SOCIALLY RESPONSIBLE INVESTING

How the SRI industry has failed to respond to people who want to invest with conscience and what can be done to change it.

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OVERVIEW

SUMMARY

Imagine an organic food trade association any company could join. Members set the standards to suit themselves. Thus, any store or company can label their products "organic" if they choose because there are no rules defining what organic means. If your company does anything to improve its production methods, no matter how inconsequential, it qualifies for membership and can use the word "organic" on its labels.

The association gives an annual prize to an academic paper showing that if you eliminate six of the twelve pesticides commonly used on lettuce, you still get just as much lettuce as before. Consumers who want to know about the food they buy can't find out how it is grown or how it is certified. Instead of an independent outside agency, association members hire private for-profit "screening" companies to determine what is organic. The screening companies compete, each has a different screening method, and none reveal how they define or determine organic. The screening standards allow 90% of all food produced in the world to be labeled organic. Inside this organization a small group of core producers believe organic should mean "no use of synthetic pesticides and fertilizers." The big food companies are amused by this group's romanticism and see them as "idealists."

Sound ridiculous? Yes, except this trade association exists. It doesn't sell food, it sells investments. It is the international socially responsible investing (SRI) mutual fund industry. Like the imaginary trade group, it has no standards, no definitions, and no regulations other than financial regulations. Anyone can join; anyone can call a fund an SRI fund. Over ninety percent of Fortune 500 companies are included in SRI mutual fund portfolios.

Millions of people and thousands of institutions want their investments to express social values. And that concern is growing. Public distrust of corporations has increased over the past several years. The deterioration of the environment, exposés of corporate malfeasance, publicity about illicit labor practices (e.g., child slaves producing chocolate), and the general plight of the working poor have galvanized diverse sectors of the population to invest diligently and mindfully. Investors have placed billions of dollars with SRI institutions and funds. SRI funds promise that investors' money will avoid companies with distasteful products and track records and/or reward those companies that work toward environmental responsibility, proper governance, and social justice.

This report addresses financial management companies offering mutual funds that screen their portfolios against nonfinancial criteria, what is called the socially responsible or the ethical investing community. It examines current portfolio practices, reveals how SRI funds are actually allocated, shows how the industry misleads investors, and recommends how the industry can reform itself in order to respond to investors who want to invest with a conscience and a purpose.

THE PROJECT

Because SRI mutual funds have no common standards, definitions, or codes of practices, many investors express concern and disappointment about their investments. The disappointment does not stem from portfolio losses, but from the lists of companies in the portfolios themselves (Enron, General Electric, Lockheed Martin, McDonald's, etc).

To identify the portfolio holdings and the methods employed by asset managers to select those companies, the Natural Capital Institute undertook a large-scale project aimed at describing the current state of SRI. The project was broken into two overlapping phases with distinct objectives. Phase 1, which we began in June 2003, captured data and analyzed the universe of SRI funds worldwide. Specifically, we analyzed SRI managers' allocation of investments among publicly held corporations. The study identified virtually every retail SRI mutual fund in the world with equity holdings. Drawing from information that was publicly or privately available, NCI created a unique searchable database of retail SRI mutual funds.

In the overlapping Phase 2, which we began shortly thereafter, we endeavored to create criteria for determining businesses appropriate for portfolio inclusion that we feel more closely align with investor expectations. This will result in a forthcoming list of the "best" public and privately held companies in the world as defined by these metrics. This document addresses Phase 1 of the project only. The methodology and findings from Phase 2 will be published in a separate document entitled, "The World's Best Companies."

OBJECTIVES

Although the SRI mutual fund database can be useful for investors, nongovernmental organizations (NGOs), researchers, and fund managers, our primary concern was to address the following questions:

1. Are the terms "socially responsible investing" or "social investing" so broad as to have little meaning? In other words, are the screening criteria and language employed by the SRI community adequate to express the scope and complexity of current business models as well as the problems facing humanity?

2. Do SRI mutual funds play an important role in changing corporate practices? Or do they end up accomplishing the opposite purpose, serving as marketing tools used to appease investor sentiments and greenwash corporations?

3. Should return on SRI funds be benchmarked against mainstream stock indices comprised of corporations that do not meet the same standards on social and environmental issues? Or should they be compared to companies with the highest standards of responsibility and reporting?

4. For that matter, is there a socially responsible rate of return and, if so, how should it be determined?

The question we do not address, one that permeates every SRI conference, is whether socially screened funds outperform or underperform the market. The underlying rationale that socially just and environmentally sound companies will, can, or should have higher rates of return has been well studied, but not well understood. We believe that striving to attain the highest rate of financial return is a direct cause of social injustice and environmental degradation, as it consistently leads to externalization of costs on the environment, the future, workers, or other peoples. Colonization, imperialism, slavery, and most wars are directly attributable to oligarchies trying to achieve the highest return on investment. How the SRI industry came to believe that it could use the same standard to reverse those ills may have more to do with marketing than philosophy.

HISTORY

The history of SRI can be traced back even as far as the ethical precepts embodied in Jewish law. Quakers and other religious orders, starting as long ago as the 18th century, refused to invest in "sinful" companies such as distilleries and weapons manufacturers.

In the 1960s, concerns about the environment, civil rights, and militarism were all brought to the national foreground. Events, including the Vietnam War, the Bhopal chemical disaster in 1984, and the Exxon Valdez oil spill in 1989, helped to spur public indignation and concern with corporate practices. With the adoption of a code of conduct first put forth by Pastor Leon Sullivan in 1977 to combat apartheid and human rights violations, there was a clear divide between multinational corporations that were perceived as responsible and those that were not. The Global Sullivan Principles, created twenty years later, called for equal pay for all people, fair employment practices, and affirmative training and promotion of people of color.

Even before the Sullivan Principles were articulated, people were creating SRI funds. The first SRI mutual fund was Pax World Fund, a $1 billion fund created in 1971 by Luther Tyson and Jack Corbett who worked for the United Methodist Church. A parishioner queried Tyson as to whether there was a fund that screened out companies involved in the Vietnam War. There wasn't, so Tyson, Corbett and two businessmen started the first public fund to include social criteria in its investment decisions.

DEFINITION

According to the Social Investment Forum (SIF), the trade group representing the SRI industry in the U.S., socially responsible investing is a "process that considers the social and environmental consequences of investments, both positive and negative, within the context of rigorous financial analysis." SRI can be characterized as a form of investment that not only seeks financial return but social and environmental returns as well, also called "triple bottom line" returns. It is not a more relaxed standard but a more stringent one. It relies on exacting fiduciary processes and detailed analyses of corporate practices—analyses that are carried out by companies, agencies, or NGOs. Funds employ different criteria and emphases. Some funds merely screen out tobacco, alcohol, or armament companies. Others emphasize worker conditions and human rights. Some focus on the environment or aspects of the environment, such as alternative energy. From this description, one would think that SRI funds would be diverse. In fact, there are a relatively small number of research companies, that provide the screens and data to almost all U.S. funds, resulting in funds and stock picks that are similar.

SIZE OF INDUSTRY

The SIF states in its 2003 Trends Report that as of 2003, over $2.16 trillion was invested using some combination of nonfinancial screening, shareholder advocacy, or community investment, accounting for one out of every nine professionally invested dollars in the U.S. This figure includes state and municipal pension funds, mutual funds, foundations, religious organizations, and community development institutions, amounting to 11.3 percent of the total $1.92 trillion under professional management. From 1995 to 2003, socially invested assets grew 240 percent, while all other financial assets grew 174 percent. However, SRI assets dropped from 11.66 percent of the total invested market in 2001, to 11.27 percent in 2003.

MEANS AND METHODS

There are three ways SRI mutual funds generally select stocks and express their values. The first two involve negative and positive screening, and the third is shareholder advocacy or corporate engagement.

Negative Screening

Negative or avoidance screening excludes companies that are directly or partially involved in certain industries, practices, or services. The traditional and most common negative screens are alcohol, tobacco, weapons, and nuclear power. Other screens may include contraception (Catholic funds), animal welfare, non-marital partner benefits, workplace conditions, firearms, biotechnology, gambling, and pornography. Different funds screen for different combinations of these criteria. Some only exclude when revenue exceeds a certain threshold. Other funds may extend screens to the company's suppliers or customers.

Positive Screening

The criteria for inclusive proactive screens range over a wide spectrum of concerns, including corporate governance, employment diversity and opportunity, the environment, human rights, renewable energy, beneficial products and services, and sustainability.

Virtually any screen can be used positively or negatively. For example, a bad environmental record will disqualify a company, but a good record can cause inclusion. The most widely used screens are tobacco, alcohol, labor relations, environment, gambling, weapons and military, and equal employment opportunity. According to the SIF's 2003 Trends Report, 64 percent of all screened mutual funds in the U.S. use more than five screens, while 18 percent use two to four screens, and the remaining 18 percent use only one.

Shareholder Advocacy

When SRI funds were formed, one goal was to amass critical amounts of capital in institutions that would speak out to management and in annual meetings on critical issues. Of the $2.14 trillion reportedly invested in socially screened portfolios in the U.S., just over 20 percent, or $441 billion, is in portfolios that engage in or are willing to engage in some kind of shareholder advocacy.

SCOPE

We began compiling our list of SRI funds by intentionally placing no limit on the types of funds that could be included in our study, other than using the definition of a "socially responsible" mutual fund.

As the process of fund identification proceeded, we found a wide spectrum of financial instruments and services that turned up on SRI lists, websites and resources. These included traditional retail and institutional funds, SRI venture and social venture capital funds, as well as SRI money market, annuity, and savings accounts. This wide range of SRI products and services stimulated the need to clarify what was to be included in our analysis, and what was not.

As we progressed with the project, we defined the scope of our database as follows:

INCLUSIONS

Our database includes all publicly available investment funds worldwide that state in their marketing materials that they are "socially responsible investment" products and/or that select their portfolio investments using nonfinancial criteria in a "socially responsible," "ethical," "green," "sustainable," or faith-based manner.

We entered information from the following types of funds:

- Mutual funds (sold to individual and institutional investors)
- Open-ended investment companies (OEICs)
- Unit investment trusts

EXCLUSIONS

Our study does not include the following types of funds:

- Portfolio funds offered exclusively to clients of private asset management firms or private pension funds
- Private equity or venture capital funds
- Annuity funds or sub accounts
- Savings accounts
- "Funds of funds" (so as not to double count the total assets invested by SRI funds in corporations)

Moreover, our study does not include:

- Funds that contain only debt investments (i.e., fixed income funds)
- Funds that are referred to as SRI solely because of their contributions to charitable or other nonprofit organizations

- Funds focused solely on community investment or international development

- Funds identified as straight "health-care sector" or "environmental sector" funds (e.g., those that include waste management companies), except when the fund's objectives explicitly include nonfinancial (i.e., SRI/ ethical/sustainable, etc.) criteria for portfolio selection

Note that the following section describes how the database was created, including sources of information, access to data, database development, data importation and entry, screening information, etc. Readers may want to skip this section and proceed directly to the next section called "Findings."

DATA COLLECTION

METHODOLOGY

Our task was to collect portfolio data for every "socially responsible" mutual fund in the world. We have spent the last year culling through list after list, pulling together a comprehensive list of SRI funds currently in existence. Some of these funds are self-identified as "socially responsible" or "ethical"; others have appeared on third-party lists of SRI funds, and thus warranted our investigation.

We took the following basic steps to collect data for Phase 1:

1. Identifying SRI funds and their managers around the globe through intense secondary research

2. Examining the website of each fund and/or its parent company

3. Reviewing available fund literature

4. Contacting each fund manager to confirm the existence of SRI funds and learn of additional funds

SRI SEARCH

The project started by conducting a broad search for all SRI/ethical investing websites, existing lists of funds, industry and academic reports. We collected a long list of these resources, as well as a comprehensive collection of academic and industry articles and reports that have been cataloged on the NCI server for use throughout the project.

The major SRI resource sites and organizations we consulted included the following, among others:

Asia	The Association for Sustainable & Responsible Investment in Asia (ASrIA)	www.asria.org
Australia	Corporate Monitor	www.corporatemonitor.com.au
Europe	ETHIBEL	www.ethibel.org
	Ethical Investment Research Service (EIRIS)	www.eiris.org
	European Social Investment Forum (Eurosif)	www.eurosif.org
	SRI Compass	www.sricompass.org
	Sustainable Investment	www.sustainable-investment.org
	UK Social Investment Forum (UKSIF)	www.uksif.org
Global	Investor Responsibility Research Center (IRRC)	www.irrc.org
	Sustainable Investment Research International Ltd (SiRi)	www.siricompany.com
North America	Interfaith Center on Corporate Responsibility (ICCR)	www.iccr.org
	SocialFunds.com	www.socialfunds.com
	The Social Investment Forum (SIF)	www.socialinvest.org
	The Social Investment Organization (SIO)	www.socialinvestment.ca

A more complete list of resources can be found in appendix A.

In addition, we consulted mainstream sources such as Morningstar, CBS MarketWatch, Yahoo! Finance, Hoovers, and national regulation bodies for general information, including performance data on funds, as well as general information on companies held by those funds.

From many of the sources listed above, as well as other smaller internet SRI sites, we compiled a master list of all SRI funds that we could find. We found that the existing lists on the web were quite outdated. This was especially true for lists of funds in Europe; our initial count of funds on that continent increased by about 100 throughout this process.

We systematically progressed through this preliminary list of funds, locating asset management firm websites and fund-specific websites where available, and searching for the fund literature that would serve as the primary source for our database input. These documents included fund fact sheets, prospectuses, and annual and semiannual reports. We sent inquiries via email to each asset management firm to confirm the existence of their funds, inquire about additional SRI funds they may offer, and request materials we were unable to acquire from their sites.

SUMMARY STATISTICS

In order to keep track of our list of all funds we considered, we created a "master list" of all possible contenders for inclusion in the database. To avoid double counting, we organized the funds by their country of registration, not necessarily by the country (or countries) in which they are sold.

As of April 30, 2004, our master list of funds broke down as follows:

Region	Number of Identified Funds	Number with Complete Holdings Confirmed	Number with Partial Holdings Confirmed	Number with No Holdings Data Confirmed	Number with No Information Available
Africa	3	2	0	1	0
Australia & NZ	45	19	2	16	8
Canada	40	40	0	0	0
Europe	367	215	70	13	69
Japan	12	11	1	0	0
South America	2	2	0	0	0
Asia (exc. Japan)	8	2	0	0	6
US	109	108	1	0	0
Middle East	16	0	1	0	15
Total	602	399	75	30	98
% of Total		66.3	12.5	5.0	16.3

As indicated by the summary statistics, the success we had at collecting information differed by location of the funds. This was due largely to different regulatory requirements for fund portfolio and data disclosure.

North America

In the United States and Canada, the SEC and CSA have mandatory reporting requirements and systems (EDGAR and SEDAR, respectively) that allowed us to retrieve portfolio holdings semiannually for all funds regardless of whether this information was posted on the fund's website or if they responded to our inquiries. Perhaps due to the existence of these systems, the funds in the U.S. and Canada were very responsive to our inquiries and were, for the most part, immediately forthcoming with their reports and data.

Europe

In other parts of the world, however, we were not so lucky. In European countries such as Austria, Denmark, Ireland, Luxembourg, the Netherlands, Norway, Sweden, and Spain, we were able to acquire the desired fund literature for most all the funds we had identified. However, in countries such as Belgium, Germany, and Italy, we were only able to obtain complete information on approximately half of the funds.

To our surprise, given their sheer volume, the European funds most unresponsive to data requests were based in the U.K. and France. As of March 2004, we had only collected complete information from 6 of 65 funds in France, and 26 out of 76 in the U.K. While partial holdings have been found for many of these funds, most asset management firms in these countries were unwilling to share their holdings with us.

Australia

As in the U.K. and France, most asset management firms in Australia will not share portfolio asset allocation information with the public. They produce annual reports, but these reports do not contain any lists of holdings, only traditional financial statements for the asset management firms and sometimes fund asset summaries.

Asia

We identified twelve distinct SRI funds in Japan, obtaining complete information on eleven and partial information for one. Outside of Japan, we identified eight funds in Asia: six in Hong Kong, one in Malaysia, and one in Singapore. We received favorable replies and data from the two outside of Hong Kong, but Kingsway Asset Management in Hong Kong told us that they will not share any portfolio data on their funds with non-investors.

As we realized that we would be unable to acquire fund holdings for a significant number of funds outside of North America, we explored options to purchase fund data from third-party information sources. Though fruitless thus far for European funds, this effort produced limited data for the Australian funds. The Australian fund data was very inconsistent, and much of the data was not in a useful format and/or was missing key information (i.e., in many cases we have asset allocation percentages for funds but no total assets for the corresponding date).

In order to present the most up-to-date information in the database to coincide with the release of this report, we have limited the viewable fields at this time to include only those funds in the regions of North

America, Europe and Australia, where the majority of SRI mutual fund investments are found. We are also only revealing data on funds for which we have been able to obtain complete lists of portfolio holdings. As we obtain more current and complete holdings information from all of the SRI funds we've identified worldwide, we will continue to update the database.

SRI SCREENING

To capture the various categories of "screening methodology," we used language that we felt most accurately described the three possible approaches that would include each nonfinancial issue in the selection of companies. Our terminology is defined as follows:

Negative Screen	Fund does not invest in companies with any issue-related business (100 percent negative).
Restricted Negative Screen	Fund does not invest in companies with significant issue-related business (<100 percent negative).
Positive Screen	Fund uses qualitative assessments to weigh positives and negatives of companies with issue-related business.

NCI researchers are responsible on an ongoing basis for cataloging the screening criteria for each fund family. Our approach to categorizing screening is similar to the Social Investment Forum's, as we did not want to recreate or change accepted industry categories. We did, however, modestly expand the list of categories in order to more accurately capture the breadth of screens described in fund literature.

This was an iterative process that changed as we moved through the universe of funds included in our analysis. We have not found any SRI funds that present actual quantitative approaches to screening in their marketing materials. Therefore, this task has required the "bucketing" of many claims within our framework.

As with all other data, we wanted to best represent the information presented in the fund marketing materials while also creating a single framework for cross-fund comparison. This task became particularly challenging as we tried to capture the screening approaches for those funds that describe their approach as generally "sustainable" or "ethical." Many of these funds present multiple pages of materials describing their approaches, but for the most part, we found no good way to categorize this information into a particular kind of "screen." (As a result of this challenge, at the time of this report's publication we had completed the categorization process for some, but not all, of the funds in the database.) It remains difficult to discern how much of this literature is expensive marketing and how much is a legitimate, genuine effort to explain the asset managers' SRI methodology.

The twenty-four unique screening categories we selected, along with the basic definitions we used when catagorizing the screens, are found in appendix B.

DATABASE LIMITATIONS

The approach and methodology used to develop the SRI database resulted in a number of known limitations in the use of the data for analysis. Conclusions derived from this data must recognize the following limitations:

PERCENTAGE OF "SRI INDUSTRY" CAPTURED

The Social Investment Forum's (SIF) 2003 trends report found approximately $2.14 trillion in assets invested in socially screened portfolios in the United States. Of that, SIF determined that $127 billion in assets, or about 6 percent, reside in publicly available mutual funds, while $1.99 trillion are invested in privately managed portfolios for individuals and institutions. Since our study excludes private and (for those whose information was not publicly available) institutional portfolios, and having narrowed the field even more so by our methodology, we are clearly focusing on a relatively small slice of the pie known as SRI.

Even so, assuming that the ratio of mutual funds to separately managed funds and other SRI investments is similar in the rest of the world as it is in the U.S. (as represented in the SIF study), we can still draw certain conclusions from our study of mutual funds alone. If we assume that those asset managers who offer private or institutional SRI portfolio management services in addition to managing retail mutual funds would use less restrictive SRI investment criteria in the latter, we may also conservatively assume that their investment strategies for mutual funds would reflect their basic views on SRI.

Moreover, while we have made our best efforts to include all SRI funds as defined under our scope, we are sure to have missed some, as more SRI funds are being launched all the time. In addition, we found it challenging at times to distinguish between some retail and wholesale funds, and thus may have included some pension funds that appear to be "retail" funds while leaving out the majority of pension funds that are only available through private asset managers. Thus it is possible that, despite our best efforts, our list is not precisely aligned with our stated inclusions and exclusions.

TIME SPAN OF DATA

As we relied upon publicly available fund literature and reports, or that which was made available to us upon request, we were unable to control the range of dates for which we have data. While we were able to extract holdings for most funds from annual or semiannual reports from 2003 and 2004, some of the portfolio holdings data we collected go back to mid-2002 or even late 2001. The database clearly reflects the dates associated with all data points.

The magnitude of error introduced by this wide range of data is directly related to the turnover ratio for each fund. Turnover ratios are not readily available in most fund literature and were not an included field in the database. Thus, this data is not suitable for highly technical time series analysis.

DATA CONSISTENCY

Due to the large number of data entry staff, inconsistencies in fund literature interpretation are sure to be present. However, this applies mostly to fields requiring interpretation (i.e., fund descriptors, etc.).

Regarding performance data, while it would be preferable to just have one set of overall performance metrics for each fund, most funds only present performance on a share class basis to account for variations in fees and taxes, etc. Therefore we needed to allow for entry of each share class, when multiple classes are offered, for each fund. This multiple share class performance data present a problem for detailed analysis of fund performance. In order to establish an overall performance metric for any given fund and its associated assets, we need to take the weighted average (by assets per share class) of all classes. However, total net assets per share class are not readily available for many funds. We initially included this field in the database but discovered that many funds presented the net asset value (NAV) for each share class, which is only the price of a share, not the total net assets for the share class. In the latest version of the database, we left out total net assets by share class, thereby setting limitations on analysis of this section.

DATA ACCURACY

Due to the manual entry of data from fund literature, errors are possible in our final database, though checks have been built in to catch as many errors as possible.

FINDINGS

SUMMARY

Our conclusions from examining and analyzing the portfolio data and marketing information from SRI mutual funds are summed up as follows:

1. The cumulative investment portfolio of the combined SRI mutual funds is virtually no different than the combined portfolio of conventional mutual funds.

2. The screening methodologies and exceptions employed by most SRI mutual funds allow practically any publicly-held corporation to be considered as an SRI portfolio company.

3. Fund names and literature can be deceptive, not reflecting the actual investment strategy of the managers.

4. SRI fund advertising caters to people's desires to improve the world by avoiding bad actors in the corporate world, but it can be misleading and oftentimes has little correlation to portfolio holdings.

5. There is lack of transparency and accountability in screening and portfolio selection.

6. The ability for investors to do market basket comparisons of different funds is difficult if not impossible.

7. There is a strong bias towards companies that aggressively pursue globalization of brands, products and regulations.

8. The environmental screens used by portfolio managers are loose and do little to help the environment.

9. The language used to describe SRI mutual funds, including the term "SRI" itself, is vague and indiscriminate and leads to misperception and distortion of investor goals.

10. Although shareholder activism is cited as a reason to invest in SRI mutual funds, few SRI mutual funds engage in shareholder advocacy or sponsor activist shareholder resolutions.

1. **The cumulative investment portfolio of the combined SRI mutual funds is virtually no different than the combined portfolio of conventional mutual funds.**

The NCI database can view the combined portfolio holdings of the world's SRI mutual funds, providing a cumulative summary of where investor money is placed. Below are two lists compiled from data in December 2003. Glancing over each list, try to identify which list is the 30 large cap companies that comprise the Dow Jones Industrial Average and which is the list of the top equity holdings of American companies by SRI mutual funds. (See answer below.)

LIST "A"	**LIST "B"**
Microsoft Corp.	Microsoft Corp.
Pfizer Inc	Pfizer Inc.
Johnson & Johnson	Johnson & Johnson
Citigroup Inc.	Citigroup Inc.
Intel Corporation	Intel Corporation
Cisco Systems, Inc	Alcoa Inc.
Amgen, Inc.	Boeing
American International Group, Inc.	American International Group, Inc.
Bank of America Corporation	E.I. DuPont de Nemours & Co.
Delphi Corporation	Caterpillar
Medtronic, Inc.	Honeywell Int.
General Electric Company	General Electric Company
International Business Machines Corp.	International Business Machines Corp.
Fannie Mae	Walt Disney Co.
Home Depot, Inc. (The)	Home Depot, Inc. (The)
Procter & Gamble Company	Procter & Gamble Company
Verizon Communications	Verizon Communications
Comcast Corporation	United Technologies
PepsiCo, Inc.	McDonald's
Wells Fargo & Company	Merck & Co.
3M Company	3M Company
J.P. Morgan Chase & Co.	J.P. Morgan Chase & Co.
SBC Communications, Inc.	SBC Communications, Inc.
American Express Company	American Express Company
The Rouse Company	Altria Group Inc.
Target Corporation	General Motors
The Coca-Cola Company	The Coca-Cola Company
Wal-Mart Stores, Inc.	Wal-Mart Stores, Inc.
Hewlett-Packard Company	Hewlett-Packard Company
Exxon Mobil	Exxon Mobil

(This list was compiled December 30, 2003. Fund portfolios constantly change and the order and position of companies change accordingly over time.)

A professional or someone with prior knowledge would be able to distinguish which list contains the companies that comprise the Dow Jones Index. (Column B is the Dow Jones Industrial Average.)

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2. The screening methodologies and exceptions employed by most SRI mutual funds allow practically any publicly-held corporation to be considered as an SRI portfolio company.

Over ninety percent of Fortune 500 companies are included in SRI portfolios. The most widely held corporate investment in SRI mutual funds is Microsoft, a company known for its ruthless, take-no-prisoners management tactics, a company that was indicted by the U.S. Justice Department for violating of the Sherman Antitrust Act, fined by the European Union for violating the law for its competitive practices, and sued by twenty State Attorneys General for numerous charges including antitrust. President Steve Ballmer was quoted by one of his executives as calling sustainability and green buildings "expensive nonsense." Microsoft's operating systems and software are legendary for their security lapses and poor quality. In the software industry itself, Microsoft is almost universally loathed, not for its size (which understandably engenders envy), but for its scorched-earth tactics that competitors describe as dirty, unethical, and dishonest. And finally, Microsoft has yet to issue a substantive report on corporate social responsibility or the environment except for an online document called the Citizenship Report, which contains commonplace language about integrity, honesty, recycling, community involvement, etc. Without doubt, the institutions that receive gifts from Microsoft are grateful, even when the gifts are intended to imbed Microsoft software and operating systems in schools and other institutions. (The contributions of the Gates Foundation are a function of the Gates family, not Microsoft.)

The Calvert Social Index evaluation of Microsoft says that, "Aside from its legal troubles, the company has a number of exemplary practices," and goes on to other issues such as workplace issues, international operations and human rights, and community relations. The Calvert report is emblematic of the SRI evaluation methodology, which this paper will later address. Essentially, the company's business model and ethos is completely or partially ignored while the internal practices, the kinds of things that can be reported upon in questionnaires, are analyzed and graded.

Several other companies that many SRI investors would find troublesome permeate the list of equity holdings held by SRI mutual funds.*

For example, during 2003:

- Coca-Cola was held by 56 SRI funds including the Green Century Equity Fund
- Wal-Mart was held by 33 SRI funds including the Ethical Global Equity Fund
- Clear Channel was held by 47 SRI funds including the Sierra Club Fund
- Altria (formerly Phillip Morris) was held by 12 SRI funds including Global Eco Growth Fund (Mrs. Green)
- Halliburton was held by 23 SRI funds including the Dow Jones Islamic Index Fund

- McDonald’s was held by 41 SRI funds including the Citizen’s Value Fund
- Raytheon (weaponry) was held by 12 SRI funds including the Capstone Social Ethics and Religious Values Fund
- Exxon Mobil was held by 40 SRI funds including ABF Green Planet
- General Electric was held by 48 SRI funds including the Alger Socially Responsible Growth Fund

The worst offenders with respect to GMOs and the trampling of consumer rights are Monsanto, Dow, Syngenta and Bayer. But that is no obstacle to getting a passing grade from SRI funds:

- Monsanto was held by 19 SRI funds including the Global Environment Fund
- Dow Chemical Company was held by 43 SRI funds including the SAM Sustainability Leaders International Fund
- Syngenta was held by 8 SRI funds including Capstone Social Ethics and Religious Values Fund
- Bayer was held by 32 SRI funds including the Nikko Global Sustainability Fund

* Fund holdings constantly change as managers buy and sell stocks, but generally speaking, the number of funds that hold these companies is constant.

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3. Fund names and literature may be deceptive, not reflecting the actual investment strategy of the managers.

The list on the prior page should underscore this concern. For example Muslim investors may be puzzled to find Halliburton on the Dow Jones Islamic Index Fund. This fund essentially corresponds to Shari’ah screens, prohibiting investment in (among other things) alcohol, weapons, firearms, gambling, pornography, and tobacco. Corruption, profiteering and war-mongering are not included as criteria.

The Global Eco Growth Fund (Mrs. Green) is distributed by Daiwa Securities in Japan and has one screen only, which is for the environment. Companies included in the fund’s portfolio are Exxon Mobil, Schlumberger Limited, Clear Channel, Citigroup, and Baker Hughes. How these companies match up with their screening methodology is unknown. There is no mechanism whereby an investor can investigate the evaluation process.

The Domini Social Index Portfolio, with its emphasis on S&P 500 companies with large market capitalization includes The Gap, Walt Disney, and Coca-Cola. Each of these companies has had troubling practices with respect to their communities, labor, their products, and/or the workplace. In the case of Domini, their literature and their website contain a very clear overview of their screening criteria. What is not available is an explanation of how these criteria are applied. What Domini does say is that KLD Research & Analytics (the separate screening company they created and now employ) "is reluctant to remove companies from the Index for qualitative concerns, unless it is clear that these concerns will be long-term and of major proportions." They conduct what might be called a light screening of companies.

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4. SRI fund advertising caters to people's desires to improve the world by avoiding bad actors in the corporate world, but it can be misleading and oftentimes has little correlation to portfolio holdings.

As mentioned earlier, the Pax World Funds were the first mutual funds to introduce social and environmental criteria into their portfolio selection over thirty years ago. Today, Pax advertises aggressively in the alternative media such as Mother Jones, Green Money Journal and Utne Reader. Its ads are bordered by its guiding investment principles with body copy saying: "For over 33 years, we've subjected potential investments to rigid social- and environmental-responsible screens… We believe our lofty ideals don't hurt our performance." Here are some of those principles next to a list of portfolio companies in our database at the end of December 2003:

Protect Old Growth Forests	Starbucks Corporation (plantation-grown coffee involves the removal of tropical forests)
Environmental Stewardship	Fluor Corporation (builds refineries, oil and gas production, chemical plants, and mining operations for other companies)
Green, Not Greed	Microsoft Corporation (they are synonymous with only one of these words)
Workplace Diversity	Tidewater, Inc. (marine services for offshore oil and gas; all officers and board are white men)
No Weapons	Intersil (produces radiation hardened circuits for the military)
Treat Toxic Wastes	UGI Corporation (natural gas and coal-fired electrical generation)
Reduce, Reuse, Recycle	Pepsi Bottling Group—negligible recycled content in plastic bottles, no sustainability initiatives, no Corporate Social Responsibility (CSR) report
Prevent Pollution	General Motors (How do you spell Hummer?)
Clean Air, Clean Water, Clean Energy	DPL, Inc. (coal-fired power plants in Ohio)
Equal Opportunity	Apogent, Comcast, Nokia and many other of their holdings have only one woman on the board; Intersil has no women on board or in management
Diverse Independent Boards	Chesapeake Energy Corp (natural gas producer with only white men on the board, only one women in senior management)

Conserve Earth's Resources	Baker Hughes (oilfield services, like Halliburton)
Restore Ecosystems	Corn Products International (produces high fructose syrup for soft drinks)
Encourage Alternative Energy	Apache Corporation (oil and gas)
Equal Pay for Equal Work	Bed, Bath and Beyond (many products made in China)

I don't think anyone questions Pax's commitment to social equity. It is the interpretation and application that is confusing.

A Domini Social Investment advertisement run in HOPE magazine carries a headline, "Domini Cares About Labor Rights." Yet Domini is a long-time and committed investor in McDonald's, a company with an atrocious labor record, a long history of hostility to labor unions, known for employing illegal anti-labor tactics. In Puerto Rico, every McDonald's store in the country was shut down after being unionized, only to open years later with non-union labor. In Los Angeles, McDonald's required that workers at LAX be personally escorted to and from their cars so as to avoid discussion with union organizers. McDonald's supports and belongs to trade organizations that vigorously oppose legislation establishing higher minimum wages, living wages, or indexing minimum wages to the rate of inflation.

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5. There is lack of transparency and accountability in screening and portfolio selection.

The SRI industry began as a means to communicate a higher set of values than the mere accumulation of financial return. Responding to both the environment and the oppressive apartheid regime in South Africa, investors were able to hold corporations accountable for their practices, both socially and environmentally. Without question, the SRI mutual fund world exercises influence that is disproportionate to its size in the marketplace. Brand loyalty and reputation are precious to companies and represent in many cases their most valuable asset, tangible or intangible.

Against this backdrop, there are some 600 mutual funds in the world that describe themselves as socially responsible, or use language that indicates to their prospective investors that monies invested correspond to a higher set of values than conventional investing.

> "Anita Green is part of our management team that tries to protect investors from the nightmares of corporate malfeasance."
>
> —*Pax World Funds (they invested in Enron.)*

> "Socially responsible investing for her future. SWEET!"
> (Advertisement shows a picture of a small girl with jam on her face.)
>
> —*New Covenant Funds (owns Halliburton and McDonald's)*

The problem is that investors do not have access to the methodology, the screening, the ranking criteria, or any other data that would inform them about how or why a given company is included in a portfolio. In other words, there is no transparency or accountability, either in fund prospectuses or on websites. Calvert Funds and many others owned Enron before it imploded. But investors cannot discover how these decisions were made. It is fair to say that professional money managers who do not care about corporate responsibility manage some of the SRI mutual funds. If customers want socially screened funds, there are asset managers who will create one, outsource the screening, and populate it with companies that pass the liberal screens provided. Instant social responsibility.

Screening for almost all mutual funds is done by outside firms. Some of the main companies and organizations that do SRI portfolio screening and analysis are:

Avanzi SRI Research, Italy
Arese, France
Caring Company, Sweden
CoreRatings, U.K.
Centre Info Sustainable Development, Switzerland
Dutch Sustainability Research, Netherlands
Eco.ch, Switzerland
EIRiS Services, U.K.
ETHIBEL/Cordius Asset Management, Belgium
Ethix, Sweden
Fundación Ecologica y Desarollo, Spain
GES Investment Services, Sweden
KLD Research & Analytics, U.S.
Innovest, U.S.
Investor Responsibility Research Center, U.S.
Michael Jantzi Research Associates, Canada
Oekom Research, Germany
SAM (Sustainable Asset Management), Switzerland
Triodos Research, Netherlands
Pensions & Investment Research Consultants, U.K.
scoris, Germany
Sustainable Investment Research Institute, Australia
Stock at Stake, Belgium
Vigeo, France
West LB, Germany

Most firms select a company that uses a proprietary screening methodology that is adapted to the fund's goals. Research houses use questionnaires, management interviews where necessary, and other tools to assess a company's overall rating according to their own index. Based on this rating, a company either passes or fails and thus is either available for investing or not.

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6. The ability for investors to do market basket comparisons of different funds is difficult if not impossible.

Without a transparent and harmonized process for selecting and evaluating companies, the customer cannot possibly judge the social and environmental aspects of one fund versus another except by reputation or by doing their own due diligence. The scrutiny that some SRI mutual funds give to corporations must now be placed on the SRI mutual fund industry itself. The NCI database of SRI mutual funds is the first database that can actually look at the SRI field and compare portfolios easily. But it cannot compare methodology or specific selection criteria because these are not available to us or anyone else.

7. There is a strong bias toward companies that aggressively pursue globalization of brands, products, and regulations.

The top fifteen companies held by SRI mutual funds worldwide as of December 2003 were as follows:

1. Vodafone Group PLC
2. Microsoft Corporation
3. Pfizer Inc.
4. Johnson & Johnson
5. Citigroup
6. Intel Corporation
7. Cisco Corporation
8. Royal Bank of Scotland
9. Nokia
10. Amgen
11. GlaxoSmithKline
12. American International Group, Inc.
13. Astra Zeneca
14. Bank of America Corp.
15. Merck & Co.

This paper does not take a position on globalization, but SRI mutual funds do perforce. By placing the bulk of their money with large-cap global companies, these funds are supporting globalized brands and large multinational companies. The link to social and environmental justice here is tenuous at best. This is not to say that companies on the above list are good or bad actors in this regard. It's only to point out that the issue of globalization has been avoided completely with respect to screening and lobbying.

8. The environmental screens used by portfolio managers are loose and do little to help the environment.

It is an understatement to say that there is a global environmental crisis in the making. The movie, "The Day After Tomorrow," apocalyptic as its title may be, suggests that there is a worldwide audience that accepts the idea of global climate change and is curious about the implications. Although the timing and timetable of the events in the movie were fictional and impossible from a scientific point of view, the extreme weather events employed as dramatic devices are faithful to climatology and the predictions being mooted about in science. Ideas about severe environmental loss are politically accepted in all but the narrowest reaches of neo-conservatism.

What constitutes environmental social responsibility depends on the times and the common knowledge of those times. What might have been a responsible act by a company twenty years ago might be common practice but irresponsible today. Responsible means having the capacity to respond, being accountable for the successful carrying out of a duty. Given the nature and rate of environmental loss, it can be said that, with the exception of Portfolio 21 and a handful of other U.S. and European funds, SRI environmental screens do not screen for environmental responsibility. To be sure, they exclude many of the companies who ignore or flagrantly violate the environment. Beyond that, meeting SRI environmental screens requires a low threshold of performance by a corporation.

Take the Sierra Club Stock Fund for example. There is not a single company in their portfolio that addresses the environment in an innovative or proactive way. There is no company that measures its ecological footprint. There are no alternative energy companies. They invest in companies that make surge protectors, fastening screws, steakhouses, anti-wrinkle creams, and candy bars. They are investors in Cousins Properties, one of the major contributors to sprawl in Atlanta ("From the time Cousins was founded, the Company has understood the value of land and has sought to control large tracts of strategically located land holdings for future commercial and residential development"). I single out the Sierra Club because of the nature of the organization. Founded by John Muir, it is one of the oldest and most respected NGOs in the world working for land conservation.

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9. The language used to describe SRI mutual funds, including the term "SRI" itself, is vague and indiscriminate and leads to misperception and distortion of investor goals.

Investing can be an emotional and stressful experience. Most small investors invest money that they have saved. They cannot afford to lose it as it represents a future down payment on a house, college funds, and/or retirement security. There is tremendous pressure on financial managers to perform. What SRI investing did was raise the bar. Financial returns commensurate with stock market indicators were not sufficient. The triple bottom line became a standard. Starting in the 1960s, investors have become increasingly concerned about where their money is placed, how their pension or 401K funds are managed, and how college and foundation endowments are invested.

Financial anxiety experienced by investors as well as competition in the industry has induced asset managers to focus on achieving the highest rate of return, four- or five-star Morningstar ratings, or any other indicator that will bring increased investments to their funds. Look at any magazine that features SRI mutual funds. If the performance is lower than accepted benchmarks such as the S&P or Dow Jones, the language will focus on the fund's mission: "While recent market developments have produced negative returns for the fund, our investment philosophy has produced positive results over the long term" (Pax World Fund). If the performance is as good or better than standard indices, the language will highlight returns: "Apparently, last year money did grow on trees for the Green Century Balanced Fund," which showed a one year return of 63.47 percent. Either way, the phrase "socially responsible investing" and associated terms used to gain the favor of investors who want to express social and environmental values are powerful marketing tools. SRI investing has grown consistently, even after the collapse of the stock market in 2000, demonstrating its resiliency and the strong underlying demand. The problem is that the marketing and descriptive language is inaccurate.

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10. Although shareholder activism is cited as a reason to invest in SRI mutual funds, few SRI mutual funds engage in shareholder advocacy or sponsor activist shareholder resolutions.

Given the size of the SRI asset base, it would seem that shareholder advocacy would constitute an important and vital part of overall activity. In fact, per the SIF 2003 Trends Report, 282 resolutions involving social or environmental concerns were filed with U.S. corporations in the first half of 2003, representing a modest number compared to the universe of publicly held corporations (over 10,000). Another way to put it is that for every resolution, there are $7.1 billion in SRI assets. Eighty resolutions were introduced concerning environmental issues (climate, GMOs, energy and resource use, and reporting), 47 involved global labor standards and 16 involved human rights issues. Other issues involved banking, charitable contributions, militarism, Northern Ireland, health care, political contributions, and tobacco. Winning resolutions in 2002 included eliminating sexual orientation discrimination at the Cracker Barrel Group, AIG, Home Depot, and Tootsie Roll; the phase-out of mercury oral thermometers at Cardinal Health, HCA, and JC Penny; and the announcement by Staples to increase to 30 percent post-consumer-waste and alternative fiber content in its paper. In 2003, Gillette and Reebok agreed to establish a baseline for greenhouse gas emissions. Twenty-eight other climate-related resolutions focusing on greenhouse gas reporting and emissions were rejected. Given that the world faces dire problems with respect to hunger, climate change, species loss, endemic poverty, etc., the list of successful initiatives appears rather wan.

What is most telling is that relatively few shareholder resolutions are initiated by SRI mutual fund companies. Of the resolutions sponsored in the first six months of 2003, only ten asset management firms offering retail mutual funds were sponsors or cosponsors. Compare that to the 120 or so different Catholic organizations such as Benedictine Sisters, Sisters of Loretto, Dominicans, Maryknoll Brothers, etc. who were also sponsors and co-sponsors of these resolutions.

Clearly no large company has changed its fundamental business practices due to SRI retail investing. That makes sense since the amount of institutional capital placed by the SRI community is small. For example, despite the fact that Microsoft is the number one cumulative investment held by 119 SRI mutual funds, the total funds invested at the time our survey was done ($391 million) represented .013 percent of Microsoft's market capitalization. With respect to Intel, SRI capitalization represented .016 percent of its holdings. The bigger SRI mutual funds gain access to management and have an opportunity to express their views on social and environmental issues. Calvert makes this known in its reporting, as do Domini and other fund management companies. But collegiality with top management can be deceiving. At least two SRI managers reported that it was the openness and candor of Enron's top management that was decisive in their making an investment in Enron.

The question is then: What effect do monies placed in these funds have on large-cap companies? The fair answer is a little, sometimes, depending on whether the company is getting feedback or pressure from non-investor groups. For example, it was the Rainforest Action Network (RAN) starting in 2000 that mobilized the successful four-year campaign against Citibank. RAN initiated the campaign after documenting the extensive damage mega-banks are doing to the environment, indigenous peoples' lands, biodiversity, the world's forests, and the global climate by lending money to environmentally damaging projects. Although several mutual funds cosponsored a shareholder resolution that mimicked RAN's original demands, it was arguably RAN's mobilization of activists that brought Citibank to the negotiating table and eventually resulted in environmental policy changes, certainly the most significant by any large financial institution.

One hundred sixteen mutual funds owned approximately $260 million worth of Citigroup stock during the campaign. Funds that owned Citibank during this time included the Ethical Global Equity Fund, the JP Morgan Fleming Global Socially Responsible Fund, Meritas U.S. Equity Fund, and the Storebrand Global WWF (World Wildlife Foundation) Fund. To their credit, several mutual funds divested during the campaign.

What this points to is the need for coordination and networking amongst the funds. With few exceptions, SRI mutual funds are not activists. They see their primary duty as being a fiduciary and their number one goal as shareholder return.

Funds that are active in Shareholder Advocacy are Domini and Calvert. Calvert has filed 34 resolutions mid-way through 2004, over 40 percent of them recommending the targeted company subscribe to the Global Reporting Initiative (GRI). Domini filed 22 resolutions during the 2004 proxy season.

RECOMMENDATIONS

1. Change screening criteria
2. Improve and modify fund language descriptions
3. Moderate investor expectations
4. Become transparent and specific with respect to how companies are chosen
5. Maintain constant online disclosure of portfolios with full commentary on why a company has been selected or deleted

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1. Change screening criteria

Screening criteria are mysterious to virtually all investors despite the fact that most screening organizations tout their transparency. Transparency, however, generally refers to the ability of the corporations being evaluated to understand the analytic methods, not investors. In informal discussions with SRI investors, most express surprise when they see what is being held by trusted names in the SRI field. Although funds will publish their criteria in general terms, they do not publish the analysis of how those criteria were applied to a given corporation. The nuance of such terms as "constructive engagement," "best-in-class," "pioneer/innovator," and "intelligent screening" eludes investors when a portfolio includes Wal-Mart, General Electric, Enron (held by SRI funds until its demise), and Tyco. Ironically, even though almost all companies are included in SRI funds, screening criteria today are more complex and detailed than ever before. According to EIRiS (Ethical Investment Research Service), over 300 different criteria are employed today versus only five 20 years ago. But the granularity of the screening misses the most important screen of all, the business model or intention.

The single most important criterion for a company is whether its products or services should exist at all. In other words, are its services and products helpful to the world we inhabit? Although every company believes its mission is helpful, the raison d'etre of SRI was to challenge the process and purpose of publicly held corporations. For example, McDonald's spends $2 billion a year (more than any other company in the world) on advertising, and much of its advertising and promotional expenditures are aimed at getting young children addicted to fast food including burgers, fries, and Coke. Even though obesity and type 2 diabetes are cover stories in the major news magazines, and the connection to fatty, sweet junk food is an undeniably recognized contributor to childhood obesity and disease, fast food companies fight any legislative or regulatory move that would limit their ability to continue their practices. What does it matter if one fast food company is singled out as "best in its class," which is the rationale employed by KLD Research & Analytics? As a friend once put it, if you are going the wrong way, it doesn't matter how you get there. To cite McDonald's waste management practices as a valid criterion for passing environmental screens neatly avoids the real issue: How is McDonald's wasting our children?

If the SRI industry wants to constructively engage corporations that are bad actors in some or all aspects of their business, or to confront companies whose core products are harmful or destructive, that is certainly a valid criterion. But using broad and diffuse screening criteria results in selecting companies with widely divergent social and environmental performance. The companies are lumped together into a single fund, creating portfolios that are odd if not totally inexplicable when it comes to any reasonable standard of social responsibility.

The Foundation for Strategic Environmental Research recently concluded that, "Unfortunately, many SRI-products existing today are describing — in their marketing language — that they select the leading companies regarding social responsibility for investment" when they are essentially "avoid(ing) the 'worst performers.'" In some SRI funds, only 10 percent of companies were excluded from the universe of potential companies whereas a few funds eliminated 90 percent of publicly held companies. "Best-in-class" can mean head and shoulders above the competition, or it can mean best-in-class among transnational corporations that have good return on equity.

All of this requires reexamination of language. Both the 10 percent and the 90 percent fund are called SRI funds. This nomenclature must change lest the industry run the risk of being made meaningless by its own success.

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2. Improve and modify fund language descriptions

Language does two things: it communicates and it makes distinctions. Language is not only crucial to the formation of the human mind, but it is crucial to the formation of understanding in the human mind. Any time language (words or terms in this case) is employed in overly broad and diffuse ways, understanding is lost and distinctions are blurred, even erased.

The language employed by the SRI movement originated in the 1960s and 1970s and was, at the time, new and original. It made a distinction between conventional risk-adjusted investing criteria and value-adjusted investing criteria. Today, given the growth of the SRI industry, it is time to reassess the terms and descriptors so that investors know what they are "buying."

a. **The SRI industry should create a rating system** that allows investors to evaluate the social and environmental performance of the companies and SRI mutual funds themselves. Although existing SRI funds seek high Morningstar ratings, they have not created a comparable standard for the other two legs of the triple bottom line. There are emerging attempts such as AA1000 and SA8000 for corporations, but they do not directly solve the problem. At least 30 other standards, codes, and metrics exist for corporations to assess and measure their social and environmental performance. As difficult as it is to assign numerical rankings to environmental and social issues, it is better to be approximately right than completely absent. Scoring methodology will evolve over time, and there will most certainly have to be adjustments made for different industrial sectors. The end results would include an overall ranking of a fund and rankings by company in the portfolio. Even if the method only placed funds into quintiles, it would be better than what exists now. Additionally, nonprofit screening systems such as Ethibel could be iconically attached to a company in a fund and cumulatively summarized; e.g., an Ethibel score of 37 percent would mean that 37 percent of the companies were on the Ethibel 200 list. In short, though funds cannot be ranked without significant effort, a system to do so should be established—the lack of ranking has led to widespread misuse and exploitation of the SRI term.

The following suggestions might more closely correspond to investors' needs, rather than those of corporations. The names are not catchy, but they are also not deceptive. They are what SRI fund names should be — honest and transparent:

b. **Funds with mixed results** using many different screening criteria should be called **Mixed Funds**. Footnotes would explain the different screening criteria employed and provide definitions for them. Ideally, the SRI industry would agree to common language on all terms employed so that a phrase like "best-in-class" means something. Another fund category or name could be **Great Shifters** or Adapters. This group would be comprised of companies that realize their products or services are not up to snuff with respect to sustainability and social equity, but who are now doing an authentic and creditable job of addressing materials, labor practices, advertising, waste, energy, etc.

c. **Investors want more shareholder advocacy**. Funds could be established whose purpose is to confront and challenge bad actors. These could be called **Hold-Your-Nose-We-Are-Going-In Funds**. Their return may be average, good, or fair financially, but their costs would be higher and investors would understand why. Many investors would delight in placing money in a fund that spoke loudly and clearly to Exxon Mobil, Wal-Mart, Clear Channel, Halliburton, Monsanto, etc. The funds that do the most shareholder screening in the U.S., Calvert and Domini, rightfully do not invest in these companies and thus have no proxy say. Many of the funds that do hold these companies actually think they are good investments and do not exercise shareholder rights. Thus, these companies fall between the cracks with respect to shareholder advocacy in SRI funds, although the companies are addressed by NGOs and religious orders.

d. **Biology Funds** would be comprised of companies that are directly addressing Earth's living systems with products, processes, and services that restore ecosystem viability. This category may include companies involved with sustainable forestry, biological agriculture, and low-cost water purification and remediation, for example. Their purpose would not be to lessen the damage being done to ecosystems, but to repair the damage that has been done by others and restore ecosystem viability.

e. **Mobility Funds** would address the need for affordable transportation. Even though the increase in global greenhouse gas emissions is the number one environmental problem, SRI funds hold stock in every car company in the world. Only two bicycle companies are held, one in a small fund in Luxembourg and the other by a handful of UK funds (bicycle component and sporting goods company Shimano is held by ten funds). Although companies involved with public transportation are in portfolios, real estate developers who work toward automobile-free towns are barely represented. As with Biology Funds, the fund name should indicate what the solution is. The solution is not cars, but mobility. From that point of view, the question is how to best achieve that goal. The big three automobile companies vigorously fought the State of California's attempt to impose higher emission standards on automobiles. And those three companies are held by a total of 134 SRI mutual funds.

f. Many people who already eschew conventional medicine would welcome **Real Health Funds**. The current health system is not a health system but a pathology system that addresses symptoms, not disease. SRI portfolios rely heavily on major pharmaceutical companies for fund "diversity" and performance. Even a cursory amount of research into major pharmaceutical companies reveals considerable breaches of the public trust with respect to the toxic drugs released, inflated profit margins, predatory pricing, unwillingness to make generics for the world's poor, revolving door policies at regulatory agencies, widespread damage and illness caused by their products, and submission of rigged testing results. But some old-line companies such as France's Boiron and a host of new companies like Phytopharm and SR Pharma Plc take a more holistic approach to health, using methods that are neither invasive nor toxic. SRI investors may prefer to invest in these types of companies.

g. **Alternative Energy Funds** already exist— one of the best alternative energy portfolios is Merrill Lynch New Energy Technology Fund — but alternative energy companies are poorly represented in overall SRI portfolios. Not only are there alternative energy companies in abundance throughout the world, but there are also dozens of **alternative material** companies that employ biomimicry and other methods to substitute for toxic and burdensome materials presently employed in manufacturing.

There are many more possibilities. While many of these represent specialty funds that may pose too much risk for a small investor, this does not preclude the possibility of having these areas of investment as silos within one fund. With such a structure, investors could understand to what end their money was being directed rather than receiving an alphabetical list of companies whose business purpose may or may not be apparent.

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3. Moderate investor expectations

The obsessive drive to compare SRI funds with conventional funds should cease. The difference in yield is largely irrelevant. What is relevant is what a company does, how it does it, and then, and only then, is yield relevant. Investing is both a quality issue and a timing issue. If a stock is overbought, it doesn't matter how wonderful the company is; this is commonsense stock and portfolio analysis. But using standard stock indices as measures of SRI performance betrays the mission of the industry. We don't know what a socially responsible rate of return is because no real socially responsible portfolio has been put together and tracked over a significant time. What you see in SRI advertising is: "Wall Street was wrong. The ten-year track record of the [XYZ fund] has proven that social and environmental screens do not limit your performance. To the contrary, they may, in fact, lead to higher returns." This kind of promotion is disingenuous because it assumes that the companies in the portfolio are socially responsible, which is demonstrably unfounded, and leads to the dilution of standards in the industry. The industry has hooked people on the idea that SRI funds should do as well as or better than other mutual funds, and then they have to demonstrate it, which leads to portfolio creep — the dumbing down of criteria and the blurring of distinctions between what is or is not a socially responsible company. That is not to say that companies that treat their workers well, are careful about their environmental profile, and ensure safe and quality products do not outperform corporate lowlifes. They almost always do. Many funds employ a light screen that eliminates most bad actors, but in no way do the fund holdings qualify as a portfolio that approaches sustainability or social justice.

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4. Become transparent and specific with respect to how companies are chosen

To become transparent, the SRI industry will need to harmonize screening and ranking criteria and give up on the idea that one black box method is better than the next. The SRI industry has vigorously promoted the Global Reporting Initiative (GRI), an NGO and corporate effort to come up with standard reporting guidelines for corporations with respect to their environmental and social performance. Yet, the same GRI questionnaire can be interpreted twelve different ways by different screening firms. Social justice and environmental sustainability demand transparent screening processes. The concepts are too important to be arbitrarily chosen or designated, especially by a for-profit consulting or financial management firm. Just as the GRI resides in a nonprofit organization, screening criteria and responsibility should likewise reside in an impartial nonprofit organization. The criteria should be rigorous but nuanced. The end product should result in "legends" and ranking methods that investors can quickly understand and grasp.

By making this recommendation, I do not imply it is simple or simply done. Creating the GRI was an exhaustive process. Though the standards are lacking in many respects and are replete with compromise, they are nonetheless a standard, and standards have to start somewhere.

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5. Maintain constant online disclosure of portfolios with full commentary on why a company has been selected or deleted

There is no reason, given the ubiquity of online access and the low cost of website management, why any SRI mutual fund cannot give its investors current and complete information about how their money is being managed. If Sierra Club Funds wants to own Outback Steakhouses, then investors should be able to log on and find out what thinking informed that decision. Carl Pope, director of the Sierra Club, might want to find out why as well. Investors should be able to nominate companies, comment on the portfolio in chat rooms, and provide information to management and each other that will refine and constantly update the decision-making process. It is time to put the other "social" back into socially responsible investing and let the investor participate in how his or her money is being allocated.

In summary, the SRI industry needs to change.

While SRI investors call for corporate transparency, the industry is closed, proprietary and secret. While SRI calls for workplace diversity, it is an almost entirely white industry. While the industry calls for environmental responsibility, it meets at luxury resort hotels that are far from being environmentally responsible. To put it plainly, if the SRI industry were a corporation, it wouldn't qualify in a rigorously screened portfolio. Either the industry has to reform in toto (or rename itself), or that portion of the industry that wants to maintain credibility must break off from the pretenders and create an association with real standards, enforceability, and transparency. It needs to model the behavior it purportedly demands in other companies. In the US, there are funds that make real contributions to corporate reform and accountability; funds such as Portfolio 21, Calvert, Domini, Citizens, Walden, and Women's Equity are rightfully considered leaders. But they are the minority. The world needs true responsibility, the ability to respond to poverty, inequity, environmental degradation, income polarization, women's rights, global warming, and the global corporate takeover of the commons. There are companies that meet, or are striving to meet, that standard. If others want to invest in Wal-Mart and Exxon Mobil and Clear Channel, so be it, but let us at least have the grace not to confuse funds holding those companies with responsible and ethical investing.

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APPENDIX A: SELECTED SRI RESOURCES

GLOBAL

Research & Consulting Organizations

SiRi Company - Sustainable Investment Research Int'l Ltd..www.siricompany.com

Reports

MISTRA - Screening of Screening Companies (pdf).............................. www.innovestgroup.com/pdfs/MISTRA.pdf

WRI Project- Green investing.. http://capmarkets.wri.org

NORTH AMERICA

U.S.

General

Ethical Investment Mutual Funds .... www.rawdc.org/invest/funds.html

GOOD MONEY.. www.goodmoney.com

GreenMoney Journal .... www.greenmoneyjournal.com

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APPENDIX B: SCREENING CATEGORIES

CATEGORY	BASIC DEFINITION
Abortion / Contraceptives	Avoids abortion providers; drug manufacturers that manufacture and distribute abortifacients; insurance companies that pay for elective abortions (where not mandated by law); or companies that provide financial support to Planned Parenthood; manufacturers of birth control products.
Alcohol	Avoids companies that produce, market, or otherwise promote the consumption of alcoholic beverages.
Animal Welfare	Seeks promotion of humane treatment of animals. Avoids companies that provide animal testing services or manufacture or sell animal-tested cosmetics or pharmaceuticals; have any involvement in intensive farming; operate abattoirs or slaughterhouse facilities; are producers or retailers of meat, poultry, fish, dairy products or slaughterhouse byproducts. Also avoids companies involved in hunting/trapping equipment or the use of animals in end products.
Biotechnology	Avoids companies involved in the promotion or development of genetic engineering for agricultural applications. Seeks to invest in companies that support sustainable agriculture, biodiversity, local farmers, and industrial applications of biotechnology and biomimicry.
Community Investment / Support	Seeks companies with proactive investment in surrounding communities by sponsoring charitable donations, employee volunteerism, and/or housing and education programs.
Corporate Governance / Business Practices	Seeks companies with strong investment in R&D, quality assurance, product safety; avoidance of antitrust violations, consumer fraud, and marketing scandals.
Defense / Military Weapons	Avoids companies that produce weapons for domestic or foreign military.
Employment Equality / Diversity	Seeks companies in which minorities, women, gays/lesbians, and/or disabled persons are recruited and represented among senior management and the board of directors.
Environment	Avoids companies that pollute, produce toxic products, and contribute to global warming; seeks proactive involvement in recycling, waste reduction, and environmental cleanup.
Firearms	Avoids companies producing firearms or small arms ammunition for personal use.
Foreign Operations	Seeks companies that uphold high standards in their international operations; avoids investment in oppressive regimes such as Burma or China.

Gambling	Avoids companies deriving identifiable revenues from the provision of gaming services.
Health Care / Pharmaceuticals	Seeks companies whose products and services include the provision of health-care services and/or the manufacture or distribution of pharmaceuticals.
Human Rights	Avoids companies directly or indirectly complicit in human rights violations; seeks companies promoting human rights standards
Indigenous Peoples' Rights	Avoids investing in companies determined to be significantly engaged a pattern and practice of violating the rights of American Indians and other indigenous people.
Investments	Seeks companies that have demonstrated their commitment to sustainability through their investments, including capital investments (in new plants or equipment or in the R&D of ecologically superior products or technologies) or merger, acquisition and divestiture decisions with an eye toward sustainability issues.
Labor Relations / Workplace Conditions	Avoids worker exploitation and sweatshops; seeks strong union relationships, employee empowerment, and/or profit sharing.
Non-marital Partner Benefits	Avoids companies that offer their employees non-marital partner "benefits."
Nuclear	Avoids manufacturers of nuclear reactors and related equipment and companies that operate nuclear power plants.
Islamic (Shari'ah)	Avoids companies whose products and services are prohibited under Shari'ah Law including pork related products, conventional financial services (i.e. banks, insurance and mortgage companies with interest bearing lending), entertainment (i.e. cinema, hotels, music, night clubs, etc.), airlines and department stores.
Pornography / Adult Entertainment	Avoids pornographic magazines; production studios that produce offensive video and audio tapes; companies that are major sponsors of graphic sex and violence on television
Renewable Energy	Seeks power derived from sources such as hydroelectric damns, fuel cells, geothermal energy, solar energy, and/or wind energy.
Sustainability	Generic category, used primarily by European funds, to describe an integrated approach to selecting companies based on an unspecified blend of economic, environmental and social criteria; also called "triple bottom line."
Tobacco	Avoids manufacturers or distributors of tobacco or tobacco products.

*Compiled from criteria of various screening companies.