US SIF
The Forum for Sustainable and Responsible Investment

Sustainable and Responsible Investing

Top 10 Frequently Asked Questions and Answers

1. What is sustainable and responsible investing or "SRI?" What key areas does it cover?

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

- **ESG incorporation**—also known as **screening—**includes both positive and negative "filters." ESG incorporation is the practice of evaluating investment portfolios or mutual funds based on environmental, social and corporate governance (ESG) criteria in addition to traditional financial 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, sustainable and responsible investors seek to own profitable companies that make positive contributions to society. "Buy" lists may include enterprises with good employer-employee relations, strong environmental practices, products that are safe and useful, and operations that respect human rights around the world. Some sustainable and responsible 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 frequently to invest in companies that are leaders in adopting clean technologies and exceptional social and governance practices—also known as positive screens.

- **Shareholder advocacy** involves sustainable and responsible investors who take an active role as the owners of stock in corporations. 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. Through such resolutions, SRI investors aim to improve company policies and practices, encourage management to exercise good corporate citizenship and promote long-term shareholder value and financial performance. The process of dialogue and filing shareholder resolutions generates investor pressure on company management, often garners media attention, and educates the public on these issues.

- **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.

2. Who are sustainable and responsible investors?

Sustainable and responsible investors comprise individuals, including average investors to very high net worth individuals and family offices, as well as institutions, such as universities, hospitals, foundations, 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 US SIF: The Forum for Sustainable and Responsible Investment. US SIF is the US membership association for professionals, firms, institutions and organizations engaged in sustainable and responsible investing. US SIF and its members advance investment practices that consider environmental, social and corporate governance criteria to generate long-term competitive financial returns and positive societal impact. US SIF's members include investment management and advisory firms, mutual fund companies, research firms, financial planners and advisors, broker-dealers, banks, credit unions, community development organizations, non-profit associations, and pension funds, foundations and other asset owners. (To see our membership, go to http://ussif.org/directory/).

3. How large is the sustainable and responsible investing (SRI) marketplace? Is it growing? Where is the growth taking place?

US SIF Foundation's 2010 *Report on Socially Responsible Investing Trends in the United States* revealed that at the start of 2010, sustainable and responsible investing had been expanding at a much faster pace than the broader universe of all investment assets under professional management. The report found that, from 2007 to 2010, SRI assets increased more than 13 percent while all investment assets under management edged up by less than 1 percent. The report identified $3.07 trillion in total assets under management using one or more of three SRI strategies:

- The incorporation of environmental, social and governance (ESG) factors into investment analysis and portfolio construction
- The filing or co-filing of shareholder resolutions on ESG issues and
- Deposits or investments in banks, credit unions, venture capital funds and loan funds that have a specific mission of community development.

Today, nearly one out of every eight dollars under professional management in the United States is involved in sustainable and responsible investing –12.2 percent of the $25.2 trillion in total assets under management tracked by Thomson Reuters Nelson.

The 2010 *Trends* report provided the following highlights of SRI by key areas:

- **Funds and money managers:** Assets in all funds that incorporate ESG criteria– including mutual funds, exchange-traded funds (ETFs), closed end funds, and other pooled products and alternative investments – rose to $569 billion in 493 funds by 2010, a 182 percent increase over the $202 billion in the 260 funds tracked in 2007. Included in this number were 177 **alternative investment vehicles**, ranging from social venture capital and double- and triple-bottomline private equity funds to hedge funds and responsible property funds, which had estimated assets and capital commitments totaling $37.8 billion. This is up dramatically from the 46 alternative investments with $5.3 billion in the ESG space tracked for the first time in 2007. Twenty-six ETFs, with $4.0 billion in total net assets, were available at the start of 2010 that incorporate ESG criteria.

In addition, money managers with $638 billion in assets filed or co-filed shareholder resolutions on ESG issues from 2008 through 2010. (More than three-quarters of these firms also practice ESG incorporation.)

- **Institutional investors**: With $2.3 trillion in assets involved in one or more SRI strategies, institutional investors dominate the SRI universe. A wide range of institutions, including public employee retirement plans, government-sponsored college savings plans, philanthropic foundations, educational endowments, and faith-based investors, are the primary owners of $2.03 trillion in assets to which they apply ESG criteria. Institutional investors have also used the stock they hold to increasingly participate in shareholder resolutions: in 2010, $858.8 billion was controlled by institutions that file or co-file resolutions on ESG issues.

- **Community investing**: Assets in banks, credit unions, loan funds and venture capital funds with an explicit mission of community development rose from $25.8 billion in 2007 to $41.7 billion at the start of 2010.

US SIF Foundation's December 2009 survey, *Investments Consultants and Responsible Investing,* concluded that client interest in ESG and responsible investing is here to stay, with all of the 40 responding investment consulting firms reporting they did not believe client interest in SRI would decrease, and nearly 90 percent saying they believe client interest in SRI will grow over the next three years. The surveyed consultants held these views regardless of their current level of involvement in ESG services or their opinions about the impact of ESG integration strategies on portfolio performance. Some of the factors respondents cited that they believed would drive this client interest are climate change, growing public interest in "green" issues and social responsibility, and the embrace of mission-related investing by foundations.

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 (INCR), 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, called 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.

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

Sustainable and 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 sustainable and 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. This comprehensive review found that SRI investment strategies are competitive with non-SRI strategies from a performance standpoint.

In November 2009, Mercer issued a report, *Shedding Light on Responsible Investment: Approaches, Returns and Impacts*, in which it reviewed a further 16 academic studies on SRI and financial performance that were published after the 2007 UNEP FI review. It found that of these 36 studies, published between 1995 and 2009, 20—more than half—found evidence of a positive relationship between ESG factors and financial performance, and only three found evidence of a negative relationship. It concluded that "a variety of factors, such as manager skill, investment style and time period, is integral to how ESG factors translate into investment performance; therefore, it is not a 'given' that taking ESG factors into account will have a uniform impact on portfolio performance, and we expect significant variation across industries."

A compendium of academic studies on SRI funds can be found at www.sristudies.org. Several of these peer-reviewed and published studies have been awarded the prestigious Moskowitz Prize, available at http://www.ussif.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—now the MSCI KLD 400—was started in May 1990. It has continued to perform competitively —with average annualized total returns of 9.24 percent through September 2010 compared with 8.68 percent for the MSCI USA index.

In January 2010, US SIF reviewed the 160 member mutual funds on its Mutual Fund Performance Chart and found that a vast majority of the funds—65 percent—outperformed their benchmarks in the calendar year 2009, most by significant margins. Particular standouts on SRI mutual fund performance were the 73 large cap funds, the largest single category of US SIF member funds, where nearly three out of four (72.6 percent) outperformed the S&P 500. On average, large cap SRI funds bested the S&P 500 by more than 6 percentage points. A majority of the large cap funds offered by US SIF members also outperformed the S&P 500 over three years and over 10 years.

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

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

Sustainable and responsible investors are leading the way in terms of investments in clean energy and other green technology. As of March 31, 2011, nearly two thirds of the 149 SRI mutual funds offered by US SIF members reported that they look for companies with positive records relating to climate change or clean technology in developing their portfolios. For more information on funds investing in clean energy, please visit US SIF's Mutual Fund Performance Chart: http://www.ussif.org/resources/mfpc/screening.cfm.

6. What are the new SRI products?

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.

US SIF Foundation's 2010 *Trends* report identified 26 socially and environmentally screened exchange-traded funds with $4.0 billion in total net assets at the start of 2010. This is an increase of 225 percent since the report began tracking ETFs in 2007. That year, 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.

Alternative investments have become one of the most dynamic segments within the ESG investing space. Although still a relatively small slice of the overall fund universe, representing only 5 percent of the $692 billion identified here, the number of alternative investment vehicles has grown more rapidly than any other type of funds tracked. At least 125 venture-capital and private equity funds, many focusing on cleantech and renewable energy, have now emerged. Private equity funds are being managed not only by "patient capitalists" and "double-bottom-line" investors but also by some of the leading Silicon Valley venture capital firms whose principals recognize a compelling business case around sustainability themes.

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 3,000 financial institutions in the United States have joined CDARS in order to offer customers a secure and convenient way to invest in large-dollar, FDIC-insured certificates of deposit. The FDIC currently limits insurance to a maximum of $250,000 per customer per bank. However, within the CDARS network, customers are able to access up to $50 million in FDIC protection on CD investments by signing an agreement with a single bank, which then invests the funds in the

CDARS network, helping small banks attract larger deposits. Investors can select maturities ranging from four to 260 weeks, depending on investment needs. Visit www.cdars.com to learn more.

7. 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.

From 2008 through the first half of 2010, more than 200 institutional investors and money managers collectively controlling a total of at least $1.5 trillion in assets filed or co-filed shareholder resolutions on ESG issues. 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, human rights 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. In recent years, these proposals have been gaining traction, and frequently receive majority support.

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

- In 2010, Newground Social Investment withdrew its proposal at TJX when the company agreed to produce a full sustainability report by 2011, disclose its climate risks and create a U.S. team with the sole purpose of improving the company's sustainability performance. The agreement followed several years of dialogue between TJX and investors.

- From 2006 through 2010, a coalition of institutional and individual investors with combined assets of more than $1 trillion urged U.S. companies to adopt an advisory vote on executive compensation, or "Say on Pay," a common practice in British corporate governance. These investors wanted an official channel for shareholders to express their concerns to corporate boards about huge pay packages that seem unrelated to financial performance. In 2009, the 76 shareholder requests for Say on Pay procedures received the average support of no less than 46 percent of the shares voted at the target companies, and 24 gained majority votes. The campaign received a further boost in 2009 when the U.S. Congress enacted a stimulus bill that required financial institutions that had received government funds under the Troubled Assets Relief Program (TARP) to institute Say on Pay votes. The Dodd-Frank financial reform law, enacted in 2010, now requires publicly traded companies to allow an advisory shareholder vote on executive pay at least once every three years.

- In recent years, shareholders, including public pension funds and sustainable and 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.

- US 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 US 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 website 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.

8. 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 2007-2009.

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 US SIF member RiskMetrics Group and its predecessors. US SIF member Sustainable Investments Institute reports that average support for such proposals continues to rise: to more than 18 percent in 2010 and to approximately 20 percent during the first half of 2011. So far in 2011, five shareholder proposals on environmental and social issues have received majority support, compared with six in the three previous years combined.

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: in 2009, 76 proposals came to votes and averaged 46.1 percent support, with 24 majority votes recorded. Additionally, as of mid-2010, approximately 75 companies had voluntarily agreed to implement an advisory vote on pay. Moreover, the

Dodd-Frank financial reform bill requires publicly traded companies to allow an advisory vote on pay at least every three years.

- **Climate change**: In 2009, for the first time ever, a shareholder proposal related to climate change risk won majority support: at electric company Idacorp, a proposal from Trillium Asset Management and As You Sow Foundation asking it to set greenhouse gas emission reduction goals won the support of 51.2% of the shares voted. Meanwhile, in 2010, proponents withdrew 21 proposals on climate change issues, often after winning specific commitments from the target companies.

- **Hydraulic Fracturing**: The 2010 proxy season was notable for this new campaign, aimed at a technique used in drilling for natural gas, in which chemicals are injected at high pressure underground to break up rock and force the natural gas to the surface. There are concerns that the procedures may harm water supplies for local communities, particularly in New York and Pennsylvania. The proposals came to votes at six companies and won high levels of support for a first-time campaign, ranging from 21-42 percent.

- **Sustainability reporting**: Calls for sustainability reporting are attracting substantial support. In 2008, the five proposals from a coalition of US SIF members and allies that came to votes won average support of just under 30 percent; in 2010, a proposal filed by Walden Asset Management at Layne Christenson won a majority vote of 60.3 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 2009-2010, such proposals averaged support of 33 percent.

- **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. Since 2004, the Center for Political Accountability, a nonprofit advocacy group, and its allies have persuaded 75 large companies, including more than half of the S&P 100, to disclose and require board oversight of their political spending with corporate funds. In 2010, political disclosure resolutions based on this template received an average of more than 30 percent support at the 28 companies where they came to votes, marking the fifth consecutive year that average support for these resolutions has increased.

9. Why is community investing important? What types of investments does it include?

According to the 2010 *Trends* report, assets in community investing institutions rose more than 60 percent, from $25 billion in 2007 to $41.7 billion in 2010. Community investing empowers people with tools to improve the quality of life for themselves, their families and their communities. For many, community investing is the pathway to homeownership, job creation and small business development. Millions of lives have been changed throughout the US and the world by this simple and powerful methodology. Community investing includes investments in:

- Businesses providing beneficial services, jobs or opportunities to low-income or underserved individuals and communities;
- Minority banks, community banks or credit unions providing beneficial services to underserved communities;
- Entities whose primary purpose and activity is community development. Examples are Community Development Finance Institutions that finance small business, affordable housing, and provide basic financial services to low- and moderate-income consumers, nonprofits, and international funds for microfinance and emerging businesses; and
- Projects or activities that qualify for tax credits or for Community Reinvestment Act credit for targeting benefit to underserved communities.

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

The website of US SIF: The Forum for Sustainable and Responsible Investment is one of the best places for investors to learn more about sustainable and responsible investing. Among the key US SIF resources available to investors are the following:

- Sustainable and Responsible Investing (SRI) Facts
- Facts about SRI Performance
- SRI Mutual Funds Charts

Not sure where to start? Try:
http://www.ussif.org/resources/pubs/trends/documents/2010TrendsES.pdf

Individual investors can also find information on sustainable and responsible investing at:
http://www.GreenAmericaToday.org.