

SOCIALLY RESPONSIBLE INVESTING IN ACTION

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“Socially responsible investing (SRI) is ensuring that our investments are aligned with our values. None of us want to make our financial returns at the expense of seriously harming ourselves, other humans, or the environment.”

Unitarian Universalist Association's (UUA's) Committee on Socially Responsible Investing.

At NEPC, our clients frequently express interest in aligning their investments with their stated philosophy or set of beliefs, but implementation can be challenging. Some grapple with defining what it means to line up their investment strategy with a set of values. Others struggle to reach consensus on whether socially responsible investing conflicts with their fiduciary duty to grow assets. Many of those who do adopt a socially responsible investing framework have a difficult time fully integrating their value system into their investment program. Enter: the Unitarian Universalist Association. Few have an investment program where the mission is as thoroughly ingrained as it is at the UUA, an NEPC client for over 10 years.

In 2014, the UUA made headlines when it announced plans to review their fossil fuel holdings and to consider funding climate change solutions. Those who have worked with or followed the organization know this move is not a flash in the pan but another step in UUA's long history of socially responsible investing, or SRI. (While there are many different names for the variety of strategies that relate to mission investing, responsible investing or environmental, social and governance (ESG) investing, for the sake of simplicity, we will use the term SRI to cover all investing that is aligned with an organization's mission.)

In fact, the UUA was one of the first organizations in the United States to consistently invest with a mission in mind. When Tim Brennen joined the UUA as Treasurer and CFO in 2006, it was

further evidence of the organization's commitment to investing according to its set of beliefs. After all, Tim came from Ceres, the national network of institutional investors whose mission is to advance corporate responsibility for the environment. At Ceres, he worked with environmental organizations, religious investors, and pension funds on issues such as climate change and corporate disclosure.

Given the challenges in conceptualizing and executing SRI, we thought it would be helpful to get Tim's perspective on how the UUA has successfully navigated and overcome hurdles to implementing a robust SRI program. This paper summarizes NEPC's discussion with Tim. Please contact your NEPC consultant to discuss how you might integrate SRI into your investment strategy.

NEPC'S DEDICATED IMPACT INVESTING ADVISORY COMMITTEE COMPRISES A CROSS-DISCIPLINE TEAM OF 14 RESEARCH AND CONSULTING STAFF MEMBERS. THE TEAM IDENTIFIES TRENDS IN SRI, IDENTIFIES AND SPONSORS SRI INITIATIVES ACROSS RESEARCH AND CONSULTING, AND CREATES AND PRESENTS EDUCATIONAL OVERVIEWS AND WHITE PAPERS.

NEPC: What is the UUA and how did it start its SRI program?

Tim: Paraphrasing from the UUA website, we know the following:

Unitarian Universalism is a liberal religion with Jewish-Christian roots. The faith is diverse and inclusive; it has no creed. It affirms the worth of human beings, advocates freedom of belief and the search for advancing truth, and provides a warm, open, supportive community for people who believe that ethical living is the supreme witness of religion.

In 1966, just five years after its inception, — the result of a union of the Universalists and the Unitarians—the UUA, together with the United Church of Christ, the Methodists, and TIAA/CREF, used their stockholder rights at Kodak’s annual shareholder meeting to persuade the board of directors to review the company’s hiring practices. The group successfully convinced the firm to change its practices so the employee base more closely represented the population of its home town of Rochester, NY, providing local African Americans with a proportionate share of Kodak’s available jobs. This move has been heralded as one of the first ever successful social corporate actions.

A short time later, the UUA passed a resolution creating an Investment Policy that requested the UUA Board of Trustees to "exercise the power represented by the Association's ownership of common stock as an effective instrument for promoting social justice."

When UUA's Investment Committee was created in 1968, it was tasked with socially responsible

mandate. The domestic stock accounts are subject to customized negative and positive screening. Negative screening tries to avoid doing unnecessary harm, UUA utilizes three screens today: tobacco, weapons and Sudan. Positive screening attempts to choose investments in companies that provide a societal good and a safe and attractive return, such as companies with good environmental records.

International stocks, fixed income and some of the global asset allocation mandates are in funds that incorporate the broad ESG (environmental, social and governance) criteria. The portfolio also has a hedge fund mandate, which at this point is not invested in alignment with SRI.

At the UUA, additional SRI is achieved via the following activities:

- **Shareholder activism:** proposing and representing resolutions at annual stockholder meetings to encourage companies to adopt policies consistent with the mission.
- **Proxy voting:** using shareholder rights to vote on important issues of corporate governance, and proposed shareholder resolutions, through the annual proxy voting process.
- **Community investing:** setting aside 1%, to be invested in local businesses that generate jobs and opportunities in addition to an attractive return.

NEPC: What is next for the UUA in SRI?

Tim: Investing in private markets is on the short list as the Investment Committee has recently approved a 10% commitment to this asset class. While there are SRI opportunities in private market assets, finding them is especially important given the long-term commitment of these investments.

NEPC: What hurdles has the UUA overcome in aligning its investment program with its mission?

Tim: Though the organization has been an activist investor since the 1960’s, it wasn’t until 2000 that the UUA established an SRI Committee to operate alongside the Investment Committee. While the Investment Committee focuses on investments, including aiming for optimal risk-

FOR THOSE QUESTIONING SRI’S ABILITY TO INFLUENCE THE BUSINESS PRACTICES OF LARGE CORPORATIONS, THE SUCCESSFUL BOYCOTT IN THE 1970’S OF FIRMS DOING BUSINESS IN SOUTH AFRICA WAS AN EYE-OPENER THE WORLD OVER AS AMERICA’S LARGEST COMPANIES WERE CONVINCED TO DISCONTINUE THEIR OPERATIONS IN SOUTH AFRICA.

investing. Subsequently, in 1970, 5% percent of the UUA's endowment was designated to be invested in "enterprises which make a high social contribution."

NEPC: How does the UUA implement SRI in the investment portfolio?

Tim: Ultimately, the SRI program at the UUA is guided by the Association’s Principles and Purposes, as stated in the by-laws, and resolutions passed at our annual General Assembly of Congregations. The SRI Guidelines interpret these sources for application to our investments. Approximately 60% of the investment portfolio is invested with an SRI



adjusted returns, the SRI Committee serves as a continual reminder of the organization's mission and commitment to align investments with the mission. Committee members sit in on each other's meetings. In addition to being the "conscience" of the Investment Committee, the SRI Committee leads shareholder advocacy, that is, the filing of resolutions to be addressed at a corporation's annual meeting. It also leads the 1% of the investment pool dedicated to direct investments in communities.

Today the two committees work well together, each appreciating what the other offers. That said, in the beginning creating consensus between the Investment Committee, which leaned toward investing based on traditional metrics, and the SRI Committee, which was solely focused on investing according to the mission, was difficult. Despite having a common goal and a combined desire to balance risk, return and justice, it wasn't always easy to keep everyone happy.

A uniting factor between the two committees was established when the organization started tapping into the expertise of a third-party SRI data specialist, Sustainalytics (www.sustainalytics.com), to weight the stock universe based on the SRI criteria identified by the committees as most important in aligning the portfolio to the mission. This is a robust and dynamic discussion held every six months with Sustainalytics where each member of both committees has a voice in thoroughly reviewing the updated criteria, weights and resulting list. By weighting the criteria, the committee acknowledges that each investment is a tradeoff between positive and negative attributes; this helps everyone remember that every investment is a compromise. The result is a customized list that excludes some stocks and over weights others, depending on how well the stocks fit the committees' SRI criteria. This data-driven analysis keeps the two committees out of the weeds from reviewing and debating at every meeting each stock that enters or exits the aggregate portfolio.

It helps that today there are more SRI-oriented offerings providing a deeper and broader bench of investment options than ever. This reinforces the bridge between the two committees and allows them to speak a common language of striving for SRI without sacrificing return. One or two members of the SRI Committee attend every Investment Committee meeting, and there is always one overlapping committee member with a

vote on the Investment Committee. Finally, as the committee membership turns over, new members are educated on the history and purposes of the committees, leading to an ever-more cohesive relationship between the two bodies.

With time and commitment to the common, broader mission of the UAA, any feathers that were ruffled have been smoothed; today the two bodies work well together and complement each other.

NEPC: Does integrating SRI mean that investment returns get sacrificed?

Tim: I don't think so. While conventional wisdom historically suggests that SRI is detrimental to returns, today SRI doesn't necessarily come at the expense of returns. This is because increased awareness from society and demand from investors have fueled investment opportunities and the potential for better returns.

Furthermore, a wide range of academic studies has been conducted on the impact of SRI on financial performance; while the research is not conclusive, most research shows that there is no performance penalty, and there is some evidence that SRI strategies can add alpha.

UUA has achieved above median risk-adjusted returns compared with endowments of similar size¹ over the long term, while engaging in SRI, shareholder advocacy, and community investing.

Research on the impact SRI has on return:

- Schroder, M. "The Performance of Socially Responsible Investment: Investment Funds and Indices." *Financial Markets and Portfolio Management*, Vol. 18, No. 2 (June 2004).
- Eccles, R., I. Ioannou, and G. Serafeim. "The Impact of Corporate Sustainability on Organizational Processes and Performance." Harvard Business School, Working paper (July 2013), ssrn.com/abstract=1964011

¹ The universe median is represented by the median endowment fund with assets between \$50 million and \$250 million in the \$1.8 trillion InvestorForce Universe. Past performance is no guarantee of future results.

NEPC: What challenges does the UUA continue to face regarding aligning the mission with the investment program?

Tim: Inevitably, as to be expected with a topic that engenders passion, there are some UUA members who think the organization hasn't done enough. With so many constituents, it is hard to accommodate everyone's views. Some people may feel the organization doesn't act quickly enough; others may have different views on what actions to take. In the end, it's always a balance between risk, return, justice, and remembering the success we've enjoyed to date and continually moving forward.

NEPC: The UUA's commitment to its mission via responsible investment is admirable. Yet, the robust program may seem overwhelming for investors at the early stages. What specifically can investors do today?

Tim:

1. Vote your proxies. Services provided by Institutional Shareholder Services can be used for separate accounts. Investors in commingled funds can engage their managers around their voting policies. Model policies can be found at ISS (www.issgovernance.com).
2. Hire managers with socially responsible backgrounds and work with them to create a mandate. Contact your NEPC consultant to discuss manager options.
3. If shareholder advocacy (that is, filing a resolution to be addressed at a corporation's annual meeting) is intimidating, co-file a resolution. There are no particular requirements after filing. Generally, the lead filer does the heavy lifting, with supporting organizations participating in dialogues and attending annual meetings.

4. Participate in SRI conferences and organizations such as Ceres (www.ceres.org), US SIF (www.ussif.org), Interfaith Center on Corporate Responsibility (www.iccr.org), Mission Investors Exchange (www.missioninvestors.org), and the Investor Network on Climate Risk (www.ceres.org/investor-network/incr).
5. Sign up for emails of newsletters and investor letters from SRI organizations and SRI-oriented investment managers.
6. Allocate some of your portfolio to community investments and micro finance (1% is common).
7. Engage your managers and consultants on SRI issues. How do they factor SRI issues into their investment process? Ask about specific issues, for instance climate change, benefits for same sex couples and Sudan. Ask how they vote proxies and for their voting policies.

NEPC consultants are always available to discuss SRI and how it might serve your organization's mission. Please call us for further details.

NEPC is a member of Principles of Responsible Investing (PRI), a United Nations-supported initiative. It is an international network of investors working together to put the six Principles for Responsible Investment into practice. Its goal is to understand the implications of sustainability for investors and support signatories to incorporate these issues into their investment decision-making and ownership practices (www.unpri.org).

