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responsible investment policy

Prepared by

Investment Management

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Trustee of Health Employees Superannuation Trust Australia (HESTA) ABN 64 971 749 321

Contents

1. Purpose and objectives of the Policy

This Responsible Investment Policy (‘**the Policy**’) sets out the approach taken by HESTA to Responsible Investment (‘**RI**’) and how we ensure that environmental, social and governance (“**ESG**”) risks and opportunities are adequately considered and managed. The Policy outlines the guiding principles for the role of H.E.S.T. Australia Limited (‘**the Trustee**’ or ‘**HESTA**’) in using our investment activities to create a better future for our members through supporting a healthy economy, environment and society.

The Policy supports the Trustee’s Risk Management Framework and is a component of the Fund’s Investment Governance Framework.

2. Governing legislation and regulatory requirements

In constructing this Policy, the Trustee has considered its duty to comply with the ‘sole purpose test’ set out in the *Superannuation Industry (Supervision) Act 1993* (‘**SIS Act**’). The sole purpose test Section 52 requires HESTA to:

Act in the best financial interests of its members;

Invest members’ retirement income in a way that considers the level of risk taken on when investing a member’s contributions, and the return generated by how HESTA is investing the contributions.

In addition to the requirements set out in the SIS Act, HESTA also notes the Australian Prudential Regulation Authority’s (‘**APRA**’) approach to non-financial risks, including climate change risks, and considers these when executing the Policy.

3. Roles and responsibilities

Investment Committee – responsible for overseeing the Trustee’s investment strategy and frameworks, and ensuring proper governance of the Fund’s investment practices. In doing so, the Committee annually approves the Policy, and oversees the implementation and monitoring of the Policy.

Impact Committee – provides guidance to the Investment Committee on the Policy.

Trustee Office/Executive – accountability for implementation of the Policy sits with the Chief Investment Officer; responsibility for implementation of the Policy sits with the Investment General Managers, alongside the Head of Impact.

The Investment team is responsible for the operational requirements of the Policy.

Trustee Office/Risk Team and Compliance Team – the teams are responsible for maintaining the online Risk and Compliance tool (HESTAControl) which incorporates the requirements of this Policy to ensure that relevant controls and measures are monitored. The teams are also responsible for monitoring any reported incidents to ensure that appropriate action plans are established and responsibilities allocated to remediate any identified incidents.

Internal Audit – this function is responsible for evaluating the adequacy and effectiveness of the financial and risk management framework of the Trustee.

External Audit – approved auditors are engaged each year to undertake an annual audit of the Fund's financial statements and the annual information required under reporting standards made by APRA.

4. Definitions

Long-term investor: refers to an investor with an investment horizon that considers opportunities in terms of decades rather than months or years.

Universal owner: refers to an investor with a large investment portfolio diversified across asset classes, sectors and geographies such that they are effectively invested in a slice of the global economy. As such, they cannot diversify away all risk and are therefore affected by the health of the global economy.

Stewardship or active ownership: refers to the means by which investors most directly influence companies, markets, and economies; and, in turn, society and the environment as a whole.

5. Responsible investment overview

At HESTA, we aim to make a real difference to the financial future of every member. Our responsible investment practices are a crucial part of this purpose as reflected in one of our investment beliefs:

"HESTA will be a responsible investor and recognises that members' best interests are served by supporting a healthy economy, environment and society."

HESTA acknowledges that as a 'universal owner' we are exposed to the externalities associated with individual portfolio companies. Therefore, to deliver strong financial returns for our members' financial futures, we must address financial and non-financial considerations and advocate for necessary changes to the financial system. We have a fiduciary duty to act in the best long-term interests of our members, and acknowledge that ESG issues can affect the performance of our investment portfolios.

Our approach to RI can be summarised into five key areas, which are explored in more detail in this policy:

1. RI Integration in the investment process
2. deep impact investments
3. active ownership
4. advocacy and leadership
5. transparency and reporting.

As a universal owner, we endorse the ambitions of the United Nations' Sustainable Development Goals ('**SDGs**') at a global level as a way of delivering a healthy economy, environment and society. These 17 goals, adopted by all United Nations Member States in 2015, provide a roadmap for prosperity for the planet through global collaboration. We aim to support our members and their working lives in the health and community services sector (‘**HACS**’) by meaningfully contributing towards seven strategic areas of impact (framed within the SDGs), that are aligned with the Fund’s strategy and members’ interests. HESTA priority areas of impact are as follows:

SDG 3: Good health and wellbeing

SDG 5: Gender equality

SDG 6: Clean water and sanitation

SDG 7: Affordable and clean energy

SDG 8: Decent work and economic growth

SDG 11: Sustainable cities and communities

SDG 13: Climate Action

Our RI practices are also guided by our signature and commitment to:

The United Nations-backed Principles for Responsible Investment (‘**PRI**’) (link)

The Australian Asset Owner Stewardship Code (‘**Stewardship Code**’) (link).

HESTA is recognised as an industry leader in responsible investment. In 2019, we were proud to be named as a global leader by the UN PRI in its inaugural Leaders Group. This group consists of 47 global asset owners at the forefront of responsible investment leadership and innovation.

6. RI integration in the investment process

ESG framework

HESTA recognises that ESG factors can have an impact on portfolio returns – both positive and negative.

Consideration of these factors enables a better understanding of risks and opportunities, and therefore optimal capital allocation, particularly over the long term. We can use this information to make changes at the portfolio level to manage systemic risks or benefit from trends that will arise over time. Companies that actively seek to improve their ESG practices can produce enhanced risk-adjusted returns. As such, integrating ESG issues into investment analysis, decision-making processes and ownership practices contributes to investment success.

Examples of the type of ESG factors we consider are:

Environmental factors

- Environmental degradation: can impact quality and availability of resources like water and land, cause reputational damage, introduce potential liabilities and increase the cost of doing business.
- Climate change: and its potential transition risk, physical asset risk and/or liability risks[1].

[1] Refer to Appendix A for further detail regarding Climate Change

Social factors

- Engaged and healthy workforce: companies that consider their employees' needs and invest in their workforce are less prone to disruptions, liability and more likely to be innovative, which enhances long-term value.
- Community expectations: consideration of current and future community expectations when assessing a business model's ability to create value in the long term.
- Healthy supply chains: high visibility into supply chains and ensuring fair labour practices helps manage and avoid disruption in operations.
- Just transitions: social factors can be exacerbated by abrupt transitions, where an industry is no longer viable due to environmental reasons or broader societal expectations. Consideration of the economic effects of these transitions is important.

Governance factors

- Board independence: boards without conflicting interests help ensure alignment of interests with long-term investors.
- Remuneration: adequate incentives for board and executives that align interests with long-term investors.
- Transparency: adequate disclosure on material issues including environmental and social risks.

External partnerships

A large portion of the HESTA portfolio is managed by external investment managers. Therefore how we assess and manage these relationships becomes an important part of our approach.

We select managers that are aligned with our responsible investment belief. How managers incorporate ESG issues in their investment decision-making and active ownership activities is part of our manager due diligence, appointment and monitoring process. We seek to invest with partners who invest and advocate in alignment with HESTA's beliefs and corporate values.

We seek to add value to our partners by conducting regular assessments of their policies and practices and providing feedback to encourage progress in ESG integration. This aligns with Principle 4 of the PRI, where we commit to promoting responsible investment practices across the investment industry.

Exclusions

Our capital allocation decisions must consider the protection of our portfolio from ESG risks including systemic risks that might arise in the long term. To address these risks, there are circumstances where we choose not to provide capital to specific companies or sectors where we believe active ownership is unlikely to be effective.

We have developed an escalation framework to determine if an investment is inappropriate. This framework considers issues such as contraventions of international treaties or conventions and social risk regarding community expectations.

Where our comprehensive escalation process has led to HESTA enacting an exclusion to best mitigate risks, we disclose these exclusions in the HESTA Product Disclosure Statement.

7. Deep impact investments

We seek to invest in opportunities that have a positive impact on the environment and society with a focus on our seven areas of impact as framed by the SDGs (3, 5, 6, 7, 8, 11 and 13). These investments are focused on solutions that represent strong investment opportunities and also contribute to the challenges outlined by the SDGs. We seek additional transparency and reporting against these broader non-financial objectives.

We will look to form partnerships and pursue opportunities that are expected to contribute strong financial returns while also having a positive impact on the economy, environment and society that our members will retire into.

8. Active ownership

Active ownership or stewardship is the means by which investors most directly influence companies, markets, and economies and in turn society and the environment as a whole[2]. We do this as part of our responsibility to protect and enhance long-term investment value for members by promoting sustainable value creation in the organisations we invest in.

HESTA believes that our ownership practices can improve long-term risk-adjusted returns to our members. As such, it is entirely consistent with HESTA's fiduciary duty to act in the best interests of our members. In fact, across all ESG issues HESTA believes that good performance will deliver superior returns over the long term and that poor performance constitutes a risk that must be taken into account in investment decisions. The Active Ownership Priorities (refer to Appendix B) outline how we focus our stewardship activities.

As a long-term investor where we expect to own an asset for a number of years, active ownership is especially important in serving the interests of our members. Active ownership includes:

> *Engagement* - entering into a dialogue with companies to better understand their business model and to influence their performance and practices in line with our Active Ownership Priorities. It also includes the dialogue we have with our external investment managers to encourage progress in their ESG integration practices.
>
> *Voting* – exercising our voting rights in both listed and unlisted markets is a key element of our stewardship activities and an important link in the chain of accountability between a company and its shareholders (and an investment manager and its investors). The right to vote at company shareholders' meetings (or as unitholders) is a fundamental part of a well-functioning corporate

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[2] As defined by the PRI in Active Ownership 2.0 https://www.unpri.org/investor-tools/stewardship

governance system. Decisions on voting are made by HESTA based on our Active Ownership Priorities but also follow consultation with our investment managers, proxy advisors, engagement providers and other relevant parties. HESTA aims to execute all our voting rights to our shares in listed public companies including shares on loan. A few exceptions apply such as investments in pooled vehicles where we don't own voting rights; certain cases where not all shares are able to be recalled on time; or in markets that require a Power of Attorney (PoA) and where the cost of putting one in place doesn't outweigh the benefits of voting in that market. In countries where there is share blocking, our investment manager will determine whether the votes attached to HESTA shares should be executed, based on a cost benefit assessment. We disclose all our votes on listed companies in our website.

Legal action - Class actions allow shareholders, as a collective group, to claim for losses against a company where a reasonable case can be made that the loss occurred due to breaches of corporate laws or regulations. HESTA participates in class actions to recover losses but also as a means of encouraging better standards of corporate governance and improved accountability by companies, directors and corporate advisors to their shareholders.

We believe that through the tools available to active owners, including engagement and voting, we can most effectively influence a company to adequately address ESG issues. We believe active ownership may lead not only to improved performance at the company level, but has the potential to result in improved performance across the market.

9. Advocacy and leadership

Advocacy

As a large superannuation fund, we recognise our influential position in the market and our responsibility to use our voice responsibly to address systemic issues that are at odds with maintaining and building sustainable financial markets and generating long-term performance. That's why we promise our members that we will be *gutsy advocates driving meaningful change for generations to come*.

This may involve seeking change, or development of laws, regulations, standards or guidelines to improve long-term performance of markets and reduce market failures. Advocacy may also focus on raising awareness about ESG issues or practices that will help us achieve sustainable financial markets or better RI Practices. Our advocacy efforts are guided by our Active Ownership Priorities (Appendix B) which consider materiality, and our seven areas of impact. We seek to ensure that our advocacy, at the investment level and at the Trustee level, is aligned for a consistent message to the market.

Collaboration

HESTA also seeks to collaborate with like-minded peers and organisations. We believe in the power of collective action for tackling systemic issues, and one of the ways we ensure our interests are aligned is by seeking collaboration with other asset owners or organisations that have an asset owners' lens.

HESTA invests in more than 3,000 entities across multiple markets. To amplify the reach and impact of our active ownership activities, we develop strategic partnerships.

HESTA regularly engages with and is a member of/signatory to the following organisations:

- The PRI
- The Australian Council of Superannuation Investors (ACSI) (Engagement provider)
- Regnan (Engagement provider)*
- Hermes EOS (Engagement provider)
- Investor Group on Climate Change*(IGCC)
- International Corporate Governance Network (ICGN)
- Asia Corporate Governance Association (ACGA)
- Climate Action 100+
- 30% Club Australia*
- Workforce Disclosure Initiative (WDI)

*Refers to organisations where we have been founding members

10. Transparency and reporting

HESTA is committed to transparency, and we regularly report on our progress against our RI ambitions in line with a number of nationally and internationally recognized frameworks.

As a signatory of the PRI, one of the world's leading proponents of responsible investment, HESTA reports on its RI activities and integration on an annual basis. The PRI reporting framework measures an organisation's maturity against the seven PRI principles, offering signatories a benchmark against which to compare themselves with likeminded asset owners. The PRI Transparency and Assessment reports are available on our website.

The Australian Asset Owner Stewardship Code sets out how asset owners should practice transparent stewardship, and how it should meet its obligations to act in the best interests of members. As a signatory, we publish a Stewardship Statement (See Appendix C) showing how we comply with the Code's six principles. We disclose our engagement activities, where it is appropriate to do so, in the HESTA Annual Report or on the Fund's website. HESTA proxy voting decisions are made public periodically on our website.

The Task Force on Climate-related Financial Disclosures ('TCFD') sets out expectations for publicly listed companies, but also asset owners, on how to report on a range of climate-related actions. HESTA has long spoken of the risks posed by climate change, and will use TCFD reporting to outline the risks to its investments. 2

HESTA also reports on how we are contributing to our seven areas of impact as framed by the SDGs. While the development of global standards for impact measurement is evolving, we seek to participate actively in their development to ensure these are aligned with HESTA's RI approach. In the meantime, we are committed to demonstrating how our investments and active ownership activities contribute to the SDGs, through case studies and other relevant metrics.

Appendix A: Climate change risk management

HESTA acknowledges that climate risk is a material, foreseeable, and actionable risk in the portfolio.

HESTA, as trustee and a long-term universal asset owner, considers that the changing climate is an important risk and opportunity with financial, social and environmental implications. The TCFD, which HESTA supports, classifies climate-related risk into two categories:

1) risks related to the transition to a lower-carbon economy
2) risks related to the physical impacts of climate change.

The complexity and interrelated nature of climate change risks makes them very difficult to assess, therefore we believe that a pricing mismatch can exist.

This is why climate risk is a key, multi-faceted consideration in investment evaluation and decision making at HESTA. This takes place in various parts of the Fund's investment process spanning asset-class specific exposure analysis, investment manager capability assessment and investee company engagement.

We have incorporated the risks posed by climate change into the Trustee's risk register, with the risks counted as a material financial risk. The main reason is that we see climate change as a systemic risk that is expected to have implications over many decades.

Climate change has the potential to translate into both risks and opportunities for investments including:

> *Transition risk* – exposure to carbon pricing and regulation to reduce carbon emissions which might also lead to stranded asset risk.
>
> *Physical risk* – exposure to the physical impacts of climate change, such as potential sea-level rises, and increased frequency and intensity of severe weather events
>
> *Liability risk* – resulting from companies not adequately managing the impacts of climate change potentially resulting in a breach of directors' duties.

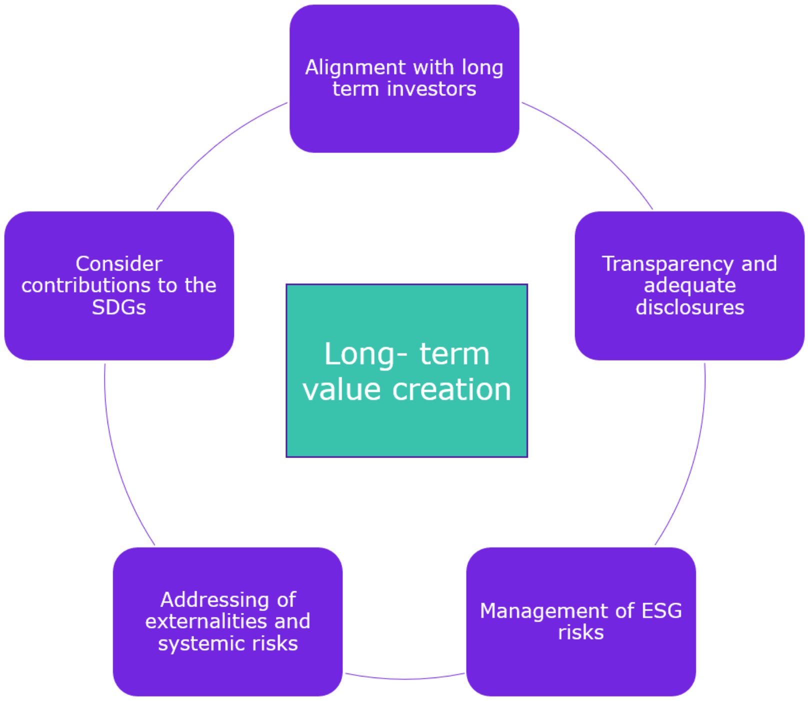
We believe companies must consider climate change risks alongside traditional financial and business risk factors. We see this as fundamental for protecting value for shareholders.

As a universal owner and long-term investor, HESTA considers this risk in all our investment decision-making.

As well as managing for climate risk, we seek to contribute to climate stability through our active ownership activities.

We seek to report how HESTA assesses climate change risks with consideration for the recommendations made by the TCFD.

Appendix B: Active ownership priorities



Clear alignment with long-term investors – we expect companies to create and enhance value for the long term, taking account of the best interests of the company, its shareholders and relevant stakeholders. A company's strategy, policies, culture and conduct, risk management and internal controls, and reporting should reflect and support this goal.

Transparency and adequate disclosures – as shareholders and creditors we require transparent and meaningful disclosure from companies for informed decision-making. Companies should publicly disclose all information that is or is expected to be material in the long term, in a timely and complete manner, including any ESG-related issues.

Management of ESG risks – we expect companies to manage for a wide range of risks within their business including material ESG risks.

Addressing of externalities and systemic risks – we expect companies to act in a sustainable and responsible way considering how their business contributes to system-wide issues and their implications in the health of the economy, environment and society where they operate now and in the future. This includes considering and managing in the present risks that might emerge in the long term. Examples of such issues are climate change, social inequality, environmental degradation and tax avoidance.

Consider their contribution to the SDGs - we encourage companies to assess and measure how they can contribute to the achievement of the SDGs and enhance those activities that have a higher positive impact in society and the environment. We believe companies can benefit from delivering products and services that help solve for the world's biggest challenges highlighted by the SDGs and contribute to a healthy economy, environment and society.

Appendix C: Stewardship principles

We have long demonstrated stewardship to protect and enhance long-term value of investments for our members. HESTA believes effective stewardship benefits companies, our members and the economy as a whole.

We're proud to be a signatory to the Australian Asset Owner Stewardship Code. The Code consists of six principles:

1. Asset owners should publicly disclose how they approach their stewardship responsibilities;
2. Publicly disclose their policy for voting at company meetings and voting activity;
3. Engage with companies (either direct, indirectly or both);
4. Monitor asset managers' stewardship activities;
5. Encourage better alignment of the operation of the financial system and regulatory policy with the financial interests of long-term investors;
6. Report to beneficiaries about their stewardship activities.

HESTA details how it addresses each of the principles in its Stewardship Statement.