Social Investment Forum

SOCIALLY RESPONSIBLE INVESTING: TOP 10 QUESTIONS & ANSWERS

1. How large is the socially responsible investing (SRI) marketplace? Is it growing? Where is the growth taking place?

The 2007 *Report on Socially Responsible Investing Trends in the United States* revealed that through December 31, 2006, socially responsible investing (SRI) has been expanding at a much faster pace than the broader universe of all investment assets under professional management. The 2007 *Trends* report, published by the Social Investment Forum Foundation, identified **$2.71 trillion in total assets under management using one or more of the three core SRI strategies – screening, shareholder advocacy, and community investing**. In the past two years, social investing has enjoyed healthy growth from the $2.29 trillion documented in the 2005 *Trends* report. (The next biennial edition of the Report, for 2009, will be published in early 2010.)

The report found that, from 2005 to 2007, SRI assets increased more than 18 percent while all investment assets under management edged up by less than 3 percent. At the start of 2007, nearly one out of every nine dollars under professional management in the United States was involved in socially responsible investing – 11 percent of the $25.1 trillion in total assets under management tracked in Nelson Information's Directory of Investment Managers.

Highlights of SRI by key area include the following:

- *SCREENED FUNDS:* Assets in all types of socially and environmentally screened funds – including mutual funds, exchange-traded funds (ETFs), closed end funds, and other pooled products and alternative investments – rose to $201.8 billion in 260 funds by 2007, a 13 percent increase over the $179.0 billion in the 201 tracked in 2005. Eight socially and environmentally screened ETFs with $2.25 billion in total net assets were available through the end of 2006 – the first time SRI-focused ETFs have been a factor in a Social Investment Forum Foundation *Trends* report.

- *INSTITUTIONAL INVESTORS:* At more than $1.9 trillion in assets, socially screened separate accounts managed for institutional investors and high net worth individual clients constituted the bulk of SRI assets tracked in the 2007 report, up 28 percent from $1.5 trillion in 2005. Institutional investors have also used the stock they hold to increasingly participate in shareholder resolutions.

- *SHAREHOLDER RESOLUTIONS:* The average level of shareholder support for resolutions on social and environmental issues increased 57 percent from 9.8 percent in 2005 to 15.4 percent in 2007, a record high.

- *COMMUNITY INVESTING:* Assets in community investing institutions rose nearly 32 percent from $19.6 billion in 2005 to $25.8 billion in 2007.

2. What are the major elements of socially responsible investing?

Socially responsible investing refers to the following core activities: *screening, shareholder advocacy, community investing.* Here is what you need to know about each of these key areas:

- **Screening** includes both positive and negative "filters." Screening is the practice of evaluating investment portfolios or mutual funds based on social, environmental and good corporate governance criteria. Screening may involve including strong corporate social responsibility (CSR) performers, avoiding poor performers, or otherwise incorporating CSR factors into the process of investment analysis and management. Generally, social investors seek to own profitable companies that make positive contributions to society. “Buy” lists may include enterprises with, for example, good employer-employee relations, strong environmental practices, products that are safe and useful, and operations that respect human rights around the world. Some social investors avoid investing in companies whose products and business practices are harmful to individuals, communities or the environment. **It is a common mistake to assume that SRI “screening” is simply exclusionary, or only involves negative screens.** In reality, SRI screens are being used more and more frequently to invest in companies that are leaders in adopting clean technologies and exceptional social and governance practices.

Shareholder advocacy involves socially responsible investors who take an active role as the owners of corporate America. These efforts include talking (“dialoguing”) with companies on issues of social, environmental or governance concern. Shareholder advocacy also frequently involves filing and co-filing shareholder resolutions on such topics as executive pay, climate change, political contributions, gender/racial discrimination, pollution, problematic labor practices and a host of other issues. Shareholder resolutions are then presented for a vote to all owners of a corporation. The process of dialogue and filing shareholder resolutions generates investor pressure on company management, often garners media attention, and educates the public on social, environmental and labor issues. Such resolutions filed by SRI investors are aimed at improving company policies and practices, encouraging management to exercise good corporate citizenship and promoting long-term shareholder value and financial performance. Divestment can be the end result in situations where other shareholder actions have not produced results.

- **Community Investing** directs capital from investors and lenders to communities that are underserved by traditional financial services institutions. Community investing provides access to credit, equity, capital and basic banking products that these communities would otherwise lack. In the United States and around the world, community investing makes it possible for local organizations to provide financial services to low-income individuals and to supply capital for small businesses and vital community services, such as affordable housing, child care and healthcare.

3. Is the performance of SRI funds competitive with mainstream funds and with their benchmarks?

Socially responsible investors are like all other investors in seeking a competitive financial return on their investments. A growing number of academic studies have demonstrated that SRI mutual funds perform competitively with non-SRI funds over time. The evidence is also clear that socially responsible investors do **not** have to pay more to align their investments with their values, or to avoid companies with poor environmental, social or governance practices.

In October 2007, the *“Demystifying Responsible Investment Performance”* report issued by the United Nations Environment Programme Finance Initiative (UNEP FI) analyzed 20 influential pieces of academic work and 10 key broker studies exploring links between different approaches to responsible investment and investment performance. The comprehensive UNEP FI found that SRI investment strategies are competitive with non-SRI strategies from a performance standpoint.

More than 20 studies demonstrating that SRI mutual fund performance is comparable to that of non-SRI funds can be found at www.sristudies.org — a compendium of major academic studies on SRI. Several of these peer-reviewed and published studies have been awarded the prestigious Moskowitz Prize, available at http://www.socialinvest.org/resources/research/.

Another indication of the competitive performance of SRI funds may be seen in SRI indexes. These indexes are designed to be benchmarked to non-SRI indexes, such as the S&P 500. The longest-running SRI index, the Domini 400, was started in May 1990. It has continued to perform competitively — the

Domini 400 with average annualized total returns of 8.43 percent through December 2008 compared with 7.78 percent for the S&P 500.

For up to date information on the performance of SRI funds managed by members of the Social Investment Forum, visit the Mutual Fund Performance Chart, at http://www.socialinvest.org/resources/mfpc/.

4. What are responsible investors doing to invest in clean energy?

Socially responsible investors are leading the way in terms of investments in clean energy and other green technology. In October 2008, the Social Investment Forum reported that mutual fund families and financial professionals offering clean energy and "green technology" investment vehicles to investors are seeing strong demand for such offerings and plan to make available several new related investment vehicles by the end of 2009.

In detailed findings from a cross-section of 14 SIF members, a Social Investment Forum survey found:

- 100 percent of the respondents reported "clean energy/tech investing" demand is up among clients.
- 72 percent either responded "yes" (36 percent) or "possibly" (36 percent) when asked if they "have plans to introduce new clean energy/tech investing opportunities before the end of 2009." (Based on the responses, this would result in a total of 10 or more possible new clean energy/green tech investment vehicles, including several mutual funds, ETFs and indexes.) Only four of the respondents indicated that they have no such plans.
- 17 mutual funds or other investment opportunities offered by the respondents now focus "exclusively on clean energy/tech investing." The assets reported for these investment vehicles are in excess of a quarter of a billion dollars.
- Eight mutual funds or other investment opportunities focused "exclusively or partially on clean energy/tech" were identified as having been launched since January 1, 2007.

5. What new products are there in the world of SRI?

The rise of responsibly invested Exchange-Traded Funds (ETFs) is the latest illustration of how SRI continues to grow and evolve. ETFs involve investment companies that aim to achieve the same return as a particular market index.

An ETF is a large bundle of securities which tracks a certain class of assets (stocks, bonds, real estate, commodities, etc.), similar to an index mutual fund. Though ETFs are built like index funds, they are treated comparably to a stock on the market: instead of being bought or sold based on the fixed closing price for the day, like a mutual fund, ETFs can be traded all day long. This offers traders more maneuverability and flexibility in their investment strategy.

According to the Social Investment Forum's 2007 *Trends* report, eight socially and environmentally screened exchange-traded funds with $2.25 billion in total net assets were identified for the first time in the 2007 edition. During 2007, other ETFs were launched to track indices addressing a variety of social and environmental concerns related to water, clean technology, alternative energy, and the crisis in the Sudan. Although ETFs accounted for only 1 percent of the total assets of all socially screened funds at the beginning of 2007, they promise to be a dynamic catalyst for SRI growth in the future.

Also new within the SRI world are Certificates of Deposit Account Registry Service (CDARS), an investment network that helps smaller community banks pool resources, exchange funds, and support local lending initiatives. More than 1,400 financial institutions in the United States have joined CDARS.

The basic insurance limit has been $100,000, but has been temporarily increased to $250,000, though this expires at the end of 2009. Within the CDARS network, they are able to access up to $50 million in FDIC protection on CD investments, helping small banks attract larger deposits. FDIC insurance on the deposits range from $10,000 to $50 million. CDARS is open to all investors with deposits in a community bank. Investors can select maturities ranging from four to 260 weeks, depending on investment needs. Visit www.cdars.com to learn more.

6. What evidence is there that SRI shareholder resolutions have an impact?

Advisory shareholder resolutions are crucial tools for encouraging U.S. companies to address key environmental, social and corporate governance (ESG) issues. By filing resolutions, which may then proceed to a vote by all shareholders in the company, active shareholders bring important issues to the attention of company management, often winning media attention and educating the public as well. Moreover, resolutions need not come to a vote to be effective. The process of filing often prompts productive discussion and agreements between the filers and management that enable the filers to withdraw their resolutions.

In 2007 and 2008, members and allies of the Social Investment Forum filed approximately 300 shareholder resolutions annually on social and environmental issues for consideration at U.S. companies' annual meetings. Included in this group were resolutions asking firms for better disclosure and oversight of their political contributions and activities. Other recent social and environmental resolutions have addressed equal employment opportunity, climate change, global labor standards and sustainability reporting. The Interfaith Center on Corporate Responsibility (ICCR) and the Ceres coalition play a major role in coordinating many of these resolutions.

In addition, investors have filed resolutions questioning companies on their governance structures and practices, particularly those involving board composition, executive pay and responsiveness to shareholders.

Here are just a few of the many examples of how shareholder resolutions make a difference.

- Since 2006, a coalition of institutional and individual investors with combined assets of more than $1 trillion have urged scores of companies to adopt an advisory vote on executive compensation, or "Say on Pay," a common practice in British corporate governance. These investors want an official channel for shareholders to express their concerns to corporate boards about huge pay packages that seem unrelated to financial performance. In response to these proposals, such major companies as Blockbuster, Intel, Ingersoll-Rand, Motorola and Verizon will each give shareholders the Say on Pay vote in 2009. Additionally, more than 100 companies will face say-on-pay resolutions in the 2009 shareholder season and in a sign of the growing impact of shareholder advocacy, the U.S. Congress enacted a stimulus bill in February 2009 that will require an estimated 400 financial institutions to institute say on pay votes.

- In recent years, shareholders, including public pension funds and socially responsible investment firms, have been able to withdraw dozens of resolutions asking companies to pledge not to discriminate against employees based on their sexual orientation when the companies have agreed to expand their non-discrimination policies to include this guarantee.

- In 2003, American Electric Power received a resolution from the State of Connecticut asking it to consider the economic risk of its carbon dioxide and other emissions. It won the support of 27 percent of the shares voted, one of the highest for a climate-related proposal at that time. The next year, American Electric Power had a subcommittee of its board focus on climate change. Since American Electric Power issued its report on climate change, many other companies have followed suit after shareholders have filed resolutions on climate change risks.

- SIF member Green Century Capital Management raised concerns about the safety of the chemical Bisphenol A and other suspected endocrine disrupters in a resolution filed for Whole Foods Market's 2006 annual meeting. After dialogue with Green Century and just prior to a vote on the resolution, the company announced that it would remove baby bottles and other products that contain BPA from its shelves as part of a new corporate policy to minimize customers' exposure to hormone-disrupting chemicals.

- In 2007, a resolution from SIF member Christian Brothers Investment Services asking Dillard's to report on sustainability issues was supported by more than 46 percent of the shares voted. Later that year, Dillard's posted to its Web site a detailed labor and human rights policy in which it endorsed all the International Labor Organization's core conventions and pledged to monitor its entire supply chain using independent organizations. When CBIS approached the company in 2008, the company agreed to report by its 2009 annual meeting on the results of its factory audits and the actions it has taken to correct any violations to its labor standards.

- Concerned shareholders, led by the Center for Political Accountability (CPA), a SIF member, have pressed companies to exercise proper oversight to ensure that political contributions made with corporate funds serve the best interests of the firms and their shareholders. Since the start of this shareholder campaign in 2004, the CPA and its allies have persuaded 52 large companies, including 35 in the S&P 100, to disclose and require board oversight of their political spending with corporate funds.

7. What are the major trends in SRI shareholder advocacy?

Shareholder advocacy by SRI investors is on the rise, based on two key indicators.

One, the number of shareholder resolutions filed at U.S. companies on environmental and social issues has risen over the last decade from an annual average of 240 in 1999-2000 to more than 380 in 2007-2008.

More important, the average support that shareholder advocates are receiving for shareholder resolutions on social and environmental issues is rising. In 2007, the 195 shareholder resolutions that came to votes on social and environmental issues won average support of 15.3 percent, an all-time record, according to records maintained since 1973 by SIF member RiskMetrics Group and its predecessors. In 2007 and 2008, a handful of resolutions even won majority support despite management opposition, a major breakthrough.

Certain categories have done particularly well in attracting broad-based investor support in recent years:

- **"Say on pay."** Since 2006, hundreds of companies have been prodded by shareholders into holding votes on CEO compensation, with votes in favor routinely topping 40 percent and even 50 percent in some cases. In 2009, about 100 companies will face shareholder "say on pay" votes.

- **Climate change**: In 2008, for the first time, proposals asking companies to consider how to reduce their greenhouse gas emissions and otherwise prepare for a carbon-constrained regulatory environment won average support of more than 20 percent in a vastly expanded campaign that saw 20 proposals come to votes through June 30, 2008.

- **Toxic chemicals**: Shareholder advocates who have been pressing companies to review and reduce the use of toxic chemicals in consumer products also won vote support, on average, of well over 20 percent, as they stepped up their campaign in 2008.

- **Sustainability reporting**: Calls for sustainability reporting are attracting substantial support. In 2008, the seven proposals that came to votes through June 30 won average support of 25 percent; in 2007, the 10 resolutions that came to votes earned average support of 27 percent.

- **Non-discrimination**: Proposals asking companies to expand their non-discrimination policies, and especially to guarantee non-discrimination on the basis of sexual orientation or gender identity, continue to win high support from investors. In 2007, such proposals averaged support of 33 percent. In 2008, two such proposals won support from more than 50 percent of the shares voted (excluding abstentions).

- **Oversight of corporate political contributions and lobbying**: Resolutions asking companies to disclose the contributions they make with corporate funds for political purposes and to establish board-level oversight for these payments, continue to gain favor with investors. Average support for these proposals grew from just 10 percent of the shares voted in 2004 and 2005 to 24 percent in 2007 and 25 percent in the first half of 2008.

8. Who are socially responsible investors?

Today, nearly one out of every nine dollars under professional management in the United States is involved in socially responsible investing – 11 percent of the $25.1 trillion in total assets under management tracked in Nelson Information's Directory of Investment Managers.Socially responsible investors comprise individuals and institutions, such as universities, hospitals, foundations, insurance companies, public and private pension funds, nonprofit organizations, and religious institutions. Institutional investors represent the largest and fastest growing segment of the SRI world.

Many SRI investors are members of the Social Investment Forum, the national nonprofit membership association dedicated to advancing the concept, practice, and growth of socially and environmentally responsible investing. SIF counts among its 500 members mutual fund companies, investment management and advisory firms, pension funds, foundations and other asset owners, research firms, financial planners and advisors, brokers-dealers, banks, credit unions, community development organizations, and non-profit associations. (To see our membership, go to http://socialinvest.org/directory/).

9. Is there growing demand among individual and institutional investors for SRI products? What is driving that demand?

There is ample evidence of expanding demand for SRI among individual and institutional investors.

The 2007 *Trends* report from the Social Investment Forum Foundation found that assets in all types of socially and environmentally screened funds – including mutual funds and exchange-traded funds (ETFs) – rose to $201.8 billion in 260 funds in 2007, a 13 percent increase over the $179.0 billion in the 201 tracked in 2005. Eight socially and environmentally screened ETFs with $2.25 billion in total net assets were available through the end of 2006 – the first time SRI-focused ETFs have been a factor in a Social Investment Forum Trends report.

A 2007 survey sponsored by the Social Investment Forum and Mercer Consulting on defined contribution (DC) retirement plans found that of the DC plan respondents that were not already offering SRI options to investors, 41 percent expected to be doing so within three years.

On the institutional investor side of the equation, a growing concern about climate change and its risk for portfolios is intensifying the interest in SRI among money managers. Investor demand is growing for portfolio opportunities in clean and green technology, alternative and renewable energy, green building and responsible property development, and other environmentally driven businesses.

A large and expanding number of institutional investors are actively supporting shareholder resolutions on social, environmental and corporate governance issues and joining investor coalitions, such as the Investor Network on Climate Risk, to make their concerns known about the risks and opportunities associated with issues such as climate change. In December 2008, for the first time ever, an investor delegation personally presented a call for action on climate change to world leaders—at the UN climate conference in Poznan, Poland. The Statement, signed by 152 global investors worth over $9 trillion, calls on world leaders to negotiate a strong and binding successor to the Kyoto Protocol to ensure that investors receive the market signals critical to funding the transition to a low-carbon economy. Three leading investor groups on climate change, the European Institutional Investors Group on Climate Change (IIGCC), the US-based Investor Network on Climate Risk (INCR), and the Investor Group on Climate Change (IGCC) in Australia and New Zealand, coordinated the statement.

Additionally, increasing numbers of institutional investors, fund families and money managers are incorporating criteria related to the crisis in the Sudan into portfolio management and shareholder advocacy, whether through targeted divestment or active engagement with companies exposed to the risks of doing business in such a volatile, repressive regime.

10. How can SRI investors find products and information about socially responsible investing?

The website of the Social Investment Forum is one of the best places for investors to learn more about socially responsible investing. Among the key SIF resources available to investors are the following:

- Socially Responsible Investing (SRI) Facts.
- Facts about SRI Performance.
- SRI Mutual Funds Charts.

Not sure where to start? Try: http://www.socialinvest.org/resources/sriguide/srifacts.cfm.

Individual investors can also find information on socially responsible investing at http://www.Green AmericaToday.org.