because they may not be available in large enough pools for it to be worth the attention of the asset owner.

Liquidity is also an issue for this form of investment: traditionally, a private market form of investing, money is often locked up for lengthy periods, and exiting a position may be difficult for an institutional or retail investor in need of liquidity. One response to this from the investment community may be rebadging broader investment approaches as 'impact'; the wise client will never buy on the basis of the badge but will always look to understand what the underlying investment philosophy and process is for any product, and select accordingly. Nonetheless, fund managers beginning to consider their portfolios' broader real world impacts – and to report on them – is a useful innovation in bringing home the reality of investment as part of the real world rather than in some way divorced from it.

6 HOLDING MANAGERS TO ACCOUNT: MONITORING DELIVERY

9.1.5 Explain the key mechanisms for reporting on and monitoring performance and mandate alignment with client objectives.

There will typically be annual performance discussions with fund managers once appointed; however, some clients may:

- insist on more frequent dialogue (this is likely particularly to be the case if financial or other performance has given rise to concerns); or
- choose to send a message that they care only about the longer term by waiting longer for any such discussions.

Performance (at least for assets that are freely traded or otherwise regularly valued) is likely to be assessed, or at least seen, more frequently than this. One of the challenges for a client is always to ensure that its fund managers do not become more short-term in their approach because they are aware the client is considering performance on a regular basis.

The Brunel Asset Management Accord highlights one way in which clients can do this. The document emphasises that short-term underperformance is not in itself likely to give rise to undue concern for the client:

> *"Investment performance, particularly in the short term, will be of limited significance in evaluating the Manager."*[15]

Rather, the list of issues that it identifies as likely to give rise to concerns are much more about culture and a failure to adhere to the expected investment process or style:

- Persistent failure to adhere to Brunel's investment principles and the spirit of the accord.
- A change in investment style, or investments that do not fit into the expected style.
- Lack of understanding of reasons for any underperformance, and/or a reluctance to learn lessons from mistakes. Conversely, complacency after good performance should be avoided.
- Failure to follow the investment restrictions or manage risk appropriately, including taking too little risk.
- Organisation instability or the loss of key personnel.

This focus on culture and conflicts, and an investment approach that is not consistent with the expected investment style is consistent with the thinking of the *ICGN Model Mandate.*[9] Among other things, this asks for early reporting of the following:

- The turnover in the portfolio for the reporting period and an explanation if the turnover is outside the expected turnover range for that period.

- Any changes to governance, ownership or structure of the fund manager, or in its investment approach or risk appetite.
- Any regulatory investigation or legal proceedings against the fund manager or any key staff or the fund.
- Any changes in staff ownership in the fund or any equivalent vehicle managed by the fund manager, or changes in staff ownership in the fund manager itself.
- Regular financial accounts of the fund manager.
- Any changes in, or waivers of, the fund manager's conflicts of interest policy.
- Any additional conflicts that have arisen over the reporting period.

Moving away from market benchmarking helps to change the mindset about performance and the particular focus on any underperformance. For example, it is a very different thing for a client to seek absolute returns or performance of a certain number of percentage points above base rates than it is to seek performance ahead of the standard equity benchmarks. Nonetheless, fund managers may be easily tempted to act in a more short-term way if they perform poorly against a general market performance, and clients who are concerned for long-term performance need to guard against this temptation.

As both Brunel and the ICGN identify, the crucial assessment in terms of ESG factors is whether the investment approach has been consistent with the process promised in the mandate and witnessed through the due diligence process. In many ways, the annual or other performance assessment is likely in practice to reflect the style of a due diligence process, seeking to confirm that the approach has remained consistent or assess what may have changed.

To provide insights into what these processes are likely to involve, the following case study includes a sample set of probing questions of the sort that an asset owner might deploy in discussions with a fund manager in ongoing regular conversations to assess whether the manager is performing in accord with expectations. These are indicative only and intended to provide an idea of the nature of insight and discussion that an actively engaged asset owner will be seeking (note that a few of these questions are developed from examples published in *Engaging the Engagers*).[13]

Case study

Sample questions an asset owner might ask to gauge a fund manager's ESG approach

Structural and cultural

You place great emphasis on the size and experience of your firm's investment team.

- How do you ensure that you get a consistent level of quality in terms of ESG analysis from such a disparate group of analysts?
- Are there sectors or geographies where you currently worry that the analysis may be weaker?
- What do you do to address any weaknesses?

You highlight your interaction with other investment teams.

- What does this amount to in practice?
- Please provide concrete examples of how this has worked in the recent past, one with your ESG team, and one with one of the other teams.
- How has interaction changed in recent years?

How are your holdings in XX and YY consistent with your stated approach to stewardship and long-term investment? Aren't there clear risks associated with these businesses? How have your investment teams factored those risks into their decision-making?

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Case study

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You have carried out a lengthy dialogue and engagement with ZZ.

- What impact has that had on the investment decision and the relative weighting within portfolios?

Property/infrastructure investments, direct and indirect

- In your estimate, which of your various property and infrastructure business holdings is best positioned in terms of preparedness for climate change and the physical disruptions, which seem increasingly frequent from extreme weather events?
- Which of your holdings is the least ready given the differences in geographical exposure to disruption?
- What does that mean for your portfolio positioning?

Financial sector investments

Bank X has recently made a commitment on coal project financing.

- Do you believe that undertaking is strong enough to ensure its risk profile on carbon-intensive assets?
- Not least given the bank's ongoing lending to oil and gas related projects, do you believe that it has a clear understanding of climate risk and potentially stranded assets in its lending portfolio?

How have you assessed the lending practices of non-bank lenders in your portfolio relative to their peers? Please describe how you have analysed their risk management in light of the significant failures in the sector and tightening regulatory environment.

You are interested in Insurance Company AA.

- Have you discussed with Insurance Company AA its approach to the risk of exposure to disruptions arising from climate change?
- How have you assessed their overall transition risk exposure?
- Are you confident that the company understands its exposures fully and is equipped and skilled enough to be managing them appropriately?

Industrial sector investments

You are liaising with Industrial Business Y.

- Are you concerned by the allegations regarding worker treatment at Industrial Business Y?
- Have you built into your model any expectation of fines or substantial damages claims, and are you confident that the dividend remains secure in most realistic scenarios?
- Can you be sure that the business is sustainable when it relies on such employment practices to maintain profitability?
- Do you have concerns about the costs of any changes in facilities or working practices to avoid future such exposures?
- Do you believe the company will retain staff and continue to be able to recruit appropriately skilled individuals?

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Case study

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You have a sizeable aggregate position in Company GG. The governance of the company is particularly weak.

- What makes you comfortable that the business is run and overseen effectively and will appropriately address emerging challenges?
- Is the complexity of the corporate structure more about financial structuring and tax minimisation than anything else?
- In which case, is there a risk that the management and board (which suffers from poor independence and weak governance) may miss signals from the underlying businesses because information flow is weak through the complex corporate structure?
- How are you engaging with the company on these issues and what progress have you made so far?

You are liaising with Company BB.

- What do you think about Company BB's exposure to corruption risks?
- Does it have satisfactory management structures to mitigate and manage such exposures?
- Are you confident in the company's approach to money-laundering protections and in knowing the full backgrounds of its business partners?

Extractives sector investments

You have some significant holdings in oil and gas businesses.

- What is your reflection on the risks that they face in terms of stranded assets?
- Which of these companies best understands the risks of climate change for their business models?
- How are they considering transitioning their businesses to a more carbon-constrained world?

State-linked extractives company Z is also highly politicised.

- Are you content that its investments are commercial and will give economic returns, rather than more based in geopolitics on behalf of the government?

You hold a number of mining businesses. Their business models are inherently unsustainable.

- Which of these companies manages its E&S risks best and which retains the greatest downside exposures?
- Which has a better handle on health and safety issues, and which better considers the implications of climate change (including the physical risks of extreme weather events) for their business?
- What has that analysis meant for your investment allocations?

Debt investments

The fund has a number of sovereign debt holdings, in particular exposures to CC and DD governments.

- Do you consider that those countries have appropriate and effective national responses to the challenge of climate change?
- Aren't their nations and economies particularly exposed to extreme weather events and also to water shortages already, factors that will only intensify as climate change progresses over the time-horizon of your bond holdings?

cont'd...

Case study

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- Will they be able to respond robustly and effectively to these challenges, without affecting economic activity and their ability to finance existing debt?
- What is your exposure to green bonds in the portfolio? Why is there only minimal exposure?

Engagement

Is there clear disclosure of the processes by which objectives are set and progress against them monitored?

- Who in the team sets engagement objectives? What is the oversight process to ensure that these objectives are robust and material, and remain consistently so across the organisation?
- How is progress against objectives assessed and captured for reporting? How do you gain confidence that material change has indeed been delivered?
- How do you decide to escalate an engagement if it has not been effective initially? What is the decision-making process and how do teams decide between different forms of escalation (such as collaborative engagement or going public with concerns)?
- Can you give examples of cases where you have chosen to exit investments rather than continue to pursue engagement?

Test the quality, materiality and bespoke nature of the objectives for an appropriate sample of engagements.

- Asset EE is a significant holding and faces some key risks. Can you demonstrate objectives that are in place for engagement with the investment, what actions have been taken to deliver those objectives and what progress has been made in delivery?
- You have sold out of asset FF over the period. Can you outline the engagement experience with its management over the last two years? What would have needed to change for you to be comfortable continuing to hold the asset?

Are headline market-wide announcements reinforced by robust and tailored asset-specific activity?

- You have made substantial public statements in the last period. How do these get translated to concrete actions on the ground? How have the dialogues with individual assets changed as a result? Please give examples, including of the relevant objectives set for engagement.

The other form of ongoing assessment of ESG delivery that clients are likely to perform is some portfolio-wide assessment. Inevitably, as this covers portfolios as a whole, this is on a more statistical basis rather than the more anecdotal basis of the questions in the previous case study. The main ESG research houses (the market is currently dominated by MSCI and Morningstar's Sustainalytics) now provide standard tools for asset owners to assess the ESG factors within their portfolios and also ESG-linked performance attribution. Typically, an asset owner that signs up to these tools will receive an analysis of all of its portfolios; alternatively, a fund manager might choose to take the service in order to test its own approach and prepare for client questioning.

Inevitably, as some of these tools are based on the research houses' data, they will be subject to the issues that arise around the quality and consistency of that data, and some fund managers may raise concerns that these are not a fair representation of the portfolios that they construct and of the quality of their ESG integration. Such a fund manager should be prepared to demonstrate how their own analysis of the ESG exposure of assets in the portfolio is a more accurate representation than those provided by external research firms. Even though there are limits to the quality of the external research, these analyses offer a basis for a conversation. As long as all parties take into account the limitations of the third-party approach (rather than assuming that the analysis provides some perfect insight), the conversation can be a challenging and useful one. In particular, the questioning can help the fund manager reveal once again the quality of its ESG integration and the depth of thought that goes into its investment decision-making.

The following case study provides an insight into the sort of data and analysis that might be provided in one of these standard ESG portfolio analysis tools. It also discusses ways in which a client might use that information to probe the quality of delivery by a fund manager.

Case study

ESG attribution

This case study highlights the style of reporting which a client might receive from a fund manager or a third-party ESG research provider about the portfolio, and the questions that might arise as a result. Of course, some fund managers take this form of research themselves so that they can, at least in part, pre-empt these questions, or at least be ready for them when they do come. It would be possible, of course, for the client to look at the data and comparisons for aggregate ESG figures, but the use of individual E, S and G factors seems most common.

Portfolio New Deal: overall portfolio analysis

	Portfolio New Deal (%)	Benchmark (%)	Positioning above or below benchmark (%)
E score	79.2	83.4	−4.2
S score	81.7	80.3	1.4
G score	84.2	84.6	−0.4

This analysis suggests that the portfolio is placed:

- better than the benchmark on S factors;
- pretty much at benchmark on G factors; and
- significantly below benchmark on E factors.

Client interest is therefore likely to focus particularly on E exposures in the portfolio.

Naturally, there would be scope for a discussion about whether the benchmark is an appropriate comparison for the portfolio (in the same way that this is frequently a discussion in relation to investment performance analysis). There is also scope for debate and discussion about the ESG research provider's analysis, although this is probably best done on an individual company basis. Most clients recognise that there are flaws in any firm's ESG analysis, and are likely to view discussions on individual ratings as an opportunity to test and understand the quality of the fund manager's own ESG analysis and integration.

Individual company analysis from ESG research provider

There are usually separate tables for each of E, S and G scores in these forms of analysis; we provide a sample of only one here. For the purposes of this case study, the table below focuses on the E score in the context of the overall portfolio positioning.

cont'd...

Case study

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Bottom five E detractors

COMPANY	E SCORE (%)	PORTFOLIO E SCORE (%)	BENCHMARK E SCORE (%)	DETRACTION LEVEL (%)
Digger Mining	33.2	79.2	83.4	50.2
Smoky Power Generation	39.7	79.2	83.4	43.7
Flaring Oil Producer	48.1	79.2	83.4	35.3
Leaky Manufacturing	56.7	79.2	83.4	26.7
Sullen Motors	62.1	79.2	83.4	21.3

Very often the client will also see a group of outperformers for each of the ESG categories, but naturally tends to focus on the detractors. They will concentrate on the individual cases and the investment decisions that have led to their inclusion in the portfolio (taking particular interest in whether their inclusion is consistent with the mandate that has been agreed), and are likely also to use these specific cases to seek to understand:

- what the relevant investment decisions reveal about the investment process overall;
- whether that overall process is consistent with their understanding of what the fund manager had undertaken to do in the due diligence discussions and in the agreed mandate; and
- whether they remain comfortable with the investment process further to their clearer understanding of it.

It is likely, therefore, that an asset owner will ask some of the sorts of probing questions highlighted in the earlier case study to assess whether:

- the companies are indeed a sensible part of the portfolio; or
- they are evidence that the manager is not in fact delivering the investment process (integrating ESG factors) that has been contracted for.

Very often a fund manager will explain that the rating provided by the agency is based on historic data, and the fund manager's own engagement with the company indicates that it has already changed and/or is in a process of change. The client is likely then to explore:

(1) what engagement the fund manager has carried out;

(2) its level of confidence in the company's approach as a result of that engagement; and

(3) over what time horizon that change is likely to be more visible to external parties.

Prudent clients return to these cases after an appropriate time has passed to see what has indeed changed over that period. Changes that reflect the fund manager's explanation will clearly reinforce client confidence; a lack of concrete change and no real prospect of such change may undermine it. Time often enables clearer determination of superior analysis.

Frequently, analyses include the carbon intensity of companies in the portfolio, often in comparison to a suitable index. We do not provide an example of this in this manual, but that will, for many clients, be an issue for close attention. It is also likely to be an area for close questioning, particularly if a fund manager's purported focus on climate change issues does not seem to be reflected in a less carbon-intensive portfolio. Again, if the fund manager asserts that this is a timing issue with the service provider's analysis, the client is likely to want to explore that further at future meetings once the manager's alternative analysis has had a chance to be delivered in practice.

7 HOLDING MANAGERS TO ACCOUNT: MEASUREMENT AND REPORTING

9.1.6 Explain the key challenges in measuring and reporting ESG-related investment performance: active, passive and smart beta approaches; performance attribution; sensitivity analysis; risk measurement; engagement activity/impact; integrated reporting and investment review.

ESG reporting by investment managers is widespread but varies in quality of disclosure. It ranges from:

- general discussions of current debates and themes with no clear linkage to the work of the fund manager, sometimes associated with generalised aspirations or assertions; through to
- much more concrete discussions of the work actually done by fund managers and delivered in practice, to the shape of portfolios and change through engagement.

As discussed in detail in **Chapter 6**, the new *UK Stewardship Code* calls for more reporting on outcomes from stewardship and ESG activity, rather than just discussions about broader events, or the policies and activities of signatories. This pressure for discussion of what has concretely been delivered to the benefit of clients (which some managers call 'impact') should improve the quality of fund manager reporting, reducing generalised reporting and increasing the focus on concrete activity. We will see how fund managers rise to this challenge from March 2021, and see what impact it has on reporting on stewardship and ESG elsewhere in the world.

Investment firms typically produce annual (and often quarterly reports) describing:

- their investment processes;
- the themes that they have worked on; and
- case studies on ESG investing or stewardship, or both.

Investment firms that are signatories to the PRI are also required to submit an annual report on their activities. According to the PRI, the reporting process allows signatories to:

- evaluate their responsible investment progress against an industry-standard framework;
- receive ongoing feedback and tools for improvement;
- benchmark their performance against peers;
- see the big picture by understanding the state of the market;
- strengthen internal processes and build ESG capacity; and
- summarise activities for staff, clients, shareholders and regulators.[16]

A public version of the PRI report is made available to others, as well as the headline scores. Naturally, those fund managers that perform particularly well on the PRI assessment will tend to highlight and publicise this – emphasising in particular those asset classes where the fund manager performs best.

Alongside these reports, there are now multiple tools available to deliver information on the ESG characteristics of a portfolio and to measure those relative to relevant benchmarks. As a 2016 report by the Pensions and Lifetime Savings Association (PLSA) pointed out:

> *"By applying ESG data to existing standard benchmarks, the pension fund can measure its portfolios against the same standard market benchmarks currently used to measure performance. For example, if the pension fund measures equity performance against the MSCI World, it can continue to use this same benchmark, but this time containing an ESG data set, to facilitate a comparison of the portfolio's ESG score with the MSCI World. Conversely, a pension fund could choose customised ESG indices for a more effective comparison. For example, if a pension fund has excluded fossil fuel stocks from its portfolio, it may wish to measure ESG performance against an index that has been optimised to exclude fossil fuel stocks."*[17]

A further form of reporting that some fund managers provide on the ESG characteristics of their portfolios is to report on real-world impacts, or at least on the equivalent real-world impacts. Such measures as the tree-planting equivalent of a carbon-tilted fund (or the equivalent of the number of cars taken off the road) are a little manufactured – and clearly rely on multiple assumptions – nonetheless they relate the investment process to the real world and may prove especially powerful for retail investors in particular. Such reporting is still in its early stages and may well need further assurance and consistency for it to have real power.

There are also numerous performance attribution service providers, disaggregating the drivers of investment performance and identifying where performance comes from. Investors will be well used to identifying the five leading stock performers and detractors from performance over their client's defined reporting period. This is usually accompanied by factor analysis and measurement of risk exposures as well.

Some of these factors and risk measurements are now likely to be attributed to ESG performance metrics. A form of ESG attribution that a client might be presented with, either by the fund manager or by a third-party provider, is outlined and discussed in the **case study** on ESG attribution above.

The attribution of returns to ESG is challenging, not least because of the significant range of investment approaches that are included within the broad realm of ESG investing. It is relatively easy to assess the performance drag or enhancement that comes from excluding an industrial sector (such as tobacco), but it is hard to demonstrate the value added by a programme of engagement, particularly given the timescales usually required for engagement programmes to reach positive outcomes. Furthermore, the more fully integrated ESG becomes into the investment process, the harder it becomes to disaggregate a particular ESG driver from the broader investment decision.

In 2015, the PLSA published a disclosure guide for public equities developed by a group of pension schemes, setting out some pared down expectations for manager-reporting on both ESG integration and stewardship activities.[18] The disclosure on ESG integration asks for separate disclosure on both:

1. identification of ESG risk; and
2. the management and monitoring of ESG risks and opportunities, with suggested possible disclosures in respect of each.

The first three possible points offered as ways to demonstrate the identification of ESG risk and opportunity are:

1. Examples of where and why the manager is prepared to take either stock or sector ESG risks, or where it sees opportunities.
2. Quantitative or qualitative examples of material ESG factors identified in fundamental analysis and stock valuation.
3. Identification of long-term ESG secular trends and themes (as potential determinants of future growth or valuation etc.) and the extent to which they have influenced portfolio construction decisions.

The proposed possible disclosures to demonstrate the management and monitoring of ESG risks and opportunities include:

- Stock level ESG analysis for top risk and performance detractors or contributors in the reporting period.
- Any material changes to portfolio companies' ESG performance. Examples may include where the manager's view of ESG risk and opportunity differs from the market or rating agencies.

Similarly, the *ICGN Model Mandate* requests two areas of disclosure that are ESG-specific:

1. **The manager's assessment of ESG risks that are embedded in the portfolio.** This should include both what these risks are, and what the manager has done to identify, monitor and manage them. This can readily be compared against the external tools used to assess ESG risk in the portfolio, or the ESG element of the performance factorial analysis. This should prove a core element of the portfolio manager demonstrating their genuine ESG investment credentials.

2. **A detailed disclosure of stewardship engagement and voting activity.** The mandate is clear that these need to be two separate disclosures, i.e. disclosure merely of voting activity is not sufficient to satisfy the requirement for engagement disclosure.

   The PRI's 2016 *Practical Guide to ESG integration for Equity Investing*[19] (which builds on the organisation's 2013 publication on aligning expectations)[2] includes multiple different case studies from fund managers outlining their approach to ESG integration and highlighting their assessments of how their ESG work has added value.

   It is apparent that there are as many approaches to the integration of ESG factors as there are underlying investment approaches themselves. What the asset owner will want to know is whether the ESG approach is:

- genuinely aligned with the fund manager's investment style;
- delivered effectively in practice; and
- aligned with their own investment needs and beliefs.

To guard against a fund manager selecting individual cases that put their work in the best light, some clients seek to identify outliers so that they can test whether the asserted method for ESG integration is genuinely delivered in practice, consistently across the portfolio as a whole.

There is no set or agreed format for engagement disclosure and so, each fund manager has their own model. Typically, this includes statistics on activity at a greater or lesser level of granularity. It is no longer acceptable to provide statistics at organisation level that are not specifically tailored to the fund in question. In addition, the typical disclosure includes a sample of written descriptions of individual engagement meetings; again, these should be tailored to the fund, but many fund managers reveal more about the focus of their activities than they intend by the imbalance in their reporting towards their home market and region.

Many fund managers, and particularly the specialist stewardship providers, disclose their form of analysis of what has been delivered in the period through their engagement activities. Most use some measure of either milestones or progress against KPIs to provide their assessment of progress. These are proprietary models and inevitably, somewhat prone to a little bias in the analysis, however clients are able to test these in detail. At a minimum, these disclosures provide some transparency into deliverables from engagement.

KEY FACTS

1. Agency problems exist within the investment chain just as they exist between companies and their owners. This agency problem also extends to aligning ESG beliefs.
2. Accountability and alignment can be delivered in large part through aligning the time horizons of fund managers with their clients. This helps ensure that fund managers will work to accomplish their fiduciary duties.
3. This can be reinforced through a focus on longer-term factors rather than short-term performance assessment.
4. ESG integration will vary between different fund management firms, and individual portfolio managers, tailored to the established investment style and approach.
5. Increasing numbers of advisory services are available to help clients assess the ESG delivery of their fund managers and attribute performance and E, S and G characteristics of the portfolio. These are perhaps best used in dialogue with managers to test whether they are delivering their expected investment style in practice.
6. Asset owners will seek to challenge and debate hard cases of individual assets within portfolios so that they can understand how effective ESG integration is in practice and how well the portfolio reflects that integration.
7. Inadequate resourcing of ESG work is always a constraint on effectiveness and the application of the integration and engagement approach across portfolios. Collective engagement is one key way to bolster resources.
8. The ESG expectations of clients have a range of drivers and therefore manifest in different forms.

CHAPTER 9

SELF-ASSESSMENT

These self-assessment questions are provided only to enable you to test your understanding of the chapter content. They are not indicative of the types and standard of questions you may see in the examination.

Questions

1. **Which of the following, according to the *Brunel Asset Management Accord*, is NOT in itself a likely cause for concern?**

   (a) Failure to manage risk appropriately.

   (b) A change in the expected investment style.

   (c) Short-term underperformance.

   (d) Lack of understanding of reasons for underperformance.

2. **What behavioural step needs to be taken to reinforce the length of the client mandate in order for fund manager time horizons to lengthen to those sought by their clients?**

   (a) Clients assess investment performance *less* frequently and predictably.

   (b) Clients assess investment performance *more* frequently and unpredictably.

   (c) Clients raise questions about the ESG characteristics of each company newly purchased by a fund manager.

   (d) Clients raise questions about the ESG characteristics of each company that is sold by a fund manager.

3. **How might a fund manager demonstrate to clients that it is addressing the challenge of resourcing of stewardship activities?**

   (a) Detail the processes by which it prioritises engagements.

   (b) Set out how it is adding stewardship staff and building expertise among its fund managers.

   (c) Demonstrate its active participation in one or more formal collective engagement vehicles.

   (d) All of the above.

4. **Which of the following is NOT a typical way in which asset managers integrate ESG?**
    (a) Using ESG as a threshold requirement before investment can be considered.
    (b) Using ESG as a factor that informs the valuation.
    (c) Using ESG as a risk assessment that offers a level of confidence in the valuation.
    (d) Using ESG as a basis for explaining investment holdings to clients.

5. **Which of the following are expected to be reported by the Pensions and Lifetime Savings Association (PLSA) disclosure guide for public equities?**
    (a) ESG integration and stewardship.
    (b) Social impact and stakeholder engagement.
    (c) ESG risk and carbon footprint.
    (d) Social risk and board engagement.

6. **Which of the following is NOT one of McKinsey's proposed dimensions of investing for the purposes of applying sustainable investing practices?**
    (a) Investment beliefs and strategy.
    (b) Regulatory and policy environment.
    (c) Performance management.
    (d) Public reporting.

7. **Which of these forms of asset owner is most likely to apply an exclusion policy barring investment in all assets exposed to a particular business area?**
    (a) Defined benefit (DB) pension scheme.
    (b) General insurance business.
    (c) Charitable foundation.
    (d) Sovereign wealth fund.

8. **Why might a fund manager disagree with an external researcher's ESG analysis of a particular asset in its portfolio?**
    (a) The fund manager may have greater insight from its direct dialogue with the asset than is available in public disclosures on which the research is based.
    (b) The fund manager may believe that the asset has an active programme of improvement that is likely to be recognised in a different rating in due course.
    (c) Both a and b.
    (d) Neither a nor b.

9. What is the clearest risk from an asset owner leaving voting decision-making in the hands of its fund managers?

(a) Fund managers will fail to align the votes with their investment thesis.

(b) If a company is held by more than one fund manager, the asset owner's shares may be voted differently.

(c) Votes are more likely to be lost in the voting system.

(d) This reduces fund manager accountability for their decisions.

10. Which of the following is NOT a driver for clients to seek ESG investment, at least for one class of client?

(a) Fiduciary duty.

(b) Reputational risk.

(c) Personal ethics.

(d) A belief that social issues are unimportant.

11. Why might a client concentrate their attention on ESG outliers in their active monitoring and assessment of fund manager performance?

(a) Because companies with weak ESG performance will test how effective fund manager ESG integration is in practice.

(b) Because allowing the fund manager to choose which case studies are focused on in discussions may lead to less insight.

(c) Because the client can focus on ESG factors of most concern to them at a given time.

(d) All the above.

12. Which of the following is NOT a way of assessing whether a fund manager effectively integrates ESG factors, according to the PLSA?

(a) Examples of where and why the manager is prepared to take either stock or sector ESG risks or where it sees opportunities.

(b) How much financial return is directly attributable to ESG factors.

(c) Quantitative or qualitative examples of material ESG factors identified in fundamental analysis and stock valuation.

(d) Identification of long-term ESG secular trends and themes and the extent to which they have influenced portfolio construction decisions.

13. Which of the following is likely to be a primary ESG driver for a European defined benefit pension scheme?

(a) Reputational risk.

(b) Fiduciary duty.

(c) Personal ethics.

(d) Founding aims.

14. Which of the following investors will most likely have the lowest risk tolerance?

(a) Life insurer.

(b) Sovereign wealth fund.

(c) General insurer.

(d) Foundation.

15. Which two ESG specific areas of disclosure are requested by the International Corporate Governance Network (ICGN) *Model Mandate*?

(a) A breakdown of the return on investment for each stakeholder group and details of how each form of ESG risk type has been hedged by the portfolio manager.

(b) A materiality map identifying the ESG impact of all investments and a detailed disclosure of the voting record of all executive and non-executive directors.

(c) A detailed disclosure of stewardship engagement and voting activity must be made, and the manager's assessment of ESG risks must be embedded in the portfolio.

(d) A pro-rata environmental footprint of all investments must be estimated and the impact of all externalities from investments must be identified.

CHAPTER 9

SELF-ASSESSMENT **ANSWERS**

1. c.
2. a.
3. d.
4. d.
5. a.
6. b.
7. c.
8. c.
9. b.
10. d.
11. d.
12. b.
13. b.
14. c.
15. c.

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