

Pension Fund Coalition for Inclusive Capitalism

Model ESG Language in Public Equities Investment Contracts

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Introduction

The Pension Fund Coalition for Inclusive Capitalism, an initiative of the Ira M. Millstein Center for Global Markets and Corporate Ownership at Columbia Law School and the Coalition for Inclusive Capitalism, aims to bring together and empower pension funds that are committed to investing in sustainable businesses that will continue to provide long-term value for beneficiaries.

In service of this goal, the Pension Fund Coalition has collaborated with certain pension funds, legal advisors, and other advisors to generate the following customizable contract language establishing minimum environmental, social, and governance (ESG) guidelines that can be used as a baseline for negotiations with public equity investment managers.

In particular, the model ESG contract language provided below is intended to serve as a guide for structuring ESG provisions in investment agreements. While the model contract language strives to provide flexibility and a variety of options to fit a range of different priorities, focus areas and investment needs, it is not a one-size-fits-all provision and will require tailoring depending on the situation. Prior to determining an approach, business and legal teams should consider the following:

1. The model ESG contract language presents a range of approaches and language from which your organization can choose (ranging from restrictive approaches to middle-of-the-road approaches) under the following headings:

- A. ESG Mandate
- B. Proxy Language
- C. Reporting Requirements on a Regular Basis
- D. Additional Interim Reports

Each of these clauses is designed to be inserted into a broader agreement with an asset manager. This model ESG contract language is meant to apply to active asset managers in public equities, and not to passive index funds or private markets investments;¹ the Pension Fund Coalition has separately developed model ESG language intended for private investment fund agreements in closed-ended private equity style funds.

2. Prior to using the model ESG contract language, identify to what extent ESG language will be used by investment professionals (in diligence and monitoring) or counsel (in documentation) in pursuing ESG priorities, and consider the following:
 - a. What are your organization's ESG priorities, and what does ESG mean to your organization? For example, how does your organization prioritize each of the social, environmental or governance issues? Which issues are higher priorities? How does your organization integrate and assess each factor uniquely and as interrelated considerations? It is important to assess your organization's broader objectives and priorities (i.e., financial returns, diversification, geographic considerations) to appropriately tailor ESG provisions.
 - b. How do you intend to integrate and account for ESG factors in your investments? For example, is your organization primarily driven by profitability and integrates ESG considerations in the investment research process among the factors to consider from a risk-management or value creation perspective? Is your organization's strategy intended to focus on ESG themes in a way that seeks to achieve certain ESG outcomes? Clarify with the asset manager what their default assumption is, as their starting point may be different from yours. Your position on this question will inform your negotiation strategy and how highly to prioritize certain clauses in the model ESG contract language.
 - c. What is your organization's mission statement as it pertains to ESG, and how do you think about achieving that mission? For example, the mission that many asset owners have for ESG is to drive value creation, support the goal of achieving superior risk-

¹ While these contract provisions were not drafted for negotiations with fixed-income investment managers, an asset owner may consider reviewing the model contract provisions with its legal and business teams and advisors to determine which provisions, if any, may be useful in that context. In this scenario, the asset owner and its advisors would need to adjust the model provisions for the fixed-income context, keeping in mind that there are a host of debt-specific issues that the model provisions do not contemplate or take into account.

- adjusted returns, and mitigate financial risks in the portfolio and systemic risk in the markets. Asset owners can use a number of different strategies towards this mission, and will want to discuss with asset managers how to best incorporate those strategies into investment decisions. When negotiating ESG provisions in investment contracts, you should think about and work with asset managers on clarifying both the mission and end goals, as well as how to best make investment decisions to reach those goals.
- i. For example, at the portfolio company level, you may want the asset manager to (w) systematically incorporate diligence of the financial materiality of ESG factors; (x) affirmatively invest on behalf of the owner in ESG-aligned investments, (y) avoid or divest from non-ESG-aligned investments, and/or (z) allow investment in high-risk or high-potential companies, through which the manager may effect positive change on behalf of the owner through engagement and value creation.
 - ii. At both asset manager and portfolio company levels, consider adopting a standardized reporting template as an exhibit to the contract to assess compliance and achievement of ESG targets, and where appropriate include economic incentives based on ESG metrics. When negotiating ESG provisions in investment agreements, the parties should consider and clarify the mission, goals, appropriate metrics, performance indicators, and monitoring and reporting to measure progress on achieving those goals, as well as how to most effectively make investment decisions to reach those goals.
- d. How do you want the ESG provisions to fit within the context of the broader agreement,² including other key business/commercial terms, such as the asset manager compensation structure terms, a fiduciary obligation to maximize return on investment, or duration of the investment agreement (and any operative termination clauses), among others? To what extent are ESG considerations a policy requirement as compared to optional additional terms? While the negotiation of ESG provisions is not necessarily a zero sum game, as ESG provisions will be considered among the many business terms on the negotiating table, it will be helpful to consider that some asset managers may not agree to a robust ESG provision without some concession afforded elsewhere. Additionally, many asset owners currently do not yet have ESG provisions at all in their investment contracts with managers, and requesting new provisions will generally require discussion around “low-bar” versus “high-bar” requests, and what managers will need from owners to accommodate such requests (e.g., specific requests

² As an example, FCLTGlobal’s Model for Long-Term Contract Provisions provides an approach to consider ESG within broader investment agreements (available at https://www.fcltglobal.org/wp-content/uploads/Institutional-Investment-Mandates-Anchors-for-Long-term-Performance_FCLTGlobal.pdf#page=16).

- and reporting may result in more administrative burden, which could lead to additional fees as well as guidance required from your end to assist managers with meeting those expectations, while, alternatively, if you want a streamlined easy process, you may need to give managers more discretion and room for judgment calls that may not exactly match your own). As such, it is important to assess your organization's broader objectives and priorities so you can determine where you are willing to compromise, what is non-negotiable, and which versions of the model ESG contract provisions, if any, you propose.
- e. What are your organization's policies and procedures as they pertain to ESG when selecting asset managers? For example, consider whether the asset manager has (a) signed on to best practices, such as the United Nations-supported Principles for Responsible Investment ("UNPRI") or Operating Principles for Impact Management (the "Impact Principles"), (b) ESG policies and procedures in place, and/or (c) systems in place to monitor progress based on ESG targets (whether focused on diversity, reducing carbon footprint or other measures).
 - f. To what extent do your organization's ESG policies and procedures seek specific compliance or outcomes at the level of the asset manager and/or at the level of portfolio companies?³

Depending on your organization's specific circumstances and situation, the model ESG contract language may need significant revisions or adaptation. When negotiating and incorporating this model ESG contract language into your broader investment agreement, you should align with asset managers on, among other things, the definitions of ESG related terms, implementation and monitoring. Legal and business teams should collaborate in determining how or to what extent to use the model ESG contract language within the broader context of your investment agreements.

Finally, this model ESG contract language is general in nature, and should be tailored to the specific legal or business situation at hand. This introduction and the model contract language set forth in further detail below are not legal advice, and should not be considered or relied on as legal advice.

³ Securities regulators such as the SEC in the U.S. and the European Council (through the AIFMD) in Europe are increasingly focused on how asset managers disclose (and support the disclosure) of ESG strategies and performance. An owner will be looking to the same as to whether the asset manager's policies also support compliance with the contract provisions addressing ESG. A succinct summary of ESG disclosure rules and standards for the asset management industry, as of January 2022, is available at: <https://client.clearygottlieb.com/63/2279/uploads/2022-01-18-a-snapshot-of-global-sustainability-disclosure-rules-for-asset-managers.pdf>

Model Contract Language

A. ESG Mandate (clauses (a) and (b))

(a) Manager hereby acknowledges that:

Approach 1: Investors with individualized ESG investment policies/guidelines

Investor has informed Manager of its desire to invest in a responsible manner that takes into account [and prioritizes] Environmental, Social and Governance (“ESG”) criteria, and confirms that it is aware that Investor has endorsed a list of ESG criteria as set forth in Exhibit A attached hereto (the “ESG Policy”).⁴ Manager hereby acknowledges receipt of the ESG Policy and agrees that Manager will, and will ensure that any assignee or subcontractor will [consider] / [incorporate] / [comply with the guidance set forth in] the ESG Policy [into] / [in] its investment decision making processes. [Manager will, upon request of Investor on a quarterly basis, confirm that it has complied with this clause for the prior quarterly period preceding such request.]⁵ Investor may update the ESG Policy periodically, in connection with its internal policies and procedures, and will provide the Manager with such updates promptly. The Manager agrees to take such updates into account in connection with any future investments. In the event that Manager is not able to comply with the updated ESG Policy, Investor and Manager shall have good faith discussions and work to agree on a compromise.

Approach 2: Investors preferring to rely on standardized metrics, ratings, etc. or on Managers to recommend standardized metrics, ratings, etc.

Investor has [committed to the application of][is a signatory to] the [United Nations Principles of Responsible Investing (“UNPRI”)] / [UN Guiding Principles on Business and Human Rights (“UNPBHR”)] / [Task Force on Climate-related Financial Disclosures (“TCFD”) guidelines] / [International Sustainability Standards Board principles] / [The Value Reporting Foundation’s Integrated Thinking Principles, Integrated Reporting Framework and/or SASB Standards] /

⁴ Consider attaching Investor’s internal ESG policy / guiding principles as an Exhibit to the contract. Alternatively, Investor may list ESG factors that they want Manager to affirmatively consider through direct engagement (see Exhibit A-1), or include any specific industries or types of companies in which they are prohibited from investing (see Exhibit A-2 for example guidelines on investment restrictions), or a combination of both.

⁵ Please note that Manager may request to include some exemptions to this requirement, which is commonly seen in PE context, but not yet predominantly seen in public equities investment contracts. Such language may look like the following: “provided, however, that Manager shall not be obligated to act, or refrain from acting, in any manner that Manager believes, [in its sole discretion][in its reasonable discretion], is either (i) inconsistent with Manager’s other duties under the Contract, or (ii) inconsistent with its primary obligation to maximize the value of the holdings in Investment Account for the benefit of Investor.” (However, there is no need to offer up this language in the first instance. Ultimately, Investor should decide whether they want Manager to make the trade-off in monetary return, or simply want Manager to diligence ESG and apply the findings to their return-oriented investment process.)

[Global Reporting Initiative Sustainability Reporting Standards (“GRI”)] / [Science-Based Targets (“SBTs”)],⁶ and the Investor [is committed to] / [requires] the [application of]/[compliance with] these Environmental, Social and Governance (“ESG”) [criteria] / [metrics] / [standards] / [considerations] / [operations guidelines] / [disclosure frameworks] [with respect to investment managers] / [with respect to potential portfolio companies] to the management of its Investment Account⁷.

OR:

Investor has committed to investing in companies that [promote the United Nations Sustainable Development Goals (“UN SDGs”)] / [materially comply with or otherwise satisfy the requirements of [the ICMA green and/or social bond principles] / [[certain portions of] the European Commission’s ten-step action plan with respect to “green financial products”] / [receive a rating equal to or above [] as evaluated under [ISS’s E&S Score]] / [State Street’s R-Factor] / [MSCI’s ESG Rating] / [S&P’s Global ESG Score as calculated from their Corporate Sustainability Assessment] / [Sustainalytics ESG Risk Rating] / [Vigeo Eiris ESG Rating]⁸.

OR:

Investor has committed to investing in companies consistent with ESG criteria, metrics, standards, guidelines and other considerations (including, but not limited to, operational guidelines for managers and disclosure frameworks for portfolio companies) (altogether, “ESG Investment Criteria”). [Manager and Investor shall mutually agree on a list of ESG Investment Criteria, which Manager shall incorporate into its investment decisions.] / [Manager has provided a list of ESG Investment Criteria to Investor, which Investor has approved and which Manager shall incorporate into its investment decisions.] Such list [is] / [will be] attached hereto as Exhibit A and may be amended from time to time by Manager with advance notice and consent of Investor.⁹

⁶ These are just a few examples of standardized metrics, ratings and guidelines that may be included depending on each Investor’s individual preferences and priorities. As the standards are quickly evolving (with some standards changing, merging or disappearing), and as new laws and regulations (both in the US and abroad) come into effect or are being contemplated and impact the state of the market, please consider those standards that are most widely accepted as appropriate for the investment strategy, geography and sector as well as language to address successor frameworks.

⁷ As drafted, this provision assumes there is a designated “Investment Account,” but can be easily revised to apply to each individual investment or group of investments, as applicable.

⁸ These are just a few examples of ESG ratings systems that may be included depending on each Investor’s individual preferences and priorities.

⁹ This option may be helpful for Investors that do not already have internal ESG principles or frameworks and/or have sufficient resources to research and evaluate third party resources, and would prefer to rely on Manager to initially propose appropriate ESG criteria, metrics, standards, and guidelines for Investor.

(b) Manager agrees to, and will ensure any assignee or subcontractor will, comply with all applicable laws and regulations relating to sustainable investing, [consider] / [incorporate] / [uphold] / [comply with the guidance set forth in] the above [ESG Principles]/[ESG criteria] in its investment decision making processes, consistent with and in acknowledgement of Investor's [commitment to socially responsible investing]/[status as a signatory of the [UNPRI]/[Impact Principles]/[ESG Principles]], [as articulated in Investor's ESG investment beliefs and the *Guiding Principles* provided to the Manager, attached hereto as Exhibit A.]

B. Proxy Language (clause (c))

Approach 1: Investor Retains Voting Rights

(c) Manager will assist, as required, Investor in exercising the Voting Rights attached to any voting class securities in each Investment Account.¹⁰ [Within a [reasonable time] / [[] business days] following each annual meeting of stockholders [and any special meeting of stockholders] of any entity for which Investor holds voting class securities with attached Voting Rights, Manager shall furnish to Investor, in writing, [(i) a complete voting record reflecting all of the votes cast by Manager on behalf of Investor for each item of business voted on at such meeting [and (ii) a report on how Manager cast its discretionary votes at all of Investor's portfolio companies on behalf of other asset owners whose portfolios are managed by Manager]¹¹.]¹²

*Approach 2: Manager Votes According to Investor's Guidelines*¹³

(c) Manager shall exercise the Voting Rights attached to any voting class securities in each Investment Account in accordance with the voting guidelines [attached hereto as Annex []] / [provided in writing to Manager by Investor].¹⁴ [Within a [reasonable time] / [[] business days] following each annual meeting of stockholders [and any special meeting of stockholders] of any entity for which Investor holds voting class securities with attached Voting Rights, Manager shall furnish to Investor, in writing, a complete voting record reflecting all of the votes cast by

¹⁰ As drafted, this provision assumes that Investors are not registered stockholders and do not directly receive proxy cards from the portfolio companies.

¹¹ While the information in (ii) may be helpful data and benchmarking for investors, depending on the jurisdiction, asset managers may have no fiduciary duty to provide this to clients who retain their own voting rights and many managers may be reluctant to provide this information to investors in such scenarios.

¹² This provision contemplates a situation where Manager still votes on Investor's behalf (even though Investor is instructing Manager how to vote the shares). Since Investors are giving specific voting instructions to Manager under this approach, Investors may decide that such a report is not necessary, particularly if Managers would find it to be overly burdensome.

¹³ Where applicable, Investors may want to discuss the recommendations laid out in the UK Taskforce on Pension Scheme Voting Implementation (TPSVI) with Managers when negotiating proxy voting rights.

¹⁴ Investor should discuss with Manager the mechanics of how voting in accordance with Investor's guidelines will work, including, for example, particular voting guidelines on certain ESG proposals and whether any exceptions may be made.

Manager on behalf of Investor for each item of business voted on at such meeting [and, with respect to any ESG proposals voted on at any portfolio company of Investor, confirmation of whether Manager voted inconsistently with how Manager voted on behalf of Investor with respect to shares managed for other asset owners].

Approach 3: Manager Retains Voting Rights

(c) [Upon reasonable written request from Investor, Manager shall provide written notice to Investor describing [the anticipated voting decisions to be made by Manager] / [any anticipated voting decisions that deviate from [management’s recommendations] / [ISS’s, Glass Lewis’s or another identified proxy advisory firm’s recommendations] with respect to the voting class securities in each Investment Account. Should Investor[, taking into account Manager’s fiduciary duty,] believe that a specific proxy should be voted a particular way, Investor may, within [] business days of receipt of such notice, contact the Manager to discuss the Investor’s viewpoint and rationale, and, if Investor so chooses, make a request to change any voting decision. The Manager will retain the right to vote the proxy; however, in the event the Manager does not vote in accordance with Investor’s recommendation, it shall provide the Investor, in writing, an explanation of the rationale for Manager’s vote.] Within a [reasonable time] / [] business days] following each annual meeting of stockholders [and any special meeting of stockholders] of any entity for which Investor holds voting class securities with attached Voting Rights, Manager shall furnish to Investor, in writing, a complete voting record reflecting all of the votes cast by Manager on behalf of Investor [and, with respect to any ESG proposals voted on at any portfolio company of the Investor, confirmation of whether Manager voted inconsistently with how Manager voted on behalf of Investor with respect to shares managed for other asset owners].

C. Reporting Requirements on a Regular Basis (clause (d))

(d) Manager shall, within 45 days after the end of each calendar [year] / [each quarter], deliver a report [(“Annual Report”)] / [(“Quarterly Report”)] to Investor detailing Manager’s investment and management activity on behalf of Investor and compliance with [the ESG Investment Considerations] / [the ESG Policy] / [clause [(a)] of this Agreement]. Such report shall, at minimum, include discussion of [(i) Manager’s process of conducting research and diligence on and tracking ESG activities of portfolio companies, (ii) any stewardship activities conducted by Manager as part of their asset management activities,¹⁵ and (iii) material developments in ESG matters at portfolio companies in which Manager currently holds or has held a material position in the prior [calendar year] / [quarter] with respect to Investor’s

¹⁵ In the current landscape, Managers may push back on creating a reporting obligation for stewardship activities, and even if this clause is successfully negotiated into the contract, the response may range depending on the Manager.

Investment Account (“Material Portfolio Companies”),¹⁶ in each case in a format generally consistent with [(and no less detailed in any material respect than)] the form reporting template attached hereto as Exhibit B.¹⁷] [Manager shall promptly advise Investor in writing of any changes or planned changes to its research, diligence or tracking process involving ESG criteria.]

D. Additional Interim Reports on Material Adverse Developments¹⁸ (clause (e))

(e) [Upon Investor’s reasonable request] [subject to applicable legal, regulatory and confidentiality obligations]¹⁹ In addition to the Annual Report, Manager shall use [best] / [reasonable best] / [commercially reasonable] efforts to notify Investor in writing with additional interim updates on any material adverse developments relating to ESG matters in portfolio companies, as soon as practicable [after becoming aware of such developments] / in sufficient detail for Investor to understand the additional risks to its investment involved in such an adverse development, and provide updates on any corrective action that has been taken in respect thereof.

¹⁶ Investor and Manager should consider having a defined term for “material portfolio companies” based on what is reasonable and practical for that particular Manager’s investment time horizon and strategy, or to agree on a process for making this determination going forward.

¹⁷ Agreeing on a specific format of quarterly ESG report upfront will force Manager to be more thoughtful about tracking ESG performance and documenting material developments, which will help enhance the Manager’s accountability. This point may be carefully negotiated -- if reporting form is unrealistically detailed, Manager may find the obligations too burdensome and objectionable.

¹⁸ This interim reporting requirement should be carefully negotiated. In the current market climate, such a provision not yet widely adopted in existing public investment agreements, as opposed to the PE context, and Investors can expect that the asset manager will volunteer information on positive ESG developments without needing to agree to do so by contract.

¹⁹ Managers will likely ask for these qualifiers, but it is up to Investor whether to give these in the first instance or wait until Managers affirmatively ask in the course of the negotiations.

Exhibit A-1
Examples of ESG Factors

These examples are not meant to be used wholesale in contracts; rather, these are meant for discussion purposes and to present possible frameworks for building ESG investment guidelines. Specific ESG factors and considerations should be tailored to the priorities and focus of each investor. The factors and considerations set forth in these examples are not meant to be representative of items that any given manager may accept, and are not meant to be a comprehensive compendium of factors and considerations.

Sample Language #1

We believe that responsible corporate behavior with respect to environmental, social and governance (“ESG”) factors generally has a positive influence on long-term financial performance. As a long-term investor, we consider ESG factors in making investment decisions, with a particular emphasis on the below list of priorities. In analyzing the opportunities and risks inherent in any investment, we look to identify and mitigate ESG factors that are, or could become material to long-term financial performance. ESG opportunities and risks are monitored throughout the life of the investment.

- Prior to investment, Manager should perform an assessment of the ESG risks or opportunities of such investment, including due diligence of public disclosures, relevant company documents and any research materials from third party service providers, as well as direct engagement.
- We believe that active engagement is usually preferable to screening stocks or investments (beyond the investment restrictions set forth under the contract), a process by which certain companies or entire industries can be precluded from consideration for investment based on ESG factors. Divestment may be appropriate when exhaustive engagement has not resulted in satisfactory progress or risk mitigation.
- Manager should engage in a direct dialogue with companies to discuss concerns on ESG risks, in light of relative risk and size of holdings. All direct engagement activities should have a view towards the ultimate benefit to the value of our holdings. Our preference is to conduct direct engagements privately.
- Proxy voting is an important component of our public equity engagement process. We have adopted Proxy Voting Guidelines addressing the areas of corporate governance in which we may be requested to vote from time to time and the principles on which we will rely, at least

initially, in determining a response to such requests. Our Proxy Voting Guidelines are available at [\[website address\]](#).

We expect companies in which we invest, directly and indirectly, to not only comply with all applicable legal and regulatory regimes, but also use [reasonable best efforts / commercially reasonable efforts to] adhere to international best practices (including [UN Principles of Responsible Investing (“UNPRI”)] / [UN Guiding Principles on Business and Human Rights (“UNPBHR”)] / [Task Force on Climate-related Financial Disclosures (“TCFD”)] / [International Sustainability Standards Board Principles] / [The Value Reporting Foundation’s Integrated Thinking Principles, Integrated Reporting Framework and/or SASB Standards²⁰ / [Global Reporting Initiative Sustainability Reporting Standards (“GRI”)] / [Science Based Targets (“SBTs”)]²¹) while implementing ESG policies.

Sample Language #2

As a long-term investor, we proactively address and consider ESG factors as part of our investment strategy. In particular, we focus on²²:

- Biodiversity
- Board quality and composition
- Climate change
- Community engagement
- Conduct, culture and ethics
- Diversity, equity and inclusion
- Social justice, including but not limited to [social, economic, racial, gender, sexual orientation, gender identity, access and other forms of inequality]²³
- Executive compensation
- Health & safety
- Human capital management
- Natural resource efficiency
- Pollution & waste reduction

²⁰ NOTE: Based on timing of publication, to be updated (along with CDSB) based on the new International Sustainability Standards Board process

²¹ These are just a few examples of standardized metrics, ratings and guidelines that may be included depending on each Investor’s individual preferences and priorities, and may need to be updated in line with future developments.

²² Investor should discuss with Manager how exactly Investor wants Manager to “focus on” any ESG factor set forth by Investor. For example, a focus on the diversity piece of diversity, equity and inclusion could relate to multiple aspects of diversity, including but not limited to gender identity, race, ethnicity, age, national origin, orientation, cultural identity and physical ability, and the target could be the board, management and/or the broader employee base. Investor should make sure Manager is aligned on Investor’s priorities and focus areas.

²³ These are examples that may be included, but Investor can tailor this list as appropriate.

- Product safety
- Risk management, including cybersecurity and data privacy risks
- Shareholder protections and rights
- Supply chain risks
- [...]

[In making decisions with regards to investments, Managers should perform an ESG assessment based on (but not limited to) the above factors, including due diligence of relevant company documents, public disclosures and any research materials from third party service providers, and an evaluation of the ESG risks and opportunities any potential company presents that may impact long-term value. We expect any companies considered to not only comply with all applicable legal and regulatory regimes, but also adhere to international best practices (including [UN Principles of Responsible Investing (“UNPRI”)] / [UN Guiding Principles on Business and Human Rights (“UNPBHR”)] / [Task Force on Climate-related Financial Disclosures (“TCFD”)] / [International Sustainability Standards Board Principles] / [The Value Reporting Foundation’s Integrated Thinking Principles, Integrated Reporting Framework and/or SASB Standards] / [Global Reporting Initiative Sustainability Reporting Standards (“GRI”)] / [Science Based Targets (“SBTs”)]²⁴) while implementing ESG policies.]²⁵

Sample Language #3

Further to considering ESG factors and consistent with Investor’s policies regarding diversity, equity and inclusion, the Manager agrees to consider:

- creating a (or reviewing its existing) diversity, equity and inclusion policy with an eye toward (a) ensuring the structures and practices of the Manager create conditions that promote full inclusion of racially and ethnically diverse groups, other underrepresented groups such as the LGBTQ+ community, and women throughout all facets of the Manager and portfolio company, and (b) designing ways to measure the policy’s effectiveness and impact. Such policy would also provide a framework to assess, acknowledge and remove any possible elements that would impede progress toward a fully diverse and inclusive organization;
- including as part of such diversity, equity and inclusion policy, broader hiring, nurturing and retention efforts, to increase the participation of racially and ethnically diverse

²⁴ These are just a few examples of standardized metrics, ratings and guidelines that may be included depending on each Investor’s individual preferences and priorities (for example, Manager to favor companies that follow SASB or GRI criteria in their disclosures and to negatively weigh companies that do not).

²⁵ Investors should specify how the investor thinks about the list of topics and how a manager should incorporate them into investment decision considerations.

groups, other underrepresented groups such as the LGBTQ+ community, and women throughout the Manager's organizational ecosystem, including (as relevant and consistent with the Manager's fiduciary duties to the investment funds it manages, if any), its management teams, investment staff, portfolio company boards, portfolio company management teams, consultants, advisors and professional service providers. Hiring initiatives might include, among other things, engaging in non-traditional recruitment efforts, such as including Historically Black Colleges and Universities to the roster of targeted under-graduate and graduate institutions as well as sponsoring internships and/or partnering with development programs targeting racially and ethnically diverse groups, other underrepresented groups such as the LGBTQ+ community, and women to access and cultivate an internal talent pool; and/or

- completing, on a voluntary basis, information regarding the foregoing when providing Investor's [{"Annual"}] / [{"Quarterly"}] Reports, to the extent not otherwise legally required.

Exhibit A-2
Examples of Investment Restrictions²⁶

*This sample language and examples of Prohibited Investments are not meant to be used wholesale in contracts; rather, these are meant for discussion purposes and to present possible frameworks for building ESG investment guidelines. Some investors may have policies that will require these restrictions for the fund as a whole and therefore the restrictions are gating considerations. The guidelines, restrictions and descriptions set forth in these examples should be tailored to the priorities and focus of each investor, are not meant to be representative of items that any given manager may accept, and are not meant to be a comprehensive compendium of factors and considerations.*²⁷

The Manager acknowledges that the Investor is subject to investment policies (the “Policies”) precluding its participation in any investment in (a) [____], (b) [____], and (c) [____] (the “Prohibited Investments”). Accordingly, as required by each of the Policies, the Investor shall be excluded from Prohibited Investments and therefore shall not have to contribute to the Manager capital (including expense contributions) in respect of a Prohibited Investment or any follow-on investment thereto. The Investor shall have the right to ask questions and receive additional information about any proposed investment as may be reasonably necessary for it to independently determine whether a proposed investment is a Prohibited Investment.

Example “Prohibited Investments” (broader guidelines):

Managers should not invest in the following:

- companies whose principal field of activity is the production of cluster munitions, biological weapons or chemical weapons
- companies whose principal field of activity is the production of nuclear weapons (excluding companies that are only engaged in transactions with countries that are approved by the United Nations for the purpose of holding and maintaining existing nuclear weapons)
- any company engaged in a transaction violating the Treaty on the Non-Proliferation of Nuclear Weapons

²⁶ Investors to consider the balance of adhering to principles by not investing in certain stocks (such as these investment restrictions) versus investing in stocks to create change. Investors should consider the headline risk of investing in certain industries, as well as opportunities presented by active ownership to encourage greater engagement on best-efforts basis with companies that adhere to good disclosures or practices. Investors should also consider the advantages and disadvantages of exclusion consistent with fiduciary duty, which may involve factors such as eliminating uncompensated risk, impact on long-term value creation and relative benefits of engagement.

²⁷ For other investment restrictions, note that the International Finance Corporation also maintains Exclusion Lists defining the types of projects the IFC does not finance at https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/company-resources/ifcexclusionlist.

- any securities categorized as tobacco under code 302030 of the Global Industry Classification Standard
- companies operating casinos and other types of gaming/gambling operations including online gambling/gaming
- companies operating in the Adult Entertainment sector
- companies that perform animal testing
- companies that manufacture, sell, purchase or use weapons, platforms for weaponry or material parts of a weapon or platform for weaponry
- companies that derive [material] / [substantial] revenue²⁸ from the operation of privatized incarceration facilities

Example “Prohibited Investments” (more detailed guidelines):

Managers should not invest in companies in the following industries and sectors:

- **Chemicals**

Companies that [directly or indirectly]²⁹ manufacture:

- (a) Chemical weapons.
- (b) Chemicals prohibited in Annex A of the Stockholm Convention, an international agreement on persistent organic pollutants (POPs) which create severe health impacts, such as cancer.
- (c) Chemicals which are inconsistent with Annex III of the Rotterdam Convention, an international agreement on hazardous pesticides and industrial chemicals.

- **Fossil Fuel-related Energy**

Companies that [directly or indirectly] support:

- (a) Specific operations or projects in UNESCO World Heritage Sites or wetlands listed by the Ramsar Convention on Wetlands.
- (b) New coal-fired power plants, including expansions, where individual units have a gross generating capacity of 500MW or more, and:
 - (i) carbon intensity exceeds 850g CO₂/kWh; or
 - (ii) the plant is in a developed country and its carbon intensity exceeds 550g CO₂/kWh. With existing technologies, this may effectively prohibit new coal-fired power plants without acceptable CCS plans or without material benefits from either combined heat and power (CHP) or biomass.

²⁸ Investors should consider defining the threshold of [“material revenue”] / [“substantial revenue”] to avoid ambiguity and, to the extent possible, provide a numerical threshold so that there is no guesswork involved for the Manager and the request is easier to execute.

²⁹ This optional language contemplates scenarios where the public parent company directly engages in the activity, as opposed to scenarios where the public company’s affiliate or subsidiary engages in the activity (or has significant business relationships with third parties (e.g., contractors, service providers, vendors, etc.) that engage in the activity. Investor may omit the “indirectly or indirectly” phrase as a whole.

- **Forestry**

Companies that [directly or indirectly] support:

- (a) Illegal logging and the subsequent trading of related timber and forest products.
- (b) Operations in UNESCO World Heritage Sites.
- (c) Operations in wetlands listed by the Ramsar Convention on Wetlands.

These prohibitions apply both to companies that log for commercial or development purposes and to companies that purchase, trade or process timber from these sources.

- **Mining & Metals**

Companies that [directly or indirectly] support:

- (a) Operations in UNESCO World Heritage Sites, unless those specific operations predated the World Heritage Site designation.
- (b) The mining, processing and/or sale of uranium for weapons purposes.
- (c) The mining or trading of rough diamonds not certified under the Kimberley Process. This scheme provides assurance that diamonds have not been used to finance wars against legitimate governments, historically a particular problem in Africa through “conflict diamonds”.
- (d) Artisanal mining – i.e. individuals mining with simple tools, usually without any form of regulation.

[For the avoidance of doubt, indirect support includes (but is not limited to), investments such as general purpose investments, where the use of proceeds is known and materially supports prohibited activities.]