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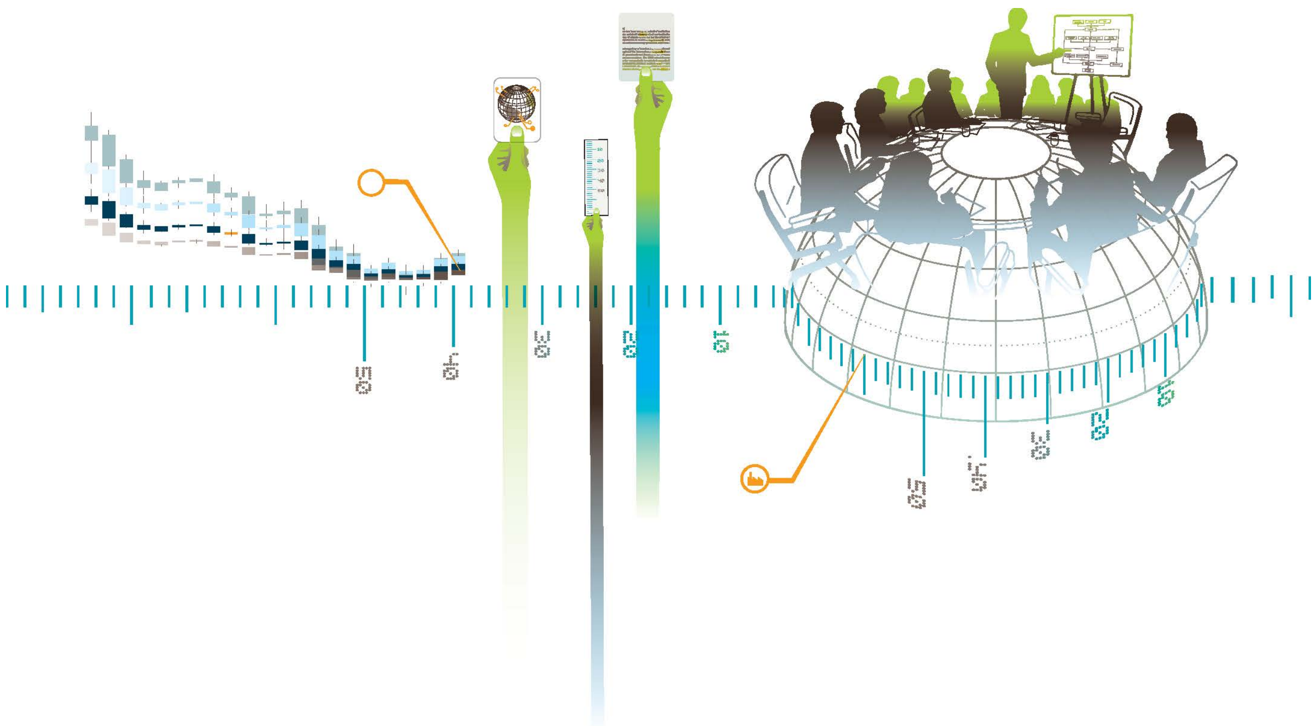
RobecoSAM PE ESG Engagement Report 2014



RobecoSAM PE ESG Engagement Report 2014

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RobecoSAM AG

www.robecosam.com

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Executive Summary

This 2014 edition of the Responsible Entrepreneurship Report marks nine years of RobecoSAM Private Equity's engagement with private equity (PE) funds on Environmental, Social and Governance (ESG) integration. With more responses than ever, and an encouraging focus on new reporting and assessment methodologies, this has been our most wide-ranging annual ESG assessment to date.

The intention of this report is to inform our investors of this year's results, and to stimulate further integration of ESG analysis in the investment process of participating PE funds. Results are based on a participating fund's responses to the annual RobecoSAM Private Equity Responsible Entrepreneurship Questionnaire, and these responses are summarized here in detail. We shed light on general ESG trends and market developments, and highlight five case studies of funds with exemplary ESG engagement. We also examine new methods of ESG risk analysis and reporting.

The most important results of the 2014 assessment can be summarized as follows:

- The average ESG score increased to 65.7% in 2014: Strategy & Policy, Social and Governance sub-scores have generally improved, with some lower scores reflecting the addition of new funds to the assessment universe.
- One third of the assessed PE funds can be categorized as ESG leaders in 2014. The number of funds categorized as followers has significantly increased.
- On average, the more mature PE fund programs demonstrate better performance than recently introduced programs.
- Our new focus on portfolio-specific ESG recommendations has had a positive effect, moving laggard funds into the follower category as they mature.
- Typically, funds with dedicated ESG teams or specialists in place achieve higher ESG scores.
- On average, funds that incorporate ESG in their due diligence process become better ESG performers.
- Portfolio companies on average show low ESG risk exposure as measured by RepRisk.

By assessing the funds across different programs, and analyzing the relationship between ESG performance and the different monitoring and reporting habits of PE funds, examples of encouraging and market-leading ESG practices are identified. Of particular note in this report are the case studies of diverse funds, which demonstrate different models for monitoring portfolio companies. These funds also encourage their portfolio companies to become accountable for the sustainability of their activities.

Ongoing evaluation of extra assessment options is vital as the PE market becomes increasingly affected by ESG considerations. We are constantly refining our approach in order to make it more efficient and fund-friendly. Our pilot with PRI represents part of these efforts. It aims to reduce the reporting burden on GPs, streamlining the ESG assessment process and creating valuable data that can be used to meaningfully align our PE funds with sustainable asset management worldwide. As focus on ESG becomes more intense, we will be in a position to share vital knowledge and insights.

1 Introduction

This ninth annual Responsible Entrepreneurship Report summarizes the results of our latest Environmental, Social, and Governance (ESG) assessment of private equity (PE) funds. It includes 73 responses[1]. Larger in scope than our 2013 report, it also introduces new discussion topics, including an analysis of ESG incidents.

ESG factors continue to gain importance on the agendas of both limited and general partners. A recent study by PwC[2] confirms that the PE market is moving towards greater ESG integration. 79% of the 60 participants in the PwC survey believe interest of PE managers in responsible investment is set to grow. While the focus of most responsible investment approaches is on the pre-investment phase, RobecoSAM's monitoring and engagement approach remains uniquely able to track the performance of private equity funds as they mature. Both RobecoSAM Private Equity and Rabobank Sustainability continue to engage with general partners, benchmarking their ESG performance and sharing best ESG practices.

In this year's report we reflect on the recent past and look into the future. We focus on past ESG performance in the first part of the report, and discuss the future elements of our engagement process in the second part. The latter, future-oriented section includes discussions of ESG tools that we can and will use in our engagement with PE managers going forward. In this context we introduce the analysis of ESG incidents captured by global news sources, in relation to the companies in the portfolios of the PE funds that participate in our ESG engagement. For this purpose, we gained access to a specialized database managed by RepRisk.

This report is structured as follows: In section 2, we discuss important elements of the ESG performance of participating fund managers in 2014. We compare performance over time and across different programs. Section 3 highlights additional insights into the ESG practices of PE managers. In particular, we look at how they have organized responsibility for ESG issues, how they incorporate ESG analysis in due diligence, and how they monitor their portfolio companies. We also look at their methods of reporting on ESG matters. In Section 4, we highlight good ESG practices of selected PE managers. In Section 5, we analyze ESG incidents recorded in the RepRisk database for the portfolio companies and their managers. Sections 6 and 7 engage in a discussion of the reporting pilot that RobecoSAM PE has set up with the UN Principles for Responsible Investment (PRI), and our involvement in different PE market initiatives on responsible investing. Finally, section 8 concludes with some thoughts on continued evaluation of ESG integration and engagement, and reveals plans for future improvement.

[1] In total, 73 private equity funds received an ESG score. Due to a pilot ran in collaboration with the PRI, some of these funds were scored based on their pilot submission. Some fund managers apply the same ESG approach to multiple PE funds. Therefore, these fund managers receive one score for multiple funds while others might receive multiple scores for multiple funds.

[2] http://www.pwc.com/en_GX/gx/sustainability/publications/assets/bridging-the-gap.pdf

2 ESG performance in 2014

In this section, we discuss the overall ESG performance of the PE funds included in the Responsible Entrepreneurship Program at the end of 2014, and highlight the trends we observe. Funds are evaluated on their ESG policy and strategy (representing 40% of the total ESG score), and on their Environmental, Social and Governance performance (each representing 20% of the total score).

We begin by describing the overall ESG results and recent changes in the assessed portfolio. Then we look at how the Environmental, Social and Governance sub-scores have evolved since 2013, and discuss the changes in the distribution of funds across different performance categories, i.e. leaders, followers and laggards. The section concludes with a note on the performance of PE funds across different programs with an ESG overlay.

2.1 Overall ESG results

The average ESG score of the PE funds in RobecoSAM Private Equity's assessment universe has increased from 64.7% in 2013 to 65.7% in 2014. This is despite the fact that a number of PE funds were newly added to the universe. This continued increase is in line with the positive trend of recent years (see Table 1).

The improved average score is a result of several factors, including the exceptional performance of the highest achievers and a renewed vigor at the lower end of the ESG spectrum. One additional fund attained a perfect score of 100% this year, and we have also seen some significant improvements at the bottom of the table.

The two funds that have consistently scored lowest in preceding years have clearly changed their stance towards ESG.

The two funds that have consistently scored lowest in preceding years have clearly changed their stance towards ESG. The lowest scoring fund has, in the past, failed to recognize the importance of an ESG policy, ESG due diligence, and regular company engagement on these topics. These things were all introduced comprehensively in 2014, resulting in an ESG score almost triple its 2013 value. Also here we see that the interest of PE managers in ESG integration is growing. Our engagement efforts have helped to get ESG on their agenda.

Table 1: Total ESG scores of funds with ESG engagement overlay, 2010-2014

	2014	2013	2012	2011	2010
Average	65.7%	64.7%	62.1%	60.5%	62.3%
Maximum	100.0%	100.0%	98.9%	98.3%	91.0%
Minimum	16.3%	13.7%	13.7%	16.1%	17.0%

Source: Robeco Responsible Entrepreneurship Questionnaires 2010-2014

The lowest scoring fund in 2014 is a new entrant, following on from last year's trend, in which we saw new entrants showing below-average performance. The lowest overall score, however, is an improvement on 2013's worst figure.

2.2 Newly added funds

During 2014, seven funds were added to the ESG assessment universe. Based on their first assessment, one entrant was categorized as an ESG leader, exemplifying sustainable investment principles. One was categorized as an ESG follower, showing at least some integration of ESG principles into its investment process, from strategy and policy standpoints as well as in respect of their ESG engagement with portfolio companies. Five of the entrants were categorized as ESG laggards.

The ESG leader fund was able to demonstrate a very well documented and thorough ESG management system. Besides an extensive set of principles, the fund was already mapping ESG risks and documenting best practices for its investors, not something we typically see in new funds.

Two laggard funds have not made any investments yet. Funds that have yet to invest are only rewarded for their ESG strategy and policy, resulting in a low score that puts a downward pressure on the average score of the ESG universe as a whole. We based the assessment of these funds on their responses to the due diligence questionnaire, which is a condensed version of the annual Responsible Entrepreneurship Questionnaire.

As in previous years, the funds newly added to the assessment universe show a below-average ESG performance. This relates to the fact that their ESG strategy and policy is less advanced than that of the average fund, which has been a part of the engagement process for several years.

2.3 ESG sub-scores

The total ESG score is comprised of four sub-scores that reflect the fund's ESG strategy and policy, and its Environmental, Social and Governance performance. On average, PE funds continue to perform the best on strategy and policy (see Table 2).

In addition, the difference between the highest and the lowest scoring fund tends to be the smallest on this sub-score. This is not surprising given that most funds include some ESG aspects either in their company policy, mission statement, corporate strategy, investment policy or processes.

Over the last four years, average sub-scores have gradually improved. This is despite the fact that new funds were added to the investment portfolio each year.

New entrants contribute to the zero minimum scores on different sub-sections, and these scores should therefore be interpreted carefully. Two new funds were only scored on their strategy and policy, and did not fill out the rest of the questionnaire. It is important to note that the funds responsible for the lowest scores in 2013 did show some improvement in 2014, reinforcing the notion that long-term engagement bears ESG fruit.

On average, PE funds continue to perform the best on strategy and policy.

Low E, S and G sub-scores are a typical consequence of low integration of ESG factors in investment strategy and policy. It is encouraging to see the average score increase on this point. Surprisingly, some funds claim that they are unable to provide evidence of their ESG processes. We believe this may be the result of misinterpretation of the questionnaire, a misunderstanding that is typically resolved after a first round of engagement with the funds.

Another factor that contributes to the variability in sub-scores is the requirement to provide examples of best ESG practices in the portfolio companies each year. Sometimes funds give a great one-off demonstration of good ESG practices—following the publication of extensive case studies or the implementation of certain policies—but fail to demonstrate such efforts on a continual basis.

Table 2: ESG sub-scores of funds with ESG engagement overlay, 2010 – 2014

Strategy & Policy scores	2014	2013	2012	2011	2010
Average	71.2%	69.4%	67.8%	65.2%	65.8%
Maximum	100.0%	100.0%	100.0%	95.7%	97.1%
Minimum	15.7%	10.0%	10.0%	12.9%	20.7%

Environmental scores	2014	2013	2012	2011	2010
Average	66.4%	66.5%	63.0%	64.3%	65.5%
Maximum	100.0%	100.0%	100.0%	100.0%	96.7%
Minimum	0.0%	3.3%	10.0%	10.0%	6.7%

Social scores	2014	2013	2012	2011	2010
Average	60.2%	59.2%	55.2%	52.4%	56.3%
Maximum	100.0%	100.0%	100.0%	100.0%	93.3%
Minimum	0.0%	3.3%	0.0%	0.0%	1.7%

Governance scores	2014	2013	2012	2011	2010
Average	60.0%	59.0%	57.0%	55.3%	57.9%
Maximum	100.0%	100.0%	100.0%	100.0%	99.3%
Minimum	0.0%	0.0%	0.0%	10.0%	1.7%

Source: Robeco Responsible Entrepreneurship Questionnaires 2010-2014

2.4 ESG leaders, laggards and followers

According to their total ESG score, we categorize the assessed PE funds either as ESG leaders (total score > 80%), ESG followers (total score between 50% and 80%), or ESG laggards (total score < 50%). A description of their defining characteristics is provided in Figure 1 below.

Figure 1: Characteristics of ESG leaders, followers and laggards

ESG Leaders	ESG Followers	ESG Laggards
ESG Leaders recognize the value of ESG integration in their investment process and in the portfolio companies. These funds are forward looking and often pioneer in the measurement of ESG performance and the monitoring of ESG metrics. Leaders typically make use of external ESG expertise and have a dedicated person or committee for dealing with ESG issues. While implementing the specific ESG policy they continuously manage to show good results on the performance of their portfolio companies on Environmental, Social and Governance issues. Often, these results are comprehensively disclosed to investors.	ESG followers generally have an ESG strategy or policy in place at the fund level (in this sense, they are comparable to ESG leaders). The translation of this policy into demonstrable results at portfolio companies' level is where they lag behind on ESG leaders. Funds categorized as ESG followers are often in the implementation stage of their ESG ambitions for the practices of portfolio companies. As an indication, from the 12 funds categorized as ESG followers in 2010, five have become ESG leaders in 2012. Another type of ESG follower is an ex-ESG leader that has had difficulties in showing ESG improvements in its portfolio companies.	ESG laggards are characterized by a weak or absent ESG strategy or policy and low Environmental, Social and Governance performance. They often make the claim that ESG is at the core of their organization, but they are not able to show substantial improvements in their portfolio companies. As stated earlier, newly added funds typically tend to be categorized as ESG laggards after the first assessment. Often, this is due to the lack of evidence the funds provide and the misinterpretation of the questionnaire. Funds in this category are reluctant to implement our recommendations, or they have been acquired based on economic merits as secondary fund stakes. These fund managers are typically less committed to answering our questionnaire than the primary investments. In some cases, funds are simply not able to show any ESG results due to the fact that they have not made any investments yet.

Source: Rabobank, RobecoSAM PE

The number of laggards in the assessment universe of 2014 decreased by three.

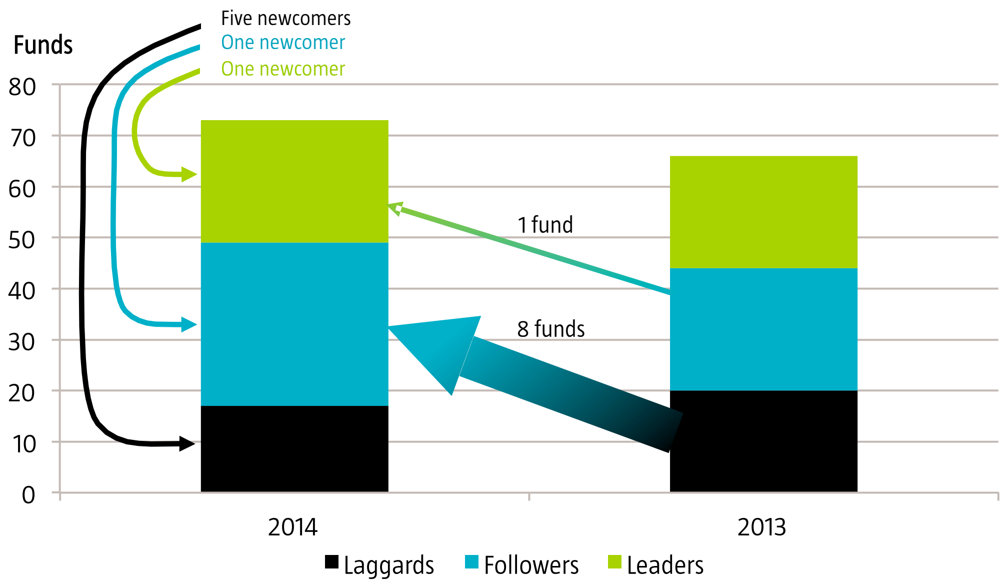
The number of laggards in the assessment universe of 2014 decreased by three (see Table 3).As shown in Figure 2, this is a positive development, given that five of the seven new entrants were categorized as laggards. In other words, while a number of new laggards entered the process, the overall movement from laggards to followers was much stronger. In the past two years, we have devoted extra attention to laggards, strenuously assisting them in the design and implementation of ESG integration in their investment processes. We attribute the welcome success of this assistance to a shift in our approach. In the past, our recommendations to the funds were more generic. Now, we strive to provide more portfolio-specific recommendations, combining portfolio company information with analysis of the sector-specific ESG issues.

Table 3: Number of ESG leaders, laggards and followers in ESG engagement programs, 2010-2014

	2014 No. of funds	%	2013 No. of funds	%	2012 No. of funds	%	2011 No. of funds	%	2010 No. of funds	%
Laggards	17	23%	20	30%	20	33%	20	40%	13	36%
Followers	32	44%	24	36%	24	39%	16	32%	12	33%
Leaders	24	33%	22	33%	17	28%	14	28%	11	31%
Total	**73**	**100%**	**66**	**100%**	**61**	**100%**	**50**	**100%**	**36**	**100%**

Source: Robeco Responsible Entrepreneurship Questionnaires 2010-2014

Figure 2: Mutations between leader-, follower- and laggard- categories between 2013 and 2014



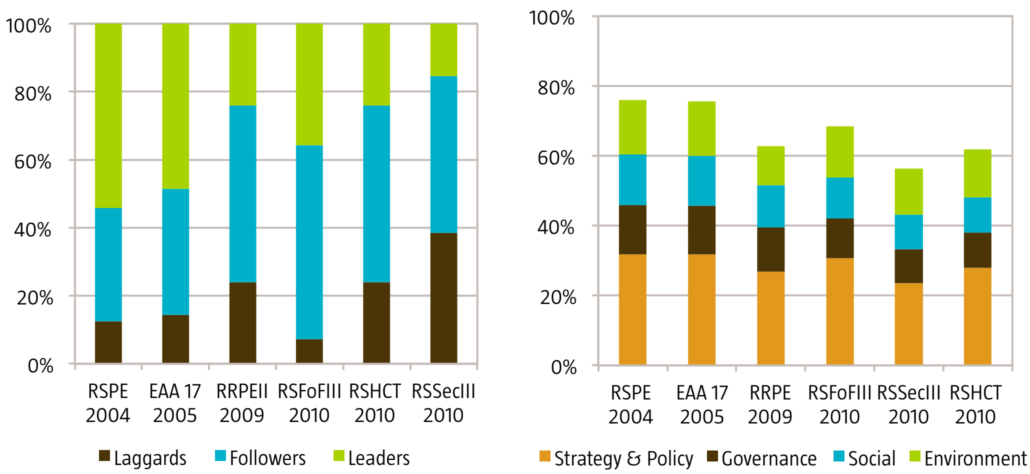
Source: Rabobank, RobecoSAM PE

It is encouraging to see eight of the 20 laggard funds of 2013 joining ESG followers this year, a move that leaves just 23% of participating funds in the laggards-category. This is an indication that the segregated engagement approach leads to positive results. The transition the laggard funds are undergoing is also a welcome indication of a larger trend, as the PE market moves towards further ESG integration.

2.5 ESG performance across different PE fund programs

RobecoSAM currently manages multiple programs with an ESG overlay. The ESG program began in 2004, with the Robeco Sustainable and Private Equity (RSPE & RSPE C.V.), and a commitment by the Environment Agency Active Fund (EAA 17 and EAA 17 II). Since then it has extended to other fund programs, shown in relative performance for 2014 in Figure 3.

Figure 3: ESG performance of different PE fund programs in 2014[3]



Source: Robeco Responsible Entrepreneurship Questionnaires 2010-2014

Figure 3 is a nice encapsulation of the differences in average ESG performance of different PE programs. These can largely be explained by looking at the age and fund type of the program in question.

Mature products tend to have higher average scores.

Mature products tend to have higher average scores, suggesting that the number of years the PE funds have spent in the engagement program have a positive effect on their ESG performance. With respect to fund types, clean tech or resource efficiency focused PE funds on average demonstrate lower ESG scores than mainstream, buyout funds. Clean tech funds generally invest in companies with a positive environmental impact, which are in the early development stages. Given that such companies generally have little means to pursue an active ESG strategy, the social and governance sub scores of clean tech funds are relatively low while their environmental scores are relatively high. Nevertheless, we increasingly see venture funds finding their way in organizing ESG management. That said, the lower scores of RobecoSAM Secondary Fund III (RSSecIII) and RobecoSAM Horeca Clean Tech (RSHCT)—both exclusively clean tech or resource efficiency funds—are in line with expectations. The generally higher performance of RSPE, RSFoFIII and EAA 17 reflects their mix of both clean tech and mainstream PE funds.

[3] Abbreviations used in the graph:
Robeco Sustainable Private Equity (RSPE & RSPE C.V.), Robeco Responsible Private Equity II (RRPE II), Robeco SAM Horeca Clean Tech (RSHCT & RSHCT II), Robeco SAM Funds of Funds lll (RSFoFlll), Robeco SAM Secondary Fund lll (RSSeclll). The Environment Agency Active Fund (EAA 17 & EAA 17 II).

3 Highlights from the 2014 assessment

In this section, we provide some additional insights on how PE fund managers have integrated ESG analysis in their investment processes. In particular, we look at how they have organized the responsibility for ESG matters in portfolio companies, and how they integrate ESG analysis in due diligence. We also examine if and how fund managers monitor ESG Key Performance Indicators (KPIs), how many of their portfolio companies have specific ESG policies in place, and how they report on ESG factors.

It should be noted that the analysis below is largely based on descriptive statistics that we have calculated from responses to our questionnaire, and not on regression analysis.

3.1 Organization of ESG responsibility

How PE managers organize responsibility for ESG matters is one of the key questions in our assessment. Funds are asked to state whether they have an ESG committee or a dedicated ESG specialist (and whether this is at operations, investor relations, or board level). If they have no dedicated specialist, they are asked if ESG matters fall under general board responsibility or are not being assigned at all. In total, 89% of the participating funds have assigned responsibility for ESG issues, and address these issues during investment committee meetings.

Of all the funds in the assessment universe, 40% had put an ESG committee in place by the end of 2014. We see an ESG committee or a dedicated ESG officer as an indication of a well-organized ESG approach. Typically, the collection of ESG data is higher on the agenda when a dedicated team or person is in place, which also leads to better ESG reporting.

Funds that have a committee or specialist in place score better on Environmental, Social and Governance performance indicators.

Funds that have a committee or specialist in place therefore tend to score better on Environmental, Social and Governance performance indicators, both as a result of enhanced focus and better record keeping. Conversely, when nobody is responsible for ESG matters or reporting (and when ESG is part of a general board responsibility), funds tend to show lower ESG sub-scores.

Funds with no ESG responsibility assigned are very rare in our portfolio, but they do occur. Often, a fund listed with unassigned ESG responsibilities is in an early stage of its development, or has misunderstood our questionnaire and is incorrectly reporting its ESG processes (see section 2). We have also identified situations in which clean tech funds report no assigned ESG responsibilities, while integrating environmental sustainability and stewardship into their whole investment proposition. Four such clean tech funds reported no ESG responsibility at the end of 2014, but an analysis of the companies they typically invest in shows that their whole business is based on sustainability.

3.2 ESG in due diligence

To some extent, most fund managers claim to incorporate ESG issues in their investment process. Their approaches to ESG integration in the due diligence and monitoring process differ widely, however. For example, some fund managers use a separate ESG questionnaire during due diligence while others include ESG questions in their regular due diligence questionnaire. Also, many funds use external experts for their environmental and governance due diligence. Human Resources consultants are often engaged by PE funds to perform due diligence on social issues.

Funds that incorporate ESG analysis in their due diligence process, particularly those using a separate questionnaire for that purpose, typically show better environmental and social performance. Moderate inclusion of ESG analysis, or a lack of it in due diligence, is often shorthand for poor ESG performance.

3.3 ESG monitoring in portfolio companies

We are interested not only in whether portfolio companies have written ESG policies, or have management systems in place, but in the specifics of how they implemented these. In engaging with PE fund managers, our standard topics of consultation aim to survey the type and quantity of ESG indicators used to monitor performance. Examples of ESG indicators include: kWh energy and m3 water consumed, direct and indirect CO2 emissions produced, number of days in training or educational programs, % of employees receiving health and safety training, number of accidents and/or casualties per year, and whether a code of conduct is present. In other words, a KPI for ESG can be anything in a portfolio company's processes that is legitimately concerned with sustainability, social responsibility or overall governance.

The indicators are selected by fund managers or their portfolio companies, based on sector- and region-specific needs. The number of KPIs varies greatly. By the end of 2014, approximately 39% of the total number of participating funds had a very extensive set of ESG-related KPIs in place. 35% of funds monitored some KPIs, 3% were still developing KPIs and 23% had no KPIs at all. The number of funds with extensive ESG KPIs increases every year, as more of them reach a stage in ESG integration where they can introduce ESG metrics that are relevant for their portfolio companies. They can only manage ESG factors if and when they can measure them.

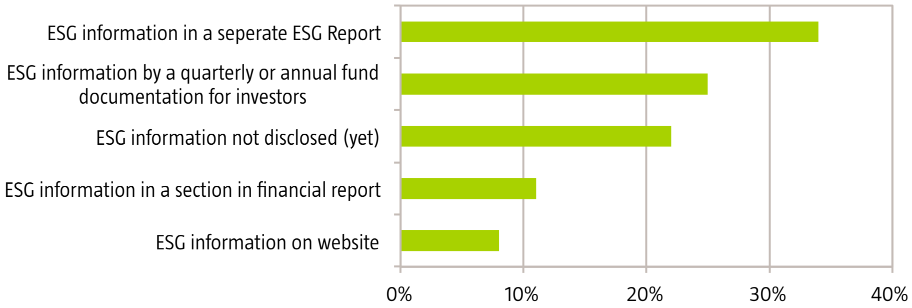
Roughly half of the PE fund managers indicated that more than 75% of their portfolio companies had an environmental policy and management system in place.

Roughly half of the PE fund managers indicated that more than 75% of their portfolio companies had an environmental policy and management system in place. These portfolio companies also use corporate governance related policies and procedures, and around 62% of them had relevant social policies and management systems in effect. About one third of funds report that their companies don't have separate environmental or social policies. This may not be as alarming as it sounds, as fund managers often implement environmental and social practices and procedures in their portfolio companies without documenting them in separate records. Additionally, some of these funds are young (in ESG engagement terms), and may not yet be monitoring their portfolio companies with respect to their environmental and social metrics.

3.4 ESG reporting

All PE managers in our engagement universe are asked whether they disclose information on ESG risks and opportunities to investors, and how this is done. At the end of 2014, almost 78% of funds disclosed ESG information in some way. Figure 4 illustrates which reporting channels PE managers used for ESG information. Of the 22% of funds currently failing to report on ESG matters, some may be looking to do so in the near future. Both mainstream and clean tech funds are found in this latter category.

Figure 4: Distribution of PE funds according to ESG reporting channels used



Source: Robeco Responsible Entrepreneurship Questionnaires 2014

There are two reporting methods that seem to link to improved ESG performance. PE funds that disclose ESG information in a separate ESG report, or funds disclosing ESG information within a regular financial report, fare better than funds disclosing information in other ways or not at all.

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4 Examples of good ESG practices

In every annual report, we highlight PE funds with good or exemplary ESG practices. This year, we have chosen funds whose managers exemplify best practice in reporting and monitoring. The managers of these funds have implemented, or are in the process of implementing, monitoring and reporting frameworks that make their ESG practices highly visible to the investor. Their approach enables them to create company-specific action plans based on annual monitoring of transparently defined, well-observed metrics.

We present five funds that have excelled in this area. Aloe is chosen for its unique application of UN Global Compact principles. BC Partners is recognized for its ability to trigger portfolio companies to set ESG targets for themselves. Berkeley Energy is celebrated for its comprehensive environmental and social action planning. Terra Firma's newly built guidance tool for investment managers makes the grade, and Alpha is included because of its exemplary ESG scorecard for portfolio companies. For PE funds that are still working on ESG integration, the practices of these five funds can serve as inspiration.

4.1 Aloe Private Equity

Aloe Private Equity (Aloe) is a private equity fund manager focusing on environmental technologies that have an end market focused on Asia. The fund manager has offices in the UK, France, India and China. RobecoSAM invested in the second of its three funds (Aloe Environment Fund 2) in 2007, and Aloe became an ESG leader in 2009 and has won the Financial Times and International Finance Corporation Sustainable Investment of the Year award twice.

The fund manager publicly committed to take the UN Global Compact principles (see Figure 5) into account in its investment decisions. As it has formally endorsed the UN Global Compact principles, Aloe is also obliged to report progress on an annual basis via the so-called Communication of Progress. In this document, Aloe reports on the implementation of the ten principles in their daily practice. As part of this communication Aloe also provides practical examples at the General Partner (GP) level, as well as at portfolio company level for all of the implementation efforts they have pursued over the year.

Figure 5: UN Global Compact Principles

Human Rights Principles
Businesses should support and respect the protection of internationally proclaimed human rights; make sure that they are not complicit in human rights abuses.

Labor Principles
Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining; the elimination of all forms of forced and compulsory labor; the effective abolition of child labor; and the elimination of discrimination in respect of employment and occupation

Environmental Principles
Business should support a precautionary approach to environmental challenges; undertake initiatives to promote greater environmental responsibility; and encourage the development and diffusion of environmental friendly technologies.

Anti-Corruption Principles
Businesses should work against corruption in all its forms, including extortion and bribery.

Source: UN Global Compact

4.2 BC Partners
BC Partners is a pan-European private equity firm that has invested in companies in Europe and selectively in North America for over 25 years. Besides London, BC Partners also has offices in Paris, Hamburg and New York. RobecoSAM invested in BC European Capital IX in 2011. The firm became an ESG Leader in 2013.

BC Partners was an early signatory of the Principles for Responsible Investment (PRI) in March 2009, and adopted its own ESG Policy in 2010. As the majority shareholder in nearly all of its portfolio companies, BC Partners takes an active role in improving ESG awareness, performance and compliance in each of its companies' operations. Since 2011, BC Partners has required that preliminary investment memoranda (PIMs) include a summary of ESG diligence conducted along with a description of any issues or concerns identified. The ESG diligence is conducted by the deal team members and discussed by the investment committee prior to the commitment of capital. All investment professionals receive introductory ESG training in order to ensure the assessment is carried out appropriately. BC Partners has strongly recommended that each new portfolio company to establish an ESG policy (should one not already exist), and complete an ESG assessment within a year. The ESG Advisory Team at PwC assists and supports the first year assessment. Following the initial ESG assessment, each portfolio company is required to carry out its own ESG assessments at board level on an annual basis. The ESG reviews capture the following areas:

- ESG issues in the last 12 months and remedial actions taken;
- ESG improvement initiatives and their status in last 12 months, and
- ESG KPIs compared to the targets set.

ESG monitoring of portfolio companies is broken down into five principal categories: Workplace, Community, Environment, Marketplace and Governance. While annual monitoring of KPIs is important from many perspectives, BC Partners stands out in their ability to trigger portfolio companies into setting ESG targets for their operations. This is evident from their ESG board reports, which RobecoSAM receives annually.

BC Partners stands out in their ability to trigger portfolio companies into setting ESG targets for their operations.

4.3 Berkeley Energy / REAF

Berkeley Energy is a global private equity firm, currently managing two funds that invest into development stage renewable energy assets using proven technologies. The fund has offices in the United Kingdom, Mauritius, Singapore, India, Kenya, and a presence in the Philippines. In 2011, RobecoSAM invested in the Renewable Energy Asia Fund, which has since grown to become an ESG leader as of 2013.

Berkeley Energy has an extensive environmental and social management system, in which they set out the tenets of their responsible investment approach. At the initial screening stage, an early assessment of the likely environmental and social impacts is carried out. At this point, a preliminary categorization of the project is identified along with any key issues. An investment at this stage can be: Category A with potential significant adverse social and/or environmental impacts that are diverse, irreversible, or unprecedented, Category B with potential limited adverse social or environmental impacts that are few in number, generally site specific, largely reversible, and readily addressed through mitigation measures, or Category C with minimal or no impacts. At the second investment review, the fund carries out an in-depth assessment based on Berkeley's environmental and social requirements, which include the IFC Performance Standards, national law and ILO Core Labor Standards. This allows for a final categorization and the development of an Environmental and Social Action Plan (ESAP) with time bound actions aimed at mitigating negative environmental and social impacts.

RobecoSAM annually receives Berkeley's Environmental, Social and Governance Performance Report. Through this report, extensive ESG information is summarized into readable factsheets, both at portfolio company and fund level. The report provides an overview of the ESG issues and opportunities, as well as community development programs, and Corporate Social Responsibility (CSR) activities aimed at improving the lives of the local community. ESG improvements that have been achieved over the lifespan of the investments, as well as actions to be undertaken within a specified timeframe are included. In addition, since it is a renewable energy fund, the CO_2 impact of investments is also detailed. Furthermore, the fund organizes anti-corruption and other Corporate Governance education seminars internally and for each portfolio company as part of the key issues to be addressed across the portfolio.

4.4 Terra Firma

Terra Firma is a large U.K. based buyout private equity firm with a European focus. The firm has been part of the RobecoSAM assessment universe since 2007, when RobecoSAM invested in Terra Firma Capital Partners III. Terra Firma has been categorized as an ESG leader since 2013.

This year, the firm has formalized its ESG investment roadmap (see Figure 6), which sets out the broad steps that are undertaken over the lifespan of the investment. There are a number of milestones required through a deal process, from initial desktop screening to inclusion of ESG factors in final investment papers. In order to strengthen the screening process, the firm developed an ESG screening and due diligence guide to help its deal teams identify relevant ESG issues in new deal opportunities. This guide is an Excel-based tool comprised of 15 questions. The user fills in details of the potential investment, such as its main countries of operation and industry segments and sectors. The tool then highlights any conflicts with fund or Limited Partner (LP) restrictions, and provides a number of country- and sector- specific ESG topics, organized into high, medium and low risk categories. For each ESG category initially identified, the toolkit provides a list of questions to assist in gathering further deal-specific information. The firm furthermore acknowledges that the answers to these questions may not be available at first, but will allow a better re-assessment of the identified factors in the future.

Figure 6: ESG Roadmap overview of Terra Firma

Screen	• Screen opportunities versus fund reference lists and LP exclusion lists • Desktop assessment to identify generic sector and country ESG risks	Initial investment paper
Diligence	• Gather deal specific information • Update assessment of relevant ESG factors • Diligence ESG risks (externally or internally) • Finalise assessment of risk and existing management approach • Identify value opportunities	Diligence approval paper
Strategy	• Develop plan of improvement • Include final ESG assessment as part of recommendation to GP	Final investment paper
Operations	• Implement changes (Either on day 1, as part of 100 day plan, or in ongoing operations) • Monitor performance and report	Ongoing reporting

Source: Terra Firma, 2015

4.5 Alpha Private Equity

Alpha Private Equity is a Luxembourg based LBO private equity firm. Its sixth fund, in which RobecoSAM invested in 2012, focuses mainly on France and Italy. The firm is represented by offices in Benelux, France, Germany, Italy, Monaco, and Switzerland and has shown impressive improvements in ESG performance over the past two years.

Alpha Private Equity is committed to a process of raising awareness of ESG and spreading best practices.

Alpha Private Equity is committed to a process of raising awareness of ESG and spreading best practices. The purpose is to make progress on these issues in the medium term. In order to reach this goal, the firm issues annual ESG scorecards by which it aims to be able to monitor changes over time in ESG practices in its portfolio companies. The firm measures a number of indicators related to the following environmental and social policy topics:

- Certification
- Resource utilization
- Environmental Litigation
- Headcount
- Health, safety and employee welfare
- Training
- Equality at work
- Societal
- Litigation on social issues

In addition, the firm tracks a number of governance indicators, such as whether the portfolio company has prepared a CSR report in the reporting period, what the percentage of independent Board of Director members is, or whether the company is directly in contact with one of the corruption-sensitive countries as specified in their policy.

Based on these indicators, each portfolio company gets assigned a risk category, ranging from low to high. These risk assessments are then summarized and completed with interviews with managers of the portfolio companies. Alpha subsequently defines the main points that require further analysis. In 2014, these were largely social issues. Alpha will specify the actions that need to be taken and design action plans for their realization in the coming year.

5 Analysis of ESG incidents using RepRisk

Until now, the topics of our engagement with PE funds have been related to their ESG strategy and policy, and how they implement and monitor it in their portfolio companies. Going forward we intend to engage on more specific issues, such as ESG risks in the supply chain of portfolio companies. One of the ESG tools we can use for this purpose is RepRisk. RepRisk is a specialized database application, which systematically collects and analyzes facts, criticism, and controversies related to companies and projects worldwide. It does this daily, tracking information in 13 languages from thousands of public sources. These include international and local media, government sites, non-governmental organizations (NGOs), newsletters, social media, and blogs. The RepRisk database currently carries information on over 52,500 companies, 13,100 projects, 9,500 NGOs and 7,100 governmental bodies.

This is the first year we have used the RepRisk database in our ESG assessment process. To make an assessment, we employ the RepRisk Index (RRI), a measure that captures and quantifies a company's or project's exposure to ESG issues. A company's RRI score indicates its reputational risk on a sliding scale. The lower the number, the lower the risk. It ranges from 0 to 100 and is calibrated as follows:

- 0-25: low exposure
- 25-50: medium exposure
- 50-75: high exposure
- 75-100: very high exposure

RRI scores facilitate an initial assessment of the risks associated with investments or business relationships. With RepRisk it is possible to compare a company's exposure with that of its peers, and to track risk exposure over time.

Multiple factors influence the RRI calculation. It incorporates the impact of news sources (i.e. the potential of the news source to influence public opinion), as well as the content itself. Severity (how harsh is the coverage?) and novelty (is it a new story?) are also addressed, giving the RRI a unique ability to accurately reflect the real-world impact of stories on the portfolio company's reputation. Frequency and timing of ESG risk incidents are taken into consideration. If a company has been newly criticized, and/or has had less ESG risk incidents in the recent past, it receives a lower RRI. The more frequent and more recent the incidents, the higher the index value.

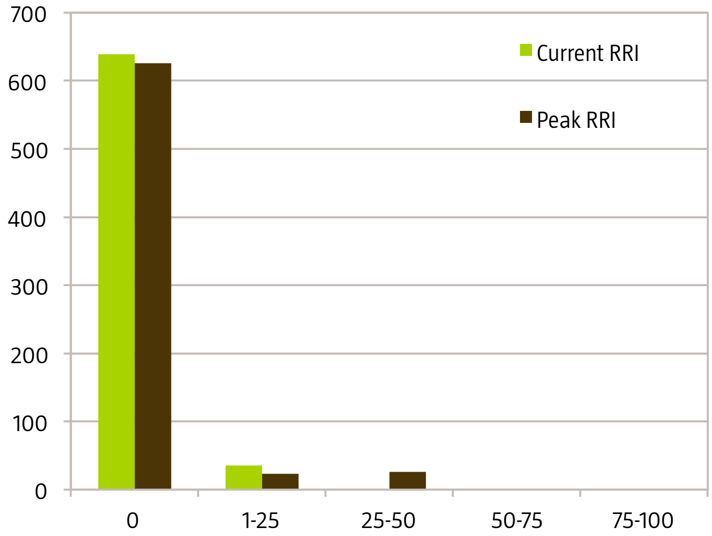
RepRisk also distinguishes between *current* and *peak* RRI. The *Current RRI* value indicates the current level of ESG reputational risk exposure of a company. The *Peak RRI* denotes the highest level of a company's ESG risk exposure in the past two years.

We ran portfolio companies in our PE funds through RepRisk to examine their ESG risk exposure. The results were encouraging. The majority of companies in the assessment universe had no exposure at all, and no companies revealed a high or very high exposure. However, several companies showed low or medium exposure, as illustrated in Figure 7.

Examples of incidents classified as low or medium risk included the following:

- Hackers stole personal information on employees, and former and current clients, from two portfolio companies.
- One portfolio company failed to take appropriate action against a known asbestos risk. Three workers were claimed have died from mesothelioma as a result.
- An oil-and-gas production platform owned by one of the portfolio companies caused a natural gas leak, which prompted an evacuation after workers lost control

Figure 7: The distribution of portfolio companies across different RRI ranges as of April 2015



Source: RepRisk

According to RepRisk, 58 out of 675 portfolio companies have, or once had, a positive RRI. This means that 58 companies have been mentioned in the media in connection with ESG issues, resulting in scores of between 9.61 and 22.92. Most of the recorded incidents occurred in the last two years. On average, portfolio companies in our assessment universe show lower ESG risk exposure than other companies monitored by RepRisk. Of the 58 portfolio companies affected by incidents, the average RRI is 9.61. This is analogous to a (very) low exposure.

Most incidents in the portfolio companies we monitor have been related to social issues in their supply chain and often occurred in India. Geographically, most ESG incidents were recorded in Asia and the least took place in Australia and Africa.

While low exposure is good, no exposure is better – and any trend towards increased ESG incidents should be identified and addressed. The results of our inaugural RepRisk analysis will be high on the agenda for dialogue with our PE fund managers this year. Furthermore, we will carefully monitor ESG incidents from now on and make them a standard part of our engagement with PE managers. In this way we believe we can get better insights into portfolio risk, which can inform discussions with PE managers on how they manage ESG risks. RepRisk analysis has also become a standard part of our pre-investment analysis for all new investments.

6 Reporting pilot with PRI

Over the years we have been writing this report, now in its ninth incarnation, we have seen GPs hit by an increasing number of ESG questionnaires. As a signatory of the United Nations Principles for Responsible Investment (PRI), we strive to contribute to the development of an industry standard aimed at decreasing the reporting burden of GPs in our engagement universe.

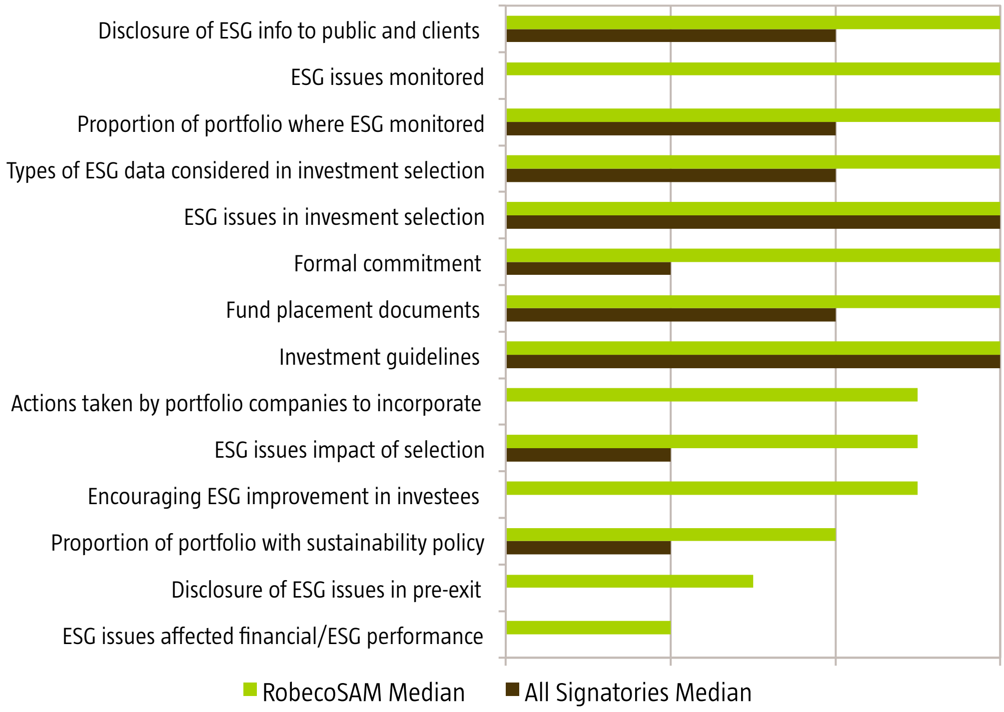
As a signatory of the United Nations Principles for Responsible Investment (PRI), we strive to contribute to the development of an industry standard aimed at decreasing the reporting burden of GPs in our engagement universe.

Our first step in this direction was to approach the Reporting & Assessment team at the PRI with a request to test their survey and reporting platform. The PRI team, PRI Board, the Advisory Council gave their support, and in December 2014 we began laying foundations for a pilot to test whether the platform would work for our monitoring purposes. Eight PE managers from our engagement universe came on board for the live test in the spring of 2015. Six of the participants were PRI signatories, and two were non-signatories.

PRI has designed a tailored interface on their reporting platform for RobecoSAM PE, so the pilot participants filled out a slightly adjusted version of the regular PRI survey. In the pilot we have only used the following three modules that are relevant for direct PE managers: Organizational Overview, Overarching Approach and Direct Private Equity. While the standard PRI survey consists of both mandatory and voluntary questions, all questions were made mandatory for RobecoSAM's pilot respondents. In addition, PRI gave us a document upload function, enabling respondents to attach supporting documents as evidence of a GP's ESG efforts. Indicators were dropped where not relevant for direct PE managers, and one or two *Additional Information* indicators were tweaked to create room for the respondents to provide examples of good ESG practices from portfolio companies

An additional advantage of using the PRI Reporting platform is that it enables us to compare the ESG performance of our GPs with the larger universe of PRI signatories investing in PE. Figure 8 provides an example of such a comparison. It shows the median scores for the mandatory indicators of the 226 PE managers that filled out the direct PE module of the standard PRI Survey in 2014, and compares them to the scores of RobecoSAM's pilot participants.

Figure 8: Median ESG indicator values for PRI signatories vs. RobecoSAM pilot participants



Source: PRI, RobecoSAM pilot participants

Upon the successful completion of the pilot we will carefully evaluate the whole process and its results. This information will be used as input for our discussion on how to organize the collection, monitoring and evaluation of ESG information from the PE managers in our ESG universe in future. This discussion will weigh the advantages of using an existing reporting platform against the flexibility of the proprietary questionnaire that we have now.

7 Involvement in international ESG initiatives

RobecoSAM PE actively participates in relevant responsible investment and sustainability initiatives organized by PRI, Europe Invest (formerly known as European Venture Capital Association, or EVCA), and other investor groups active in private equity. This section offers a brief overview of our current involvement.

In 2014, we contributed to the preparation of a guide for GPs titled *Integrating ESG In Private Equity*. The guide is the result of a joint effort of the PRI Working Group that was set up for this purpose. RobecoSAM PE was one of the LPs participating in this group. The guide aims to provide GPs with practical illustrations of ESG integration in daily practice. Its accompanying case studies explore the responses of leading PE managers to ESG at different stages of the investment process.

RobecoSAM PE was involved in the preparation of the *Responsible Investment Bibliography* published on the EVCA's website. We are a member of the EVCA Round Table on Responsible Investment, and have also participated in workshops and educational sessions run by the organization. We have attended the EVCA PE Value Creation Workshop *Putting a Financial Value on Sustainability Initiatives,* and its session on *The Management of Human Rights-Related Risks in Private Equity*.

We are currently participating in the Limited Partner Due Diligence Questionnaire (DDQ) Working Group set up by PRI. This group is working towards a guide that provides a list of ESG due diligence questions, which LPs could ask GPs pre-investment. The guide aims to encourage a consistent industry approach towards LP due diligence on ESG, by pulling together existing due diligence resources into one adaptable master document. The initiative can be seen as part of an ongoing effort to standardize information requests by LPs. PRI expects to finalize the DDQ questionnaire, with the accompanying guidance, in the fall of 2015.

8 Looking ahead

Since our first annual ESG assessment and report, RobecoSAM Private Equity's efforts to assess and improve the ESG performance of PE fund managers has developed encouragingly. We are proud of the continuing trend towards better ESG management within the funds in the RobecoSAM universe. As increasing numbers of funds join us on the ESG journey, and mature into ESG role models, it is our hope that ESG best practices become the market norm.

Our continued evolution of our approach to ESG integration and engagement defines our goal of adding value to our investors.

This is, however, an ongoing mission. Our continued evolution of our approach to ESG integration and engagement defines our goal of adding value to our investors. Our reporting and monitoring options continue to grow, with schemes considered for the future including our pilot with PRI. The additional insights we hope to gain will help us make better choices in the medium and long run.

While striving to remain at the forefront of sustainability investing in private equity, we still see room for improvement in the integration of ESG analysis in our due diligence and monitoring process. Monitoring and engagement, areas in which we are already very strong, are currently the focus of our ESG efforts. They will remain an important element of our approach in the future. However, we also intend to make better use of the extensive sustainability knowledge available within RobecoSAM and Robeco, and put more emphasis on the specific sustainability issues in the portfolios of the participating funds.

Standardization is one of our key concerns going forward. The reporting framework developed by PRI has the potential to contribute strongly to the goal of standardization, and we aim to use it where it suits our engagement objectives. Further to the standardization theme, in future we may also look at aligning sector and portfolio company ESG information more closely with the reporting systems of GPs.

Finally, we are convinced the PE industry could benefit significantly from additional empirical evidence of the relationship between ESG and financial performance. We would like to highlight this relationship with innovative and useful contributions. We look forward to a year full of ESG challenges, in a market where ESG factors continue to grow in importance.

About the authors

Authors

Silva Deželan, Nicky van 't Hof and Arend Lakke, Rabobank Sustainability Department

Input by

Niels Bardelmeijer, RobecoSAM Private Equity

This report is a joint initiative of RobecoSAM Private Equity and Rabobank Sustainability Department.

RobecoSAM Private Equity

RobecoSAM Private Equity offers core and satellite investment capabilities with a focus on mainstream and resource efficiency to institutional investors. Mainstream strategies target high-quality investments in the mid-market segment with a focus on Europe. Resource efficiency strategies benefit from the research and investment expertise of RobecoSAM, a company with almost 20 years' experience managing thematic strategies, and a focus on identifying opportunities that stem from the growing demand for finite resources. RobecoSAM Private Equity is based out of both RobecoSAM, the investment specialist focused exclusively on Sustainability Investing, in Zurich, and Robeco, in Rotterdam. Through RobecoSAM Private Equity's diverse offerings, institutional clients can gain exposure to primary private equity funds, secondary private equity funds, and co-investments in selected private companies. RobecoSAM Private Equity is a leader in ESG integration, its launch of RSPE C.V. and Robeco Sustainable Private Equity Fund, L.P in 2004 making it one of the first in the industry to launch funds applying an ESG engagement policy. RobecoSAM Private Equity continues to benefit from RobecoSAM's long-standing expertise in analyzing and identifying solution driven companies. The first private equity programs were established in 2001 with Robeco Global Private Equity C.V., and Robeco European Private Equity C.V. RobecoSAM Private Equity has since launched multiple generations of funds and customized mandates across various strategies and vintage years.

Rabobank

Rabobank is an international financial services provider operating on the basis of cooperative principles. It offers retail banking, wholesale banking, asset management, leasing, and real estate services. Rabobank Group is comprised of 121 independent local banks plus Rabobank Nederland, their central organization, and a number of subsidiaries. Overall, Rabobank Group has an employee base of 52,000 employees (in full time equivalents), who serve about 10 million clients in 41 countries, and total assets of EUR 681.1 billion (as of December 31, 2014). Rabobank began as a farmer's co-operative bank in 1898, and green issues have been ingrained in the culture from the start. Sustainability remains one of Rabobank's core values today. The bank has won many accolades for its sustainability management and reporting. Rabobank aligns its sustainability ambitions with those of its customers, with whom it jointly strives for a healthy balance between wealth and wellbeing as it spearheads the themes of sustainable agriculture and food production, and vital communities.

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