

SUBJECT	INCREASE IN UBC CONTRIBUTION TO SUSTAINABLE FUTURE POOL
MEETING DATE	APRIL 18, 2019

Forwarded on the Recommendation of the President

**APPROVED FOR
SUBMISSION**



for Santa J. Ono, President and Vice-Chancellor

DECISION REQUESTED	<p>IT IS HEREBY REQUESTED that approval be granted for:</p> <ul style="list-style-type: none"> <i>i. an increase of UBC’s commitment to the Trek Impact Endowment Fund, held within the Sustainable Future Pool, from \$25 million to \$50 million over the next three fiscal years effective April 1, 2019, provided that the performance of the Sustainable Future Pool (SFP) is not materially adverse as compared to that of the Main Endowment Pool (MEP);</i> <i>ii. the following schedule of UBC contributions to the Trek Impact Endowment Fund, provided that the performance of the SFP is not materially adverse as compared to that of the MEP: \$15 million in FY19-20; \$10 million in FY20-21; and, \$10 million in FY21-22; and;</i> <i>iii. FURTHER, that the Administration be directed to evaluate the near-term effects of these increases as part of the comprehensive review of the SFP to be undertaken prior to the end of FY20-21.</i>
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Report Date	February 20, 2019
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Presented By Peter Smalles, Vice-President Finance & Administration
 Rajiv Silgado, President & Chief Executive Officer UBC IMANT
 Tor Album, Acting Treasurer

EXECUTIVE SUMMARY

The UBC Board of Governors approved the creation of the Sustainable Future Pool (“SFP”) in February 2017 with an initial contribution of \$10 million from the Trek endowment to establish the Trek Impact Endowment Fund in the SFP. The Board of Governors also committed to contributing an additional \$5 million per year for three years to the Trek Impact Endowment Fund provided that the performance of the SFP is not materially adverse as compared to the Main Endowment Pool (“MEP”). The first of these \$5 million contributions was approved by the Board of Governors in April 2018, bringing the total UBC contributions to date of \$15 million.

Establishing the SFP is an important part of UBC’s commitment to sustainability. The SFP pursues sustainability concepts beyond the progressive strategies already being incorporated in the MEP and has reduced or no fossil fuel investments (currently it has none) and targets lower carbon emissions.

The establishment of the SFP brings together UBC’s mandate of inquiry and the creation of knowledge, UBC’s desire to lead from within, its academic experience, research expertise, and operations management to make the university a living lab - and to use what UBC learns to benefit its communities.

SUSTAINABLE FUTURE POOL – INCREASE IN CONTRIBUTIONS TO TREK IMPACT ENDOWMENT FUND

The SFP has so far seen limited interest from external donors, with only two external donors to date in addition to UBC’s contributions to the Trek Impact Endowment Fund. Development and Alumni Engagement (“DAE”) anticipates that the SFP will continue to grow, however growth may be modest and it will take time.

Key reasons include that the business cycle of establishing a new endowment fund – from initial discussions with the prospective donor to the fund being approved by BOG and established – is often two plus years (the SFP was established only two years ago), and many of the contributions made to endowment funds in a given fiscal year are pledge payments or renewed gifts to pre-existing endowment funds. It will take time to develop repeat and recurring donation histories with new funds.

In February 2019 the Board of Governors approved an increase in the spend rate for donor contributions to 3.75% by lowering the administrative charge for existing and future donor contributions to 0.40%. The main argument for implementing this change is to evaluate whether it will increase the attractiveness of the SFP to potential donors. It was further recommended that a comprehensive review was undertaken prior to the end of FY21.

Another potential way to further increase the attractiveness of the SFP would be for UBC to increase its contributions to the Trek Impact Endowment Fund. UBC is currently committed to investing a total of \$25 million, with \$15 million invested to date. Increasing the SFP ahead of external donors would show a strong commitment, not only to the SFP as a viable endowment pool, but also further enhance and solidify UBC’s commitment to sustainability. A larger endowment pool may also be perceived as more stable by potential donors and may increase donor interest going forward.

It is therefore recommended that UBC’s contributions to the Trek Impact Endowment Fund, for investment in the SFP, are increased going forward, over a three year period, provided that the performance of the SFP is not materially adverse **as compared** to the Main Endowment Pool, monitored by IMANT and reported to the Board of Governors Finance Committee.

The recommended additional contributions to the Trek Impact Endowment Fund are:

- FY19/20: \$15 million
- FY20/21: \$10 million
- FY21/22: \$10 million

These increases represent a 100% increase from the initial commitment made by the Board of Governors (from \$25 million to \$50 million) and would extend the remaining contribution period from 2 to 3 years. It is further recommended that the near term effects of these increases are evaluated as part of the comprehensive review of the SFP to be undertaken prior to the end of FY21.

The existing SFP program is implemented by Jaroslowsky Fraser and the proposed additional contributions can easily be accommodated within the current program without any negative impacts on the expected long-term returns of the portfolio. However, the SFP pool will need to grow to approx. \$100 million before a more diversified portfolio, with similar risk and return characteristics to the Main Endowment Pool, can be implemented.

The funding source for these additional contributions would be the same as for the initial contributions; an internal allocation of Trek Funds currently in the Working Capital Fund, specifically the “unspent” land lease proceeds from the Student Housing Financing Endowment (SHFE).

STRATEGIC CORE AREAS SUPPORTED

- ✓ People and Places ✓ Research Excellence ✓ Transformative Learning ✓ Local / Global Engagement
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**DESCRIPTION &
RATIONALE****Background**

UBC is committed to sustainability in endowment investments. In 2013, UBC adopted its Responsible Investment Policy to direct UBC to consider environmental, social and governance (“ESG”) factors to make more informed investment decisions for the UBC Endowment. Such ESG factors have now become an integral part of the manager selection process for the Main Endowment Pool (“MEP”).

The Sustainable Future Pool (“SFP”) was established in part as a result of a discussion about divestment of fossil fuels in by students and faculty in 2015. The University received legal advice that divestment of the MEP from fossil fuels was inconsistent with UBC’s fiduciary responsibilities.

Establishing the SFP is an important part of UBC’s commitment to sustainability. The SFP pursues sustainability concepts beyond the progressive strategies already being incorporated in the Main Endowment Pool and has reduced or no fossil fuel investments (currently it has none) and target lower carbon emissions.

It brings together UBC’s mandate of inquiry and the creation of knowledge, UBC’s desire to lead from within, its academic experience, research expertise, and operations management to make the University a living lab - and to use what UBC learns to benefit its communities.

The UBC Board of Governors approved the establishment of the SFP at the February 2016 meeting, the SFP Statement of Investment Policies & Procedures at the September 2016 meeting, and a \$10 million contribution from the Trek endowment to create the Trek Impact Endowment Fund in the SFP in February 2017.

The Board of Governors also committed to contributing an additional \$5 million per year for three years to the Trek Impact Endowment Fund provided that the performance of the SFP is not materially adverse as compared to the MEP. The first of these \$5 million contributions was approved by the Board of Governors in April 2018.

In February 2019 the Board of Governors approved an increase in the spend rate for donor contributions to 3.75% by lowering the administrative charge for existing and future donor contributions to 0.40%. The Board also approved that the spend rate of 3.5% and the corresponding administrative charge of 0.65% are to be retained for UBC’s contributions to the SFP. The main reason for implementing this change is to evaluate if it will increase the attractiveness of the SFP to potential donors.

Legal considerations

The main difference between the MEP and the SFP is that the MEP must be invested strictly in the best interests of charitable purpose trusts, which is their financial interests, and the SFP must be invested in the best interests of the university, which may take some broader criteria into account. The SFP is comprised of the university’s own monies and also donor monies where the donors have specifically agreed to the investment SFP criteria.

When exercising its fiduciary responsibilities for the SFP, the University has determined that the non-financial criteria of carbon emissions is in the best interest of UBC for the following reasons:

- UBC is a place of research and will be using SFP as part of its living lab to see if a higher level of sustainability can be incorporated into its investment processes in a prudent manner;
- UBC has a long-term focus and sustainability is a core value;
- the SFP is in a separate pool so that UBC can track its results clearly;
- the SFP opens up an investment choice to donors; and
- it provides reputational impacts to UBC amongst its students, faculty, and donors.

Given the experimental nature of the SFP and UBC's fiduciary responsibilities, UBC must maintain the ability to adjust the investment profile of the SFP. This includes the potential to transfer SFP funds to another Endowment Pool at UBC and/or discontinue the SFP if the BOG determines that it is in the best interest of UBC.

The advice from legal counsel is donor funds can be added to the SFP only where they specifically agree that their gifts will be invested in the best interests of UBC and in a manner that takes non-financial considerations into account.

Development and Alumni Engagement Considerations

Development and Alumni Engagement ("DAE") will continue to expand awareness of the SFP to the UBC frontline fundraisers and academic partners to ensure that donors making a gift to establish a new endowment are provided the SFP as an option.

DAE anticipates that the SFP will continue to grow, however it will likely be modest growth and it will take time for the following reasons:

- Major gifts are made when a donor's passion intersects with a University priority. When donors contemplate the SFP, they must accept that UBC will be taking both financial and non-financial considerations into account when UBC invests their gift, which means UBC will be considering interests other than the best interest of their passion when UBC invests their gift.
- Many donors to endowments have previously given to other UBC endowments in the Main Endowment Pool and are satisfied with the ESG principles applied to their past gifts. UBC must ensure that our past donors are proud and fulfilled by their decision to donate to the endowment that is invested in the best interest of their charitable purpose, which includes only financial considerations.
- The business cycle of establishing a new endowment – from initial discussions with the prospective donor to the fund being approved by BOG and established – is often 2 plus years, many of the endowments recently established pre-date the inception of the SFP.
- Many of the contributions made to endowment funds in a given fiscal year are pledge payments or renewed gifts to pre-existing endowment funds, it will take time to develop repeat and recurring donation histories with new funds.

UBC Investment Management Trust (IMANT) Considerations

The SFP targets an asset mix of 70% global equities and 30% Canadian bonds, with an option to include green bonds. The SFP is invested in two pooled fund vehicles with a single manager, Jaroslowsky Fraser. Both funds (equities and bonds) have materially lower carbon dioxide emissions than the established benchmark resulting from the fossil fuel exclusions and emphasis on CO2 emissions reductions by portfolio companies.

If the SFP were to grow to it may be possible to improve fund diversification. However, IMANT cautions that with a portfolio size of only \$50 million, the ability to diversify the portfolio without incurring higher transaction costs that would nullify those improvements is only marginal.

IMANT recently carried out a high level review of a hypothetical, more diversified portfolio that expands to less correlated assets like mortgages, infrastructure debt, real estate and absolute return strategies. With those asset classes the SFP portfolio would benefit from improved diversification through lower volatility. Taking the analysis further, by diversifying global equities to emerging markets and small cap stocks the SFP portfolio may benefit from improvements in expected returns as well.

Based on the asset classes considered and minimum investment requirements typically in place, IMANT's expectation is that a \$100 million SFP portfolio can be invested so as to display risk and return characteristics that are similar to the Main Endowment Pool (MEP). During 2019, IMANT will review the SFP program and product developments in the marketplace in the last two years since the implementation of the SFP and the initial selection of manager.

The additional contributions as recommended can easily be accommodated within the current pooled funds at Jaroslowsky Fraser without any negative impacts on the expected long-term returns of the portfolio.

Performance

The current market value of the SFP is just over \$15 million. The largest endowment fund is the UBC Trek Impact Endowment Fund, which represents the \$15 million contributions to date from UBC. At present there are only two external endowment funds (donors) which collectively represent 0.76% of the Pool.

Preliminary return estimates to the end of 2018 suggest that, despite its limitations, the SFP has delivered strong relative performance versus its benchmark of 70/30 global equities and Canadian bonds and returns comparable to the MEP.

Since inception the fund has outperformed its policy benchmark by 148 basis points gaining 5% vs. 3.5% for the benchmark. In calendar 2018, the SFP outperformed its benchmark by 195 basis points delivering 2.2% versus 0.2%.

The performance to date for the SFP is not materially adverse *as compared* to the Main Endowment Pool and therefore supports additional contributions to the Trek Impact Endowment Fund.

Recommendation

One way to further increase the attractiveness of the SFP would be for UBC to increase its contributions to the Trek Impact Endowment Fund. UBC is currently committed to investing a total of \$25 million, with \$15 million invested to date. Increasing the SFP ahead of external donors would show a strong commitment, not only to the SFP as a viable endowment pool, but also further enhance and solidify UBC’s commitment to sustainability. A larger endowment pool may also be perceived as more stable by potential donors and may increase donor interest going forward.

Although it may be too early to draw conclusions based on the discussion above, it is generally believed in the fund management industry that a larger pool is perceived as more stable and therefore more attractive than a smaller pool to investors. The performance of the SFP has not been materially adverse *as compared* to the MEP, which is also supportive of additional contributions.

It is therefore recommended that UBC’s contributions to the Trek Impact Endowment Fund, for investment in the SFP, are increased going forward, over a three year period, provided that the performance of the SFP continues to be not materially adverse *as compared* to the Main Endowment Pool, monitored by IMANT and reported to the Board of Governors Finance Committee.

The suggested additional contributions to the Trek Impact Endowment Fund are:

- FY19/20: \$15 million
- FY20/21: \$10 million
- FY21/22: \$10 million

These increases represent a 100% increase from the initial commitment made by the Board of Governors (from \$25 million to \$50 million) and extends the remaining contribution period from two to three years.

It is further recommended that the near term effects of these increases are evaluated as part of the comprehensive review of the SFP to be undertaken prior to the end of FY21.

<p>BENEFITS Learning, Research, Financial, Sustainability & Reputational</p>	<p>The SFP is an important part of the University’s commitment to sustainability and brings together the University’s mandate of inquiry and the creation of knowledge, its desire to lead from within, its academic experience, research expertise, and operations management to make the University a living lab.</p>
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<p>RISKS Financial, Operational & Reputational</p>	<p>The size of the SFP impacts the ability to diversify investments and leads to greater exposure to equity markets. This may lead to greater volatility of returns, as compared to a larger, more diversified pool.</p>
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The long-term asset class assumptions employed in 2017’s Staff Pension Plan asset mix review (the most current available to IMANT without undertaking an expensive full review) suggested that the 70/30 benchmark portfolio in the SFP is now expected to grow by only 5.5% annually, which is below previous expectations and below the current required return of 6.15%.

FINANCIAL Funding Sources, Impact on Liquidity	<p>The funding source for the contributions to the Trek Impact Endowment Fund in the SFP come from internal allocations of Trek Funds, specifically the “unspent” portion of endowed land lease proceeds from the Student Housing Financing Endowment (“SHFE”), currently held in the Working Capital Fund.</p> <p>There is sufficient liquidity to support the increased contributions as recommended.</p>
SCHEDULE Implementation Timeline	<p>The recommended changes would take effect from April 1st, 2019 (Fiscal Year 2020).</p>
CONSULTATION Relevant Units, Internal & External Constituencies	<p>UBC IMANT Treasury Office of the University Counsel Development and Alumni Engagement</p>

Previous Report Date	February 12, 2019
Decision	<ul style="list-style-type: none"> i) for donor contributions to the SFP, an increase in the spend rate to 3.75%, by reducing the administrative charge to 0.40%, for a period to two years effective April 1st, 2019, ii) ii) for UBC contributions to the Sustainable Future Pool, retention of the spend rate and administrative charge at 3.5% and 0.65% respectively, and iii) that the spend rate for the Sustainable Future Pool be reviewed annually, including, a comprehensive review by or March 31, 2021.
Action / Follow Up	
Previous Report Date	April 19, 2018
Decision	<p>Approval of an additional transfer of \$5 million to the Sustainable Future Pool and retain the spend rate at 3.5%.</p>
Action / Follow Up	
Previous Report Date	April 13, 2017
Decision	<p>Amendment to Policy #113, Endowment Management related to the establishment of the SFP.</p>
Action / Follow Up	
Previous Report Date	February 14, 2017
Decision	<p>Agreement to establish the SFP with \$10 million internal Trek funds and approval of the SFP Statement of Investment Policies and Procedures.</p>
Action / Follow Up	