How Responsible Is Your Investing?

New investment choices expand your options.

BY MARIA MARKHAM THOMPSON

Most nonprofit organizations practice some sort of socially responsible investing. That is, they screen companies, using ethical and philosophical criteria, before considering them for investments. They try to invest in companies whose practices are consistent with their missions.

Now, because of recent growth in investment options and screening criteria, you have a greater ability than ever before to select social responsible investments for your endowments, operating funds, pension plans, and 403(b) deferred compensation accounts. Nelson's Institutional Marketplace now lists 78 institutional money managers with 423 socially screened products in 18 equity and fixed income styles.

The wider range of socially screened funds means that smaller organizations can finally consider a retirement portfolio based entirely on socially responsible investments. During the last five years, funds have appeared in every asset class including international, fixed income, and small cap. Before this expansion, it was common for socially responsible investors to either forego full diversification or accept unscreened funds to complete the asset allocations of their portfolios. While some asset classes and styles, particularly value-based investing, are more thinly populated than others, you no longer need to diminish adherence to your principles for sound investment planning.

Nor do you need to worry about lower returns if you invest according to your conscience. The Social Investment Forum (a nonprofit that promotes socially responsible investing, **www.socialinvest.org/**) reports that performance by socially screened investments remains competitive. Among the 48 screened funds followed by the Forum in the last few years, 65-75% were graded in the two highest categories of investment return.

Separate Account or Mutual Funds?

You'll have the greatest control over the ethical aspects of your investments if you set up a separate account. You can then work with an investment manager to tailor a set of screening criteria to address your special concerns.

As a separate account holder, you can retain control of proxy voting. You can also monitor the companies you permit to enter the portfolio. You can even place companies that might otherwise be acceptable onto a prohibited list when there are concerns about their business practices.

If you don't have enough money to set up a separate account, or if you need flexibility in a 403(b) or other defined contribution savings vehicle, you have the option to use socially screened mutual funds. Over 90 different mutual funds report socially screened investment returns. Mutual fund options for socially responsible investors have grown at a faster pace in recent years than the number of new separate account options.

If you invest in mutual funds, be sure to read the prospectus and statement of additional information (SAI) carefully to determine what the fund permits and prohibits. Since the SAI isn't usually included with the fund's prospectus or on its Web site, ask the fund or the Securities and Exchange Commission (**www.sec.gov**) to send it to you. The SAI will disclose information on major fund investors, board members, consultants used in the screening process, the fund's fee structure, and a detailed discussion of permissible investment techniques.

Some mutual funds describe their social screening policies in essays on their Web sites. While these statements may provide more information than a prospectus, they aren't legally binding on the fund. A change of fund managers with different sentiments on an issue, such as handguns, could result in additions to the portfolio, even if the original manager was opposed to such investments.

In that respect, you're better off with a separate account than mutual funds. If you have a separate account, you are protected by having all your requirements included in your Investment Policy Statement and your contract with the investment manager. You make the decisions about what to screen out (or in) and what to do with investments that become undesirable due to changes in operations or purchase by another firm. With mutual funds, those decisions are often the personal or market-driven choices of the investment manager.

What Should You Screen Out (and In)?

Socially responsible investing adds another dimension to the due diligence for nonprofit boards. Board members need to ensure that the investments are consistent with the organization's mission and goals. For example, an organization that promotes low-income housing would want to screen financial institutions for Community Reinvestment Act compliance.

You may also want to screen for other factors. The most common social screens exclude companies that produce tobacco or alcohol, promote gambling, or are known to cause environmental degradation. Other investors screen out animal testing, meat processing, and discrimination against women and minorities. Still others make an effort to invest in companies that encourage charitable giving, the employment of disabled workers, and other positive policies. Table 1 lists the most common social investment screens in order of prevalence.

Don't assume that because a fund meets one of your criteria it will meet other related ones. For example, one fund states that it screens to avoid all use of animals for any purpose other than voluntary human companionship. It also screens the use of guns to harm animals. But the use of weapons against people, presumably in a military or defensive context, is not against the fund's principles. In both mutual funds and separate accounts, be sure to review all your concerns to ensure that the investments meet your criteria.

Do You Want to Make a Difference?

An absolute ban on owning investments in companies with objectionable activities is not the only way you can seek social change. Constructive engagement with management through shareholder advocacy may be your best route to changing the world. Shareholder advocacy ranges from voting proxies to proposing changes in corporate policy for shareholder consideration. While not always directly successful, such techniques have been very effective in getting management to pay attention to a variety of concerns.

Shareholder activists were able to get one of the largest mutual fund and investment management organizations to provide a socially responsible option for their investments. Although the majority of participants in the College Retirement Equities Fund (CREF) rejected resolutions to divest tobacco holdings for six consecutive years, the growing numbers that voted for this resolution each year sensitized management to public concern over the issue. Its pension system now includes an investment option that prohibits tobacco holdings.

Time to Take the First Step?

Nonprofit organizations now have the opportunities and tools needed to give their employees investment choices consistent with their missions and beliefs. Accessing these choices sometimes requires additional research. You may need to overcome institutional barriers and outdated ideas on investments. But the peace of conscience and financial well-being will be worth the effort. ■

Selected References

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These resources are available from the Society's Resource Center, www.snpo.org.

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Table 1:

Social Investment Screens in Order of Prevalence

Tobacco
Environmental Protection
Alcohol
Workplace Issues
Nuclear Weapons
Military Armament and Supplies
Gambling
Animal Testing
Product Safety
Pornography
Nuclear Energy
International Human Rights
Gender Discrimination
Racial Discrimination
Protection of Indigenous Peoples
Abortion
Weapons of Mass Destruction
Affordable Housing
Community Outreach
Corporate Board Diversity
Handguns
Meat Packing
Petroleum Production & Refining
Contraceptives
Organized Labor Boycotts
Caffeinated Beverages
South Africa
McBride Principles
(Northern Ireland)
Violence in the Media
Burma
Maquiladora Operations
(Mexican Border Manufacturing)
Violent Toys
Infant Formula Distribution in
Poor Countries
Family Benefits
Pork Processing
Employment of Disabled Workers
Sexual Orientation
Insurance Companies
Banking/Interest Bearing Activities
Charitable Giving Activities
Pharmaceuticals
Biotechnology
Medical Services and Products
Community Reinvestment Act
Disclosure of Information