

# Fiduciary duty and environmental and social themed investing in the US

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This note summarises key points from a [recorded discussion](#) on fiduciary duty and environmental and social themed investing with two pension funds based in the US.

## Participants



Keith Johnson, Head of Institutional Investor Services, Reinhart Boerner Van Deuren s.c.



Michael Lohmeier, Director, Wespath Investment Management (General Board of Pension and Health Benefits of The United Methodist Church)

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## Thinking differently about fiduciary duty

The participants questioned several aspects of how investors typically think about fiduciary duty. First, investors tend to focus on the duty of prudence, the standard of care. This involves observing and matching what peers are doing. Fiduciary duty also entails a duty of loyalty and a duty of impartiality - treating current and future obligations to pension fund beneficiaries on an impartial basis and trying to balance those. Second, fiduciary duty is closely associated with Modern Portfolio Theory. Such a focus on immediate returns can hide certain risks and opportunities to pension funds. Fiduciary duty is an evolving concept, and as such the focus on Modern Portfolio Theory may change, particularly given the economic crises of the last few years.

*Fiduciary duty is an evolutionary concept which responds to the circumstances of the economy and society around investors. I remember the days when it was considered imprudent for investors to invest in public equity.*

Keith Johnson

## Investing for financial performance and social benefit

Michael Lohmeier described how the Wespath Positive Social Purpose Lending Program (see box below) has provided short- and long-term financial returns as well as social benefits. These investments have added diversification to their portfolio, thereby reducing overall risk. Wespath has also found that the returns from these investments seem to be less volatile than those from

other investments.

The [Wespath Positive Social Purpose \(PSP\) Lending Program](#) was launched in 1990 with the goal of promoting affordable housing and community development for disadvantaged communities, while delivering competitive financial returns. From its original US \$25 million commitment to affordable housing, the program has grown steadily and now has approximately US \$750 million invested. Under the program, Wespath acquires senior positions in mortgage loans from independent third parties, usually non-profit organisations. The completed housing units provide homes for individuals and families earning less than the area's median income.

Long-term mortgages are a good duration match for annuity liabilities. Wespath has found that providing these for affordable housing and community development is less well known than long-term corporate debt where pricing has been driven up by investors seeking similar asset characteristics. Moreover, Wespath has been able to expand the investable universe, providing greater diversification, by investing in a portion of the real estate market that isn't available in publicly traded securities or traditional alternative investments.

Wespath also invests for social benefit internationally, through microfinance. Part of the investment case is that they can get access to rapidly growing economies in Africa that they can't get elsewhere. Wespath finds that traditional managers have not been able to provide similar investment opportunities in Africa.

Keith Johnson described the rationale for creating the Wisconsin private debt programme. In looking beyond the traditional financial analysis, the pension fund saw two important factors influencing its ability to deliver stable long-term benefits: continued contributions from pension beneficiaries and the economic health of the participating employers. It also saw that this programme could boost community support for the fund, which helps to ensure continued contributions from current and future pension fund beneficiaries. The programme also supports the growth of the local economy, generating further tax revenues for the public employers who participate in the fund.

The [Wisconsin Private Debt Program](#) has been in place since the 1960s, providing debt financing to smaller businesses who are not able to engage with larger investors. The programme provides long-term, senior fixed-rate loans and subordinated loans to operating businesses that can demonstrate the ability to repay their debt.

## Cost and benefit

The participants discussed the issue of additional costs and resources required to run the two programmes. Both examples involved building significant in-house expertise over a number of years. However, this relatively high up front cost paid off in the longer term as the expertise, once developed, is repeatable and can be leveraged to improve financial performance.

*We can leverage our knowledge to identify areas of investment that others won't see. We are able to understand the risk and reward trade-off and negotiate more favourable terms. We also benefit from our in-house expertise to understand how government interventions can reduce risk and potentially provide a better opportunity for our participants.*

Michael Lohmeier