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Investing in Socially Responsible Companies is a Must for Public Pension Funds – Because There is no Better Alternative

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ABSTRACT. With assets of over US$1.0 trillion and growing, public pension funds in the United States have become a major force in the private sector through their holding of equity positions in large publicly traded corporations. More recently, these funds have been expanding their investment strategy by considering a corporation's long-term risks on issues such as environmental protection, sustainability, and good corporate citizenship, and how these factors impact a company's long-term performance. Conventional wisdom argues that the fiduciary responsibility of the pension funds' trustees must be solely focused on their beneficiaries and, therefore, their investment criteria must be based strictly on narrowly defined financial measures. It is also asserted that well-established financial measurements of corporate performance already include long-term risk assessment through discounted present value of future flow of earnings. Consequently, all other criteria are contrary to the best interest of the pension funds' beneficiaries. In this paper, we assert that, contrary to conventional wisdom, pension funds, and for that matter other mutual funds, must be concerned with the long-term survival and growth of corporations. These measures are generally referred to "socially responsible investing" (SRI) and when applied to corporations, it is termed "socially responsible corporate conduct (SRCC)." We demonstrate that current measurement of future risk assessment invariably understates, and quite often completely overlooks, these long-term risks because of the inherent bias towards short-run on the part of financial intermediaries whose compensation depends greatly on short-term results. Furthermore, there is ample evidence to suggest that these intermediaries have been engaging in self-serving practices and thus failing in their duties to serve their clients', i.e. pension funds', best interests. Because of their large holdings in the total market as well as individual companies, these funds cannot easily divest from poorly performing companies without destabilizing the companies' stock and overall markets. Hence, they must opt for a strategy of emphasizing investment criteria that encourage companies to take into account long-term aspects of their operations in terms of their impact on environment, sustainability, and community welfare, to name a few. We argue that an exclusionary, and even a primary, focus on short-term financial criteria is no longer a viable option. It also calls for the pension funds to encourage greater transparency and accountability of the entire corporate sector through improved corporate governance. Thus socially responsible investing practices are not merely discretionary and desirable activities; they are a necessary imperative, which both the corporations and public pension funds, and other large institutional holders, will ignore at serious peril to themselves. Finally, the paper considers some of the recent developments where corporations have been responding to these challenges and how their actions might be strengthened through greater disclosure and transparency of corporate activities. It also makes recommendations for the pension funds to support further research in creating new measurement standards that further refine the concept of socially responsible investing as a necessary ingredient of

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long-term corporate survival and growth in the context of a changing economic, environmental and socio-political dynamic.

KEY WORDS: socially responsible investing (SRI), socially responsible corporate conduct (SRCC), public pension funds, corporate governance, free rider, public goods, financial intermediaries

Introduction

Public pension funds have become a major force in the private sector through their holding of equity positions in large publicly held companies. As of 2004, the top 10 public pension funds controlled almost US$1.0 trillion in assets.[1] This phenomenon is likely to become even more pronounced as these funds continue to expand at a rapid pace.

In the past, when confronted with poor performance and lower returns, pension funds, like most other investors, opted to divest from the poorly performing companies, if they could, rather than seek to intervene in the management of these corporations. Pension fund managers' fiduciary responsibility is to their beneficiaries. They had neither the time nor the requisite degree of resources and professional expertise to intervene in the management of individual corporations. Their ability to intervene was further constrained by conventional wisdom as to the inadvisability and futility of such effort. And finally, the tremendous liquidity in the equity markets made selling stock in the poorly performing companies as the most efficient and least expensive option.

This situation, however, has been changing. Given their large equity positions in individual corporations, it is not always possible for public pension funds – and for that matter all large institutional investors including retail mutual funds, e.g. Fidelity, Vanguard, T. Rowe Price, etc. – to divest their holdings without roiling the markets and causing a precipitous decline in stock prices with consequent losses to the pension funds' assets. Even investors who follow an indexing strategy are not immune to this problem since they must hold individual stocks that comprise the index regardless of individual stock performance. This problem becomes more acute when the undesirable corporate conduct is not limited to a handful of corporations, but reflects a pattern of conduct among a large number of companies. Thus, large public pension funds are deciding to intervene in corporate conduct with a view to improving corporate governance and management accountability.

Another issue that has embroiled public pension funds is the recent trend whereby these funds are allocating some of their investment dollars into the companies that meet certain "apparently non-financial" criteria of socially responsible conduct, generally called "socially responsible investing" or SRI. However, as we shall assert in a latter part of this paper, this labeling is largely inaccurate. The long-term implications of SRI are anything but non-financial both for the macro-economic environment of national and international trade and investment in general, and the micro-economic impact on the financial health of individual corporations and industrial sectors in particular.

The debate regarding SRI by pension funds – and its corollary "socially responsible corporate conduct" (SRCC) – has been particularly intense. It is imbued with political connotations and ideologically loaded pronouncements that often drown out rational arguments on both sides. The critics of SRI accuse the pension funds of violating their fiduciary responsibility to their pensioners. Pension funds have defended their newfound activism as an integral but hitherto neglected part of their fiduciary responsibility to their own shareholders.

Notwithstanding its importance, the debate on SRI has remained, to date, largely loaded with emotionally laden and ideologically suffused terms. It has also become stale and closed to new ideas. Like the mating dance of the penguins, all the rituals and movements are pre-determined and predictable. There is greater communication but little dialogue. This is not surprising. In any emerging issue of major economic and socio-political import, all contending parties keep issue specificity and scope deliberately vague and ambiguous so as to avoid giving other side a potential edge. Each side has its own version of facts, practical logic, and, foundation of economic, political or social theory. The other side is disparaged, albeit ever so politely, as free marketers, social liberals, aggressive unaccountable NGOs, and the unabashed defenders of the economic *status quo*, corporate self-interest, and social inequities.

It is, therefore, vital that we keep the issue open to continuous examination. For in the final analysis, we are talking about allocation of capital; who controls it; and, by what criteria the gains from economic activity are distributed among various factors of production, i.e. capital, labor, management, natural resources, technology, and entrepreneurial risk taker, to name a few.

Defining socially responsible investing

One of the difficulties in discussing the legitimacy and efficiency of SRI-based investments emanates from the fact that both its proponents and opponents have widely divergent perspective of what constitutes SRI. Even where there is some agreement as to the wording in a definition, there is no consensus as to what those words mean or ought to mean. For purposes of this discussion, we will accept the definition proffered by the Social Investments Forum, the industry association of the SRI in the United States.[2]

> Socially responsible investing (SRI) is investing in companies that meet certain baseline standards of social and environmental responsibility; actively engaging those companies to become better, more responsible corporate citizens; and dedicating a portion of assets to community economic development.[3]

Mr. William Thompson, Comptroller and trustee of the New York City Pension Fund states:

> "The New York Pension Funds take the responsibility of stock ownership seriously. They believe that advocacy and activism for shareholder rights, corporate governance reforms, and corporate responsibility is consistent with their fiduciary obligations. They understand the interconnectedness and interdependencies of markets and societies within the global economy. Accordingly, they expect companies in which they invest to strive continually to be good citizens in the communities where they do business."[4]

These definitions are significantly different in their context and meaning from the one attributed to SRI by its critics. The latter group emphasizes the notion that SRI advocates want to include "non-financial social and ethical criteria"[5] and emphasize use of ethically oriented exclusionary screens such as tobacco, and use them as "litmus tests on trendy social issues with an outsized reliance on sin screens."[6] Other critics of SRI may be less vitriolic but just as harsh in their denunciation of SRI.

Many critics also confuse SRI with philanthropy or activities that lead to greater sustainability or environmental protection as use of corporate assets for the benefit of third parties or society-at-large. It would be a mistake and a caricature to label SRI as someone's idea of "do gooders", protecting some esoteric plant or animal species, or religious zealots excoriating companies for selling perfectly legal products on ethical and moral grounds.

From the perspective of this author, SRI can best be characterized as investing in companies that conduct their operations with an eye on causing the least amount of harm to the environment and sustainability of our habitat. They are conscious of their responsibility to various stakeholders from the unintended consequences of corporate actions. In economic terms, these companies minimize negative externalities and accentuate positive externalities. Consequently, these companies also minimize future financial risks emanating from imprudent or unsafe business practices. Thus, companies conducting their operations in a socially responsible manner should be viewed as comparatively better and relatively safer long-term investment choices.

SRI as an umbrella concept incorporates varied investment criteria for selecting companies that may be considered acceptable to large groups of investors that consider social and environmental criteria in their investment decisions. One example of this approach is an index-based portfolio selection[7] where companies meet certain baseline criteria of sustainability; social responsibility; and minimization of externalities in issues pertaining to environmental protection. They may also include related issues of human rights protection and fair treatment of workers in poorer countries. These investors screen companies for socio-economic and environmental goals having first meeting their financial goals. Other investors may choose a different approach wherein a company is excluded from the investment pool because of the very nature of its core business, i.e. tobacco, or engage in business practices that are

viewed by investor groups as socially harmful or morally–ethically repugnant.

It should be noted here that many critics of the SRI find these issues of morality as fundamentally inimical to sound investing decisions, and in any case, should be the concern of individual investors and not the pension fund trustees. Notwithstanding, the superficial and apparent rationality of this argument, this type of reasoning is extremely troublesome. Are we to assume that any company that takes into account a society's social and ethical values as relevant considerations in its conduct is fundamentally wrong in its decision-making process? A free society's laws and customs reflect the bedrock ethical values and beliefs of its people. One may differ as to the extent to which these values should be considered, or particular values that should be given emphasis, in a given corporate decision, the fact remains that corporations are first and foremost creations of society and cannot and will not survive if they ignore these basic human values.

Notwithstanding, the frustration of SRI critics, this definitional ambiguity is quite understandable. SRI as a concept is evolving and would certainly create greater specificity as it matures and embraces larger groups of investors with diverse needs and sensibilities as to economic risks embedded in corporate conduct, and their preferences for good corporate conduct. We would, therefore, find an increasing number of subsets or specificity-oriented definitions under the general SRI umbrella.

Focus and scope of paper

The thesis of this paper is that pension funds, and for that matter other large institutional holders, must consider long-term environmental and socio-economic considerations in evaluating corporate performance because there is no better alternative. The scope of this paper, however, is much broader while its focus remains on pension funds and SRI. We assert that under prevailing conditions of imperfect markets, and concentration of capital and technology, an exclusive or even primary emphasis on return on capital, which is generally narrowly defined and with a short-term time perspective, would inflict enormous harm on the maintenance of free enterprise system, however imperfect.[8] The rapid trend toward globalization, and its concomitant the large multinational corporation, has severely constrained the notions of free and competitive markets allocating rewards to different factors of production in direct proportion to their contributions.[9] Instead, we have the aura of large economic institutions extracting above-normal economic rent emanating from their control of markets, technology, exploiting negative externalities, and suppressing competition. For the long term, the highly skewed allocation of returns to various factors of production would undermine not only the market-based capitalism, but also the foundations of democracy and rule of law.

The current debate on the inclusion of broader and more long-term criteria for evaluating corporate performance – as embodied in ''socially responsible investing'' by pension funds centers around two issues:

1. *Fiduciary responsibility:* It is argued that public pension funds' fiduciary responsibility mandates that funds' trustees must focus solely on the financial criteria in their investment decisions and that any other rationale, applied either wholly or in part, would violate the trustees' legal fiduciary responsibility.
2. *Financial returns of SR investments:* It is argued that SRI funds not only introduce non-financial criteria in investment decisions, they also provide lower average returns on average when compared with investments selected purely on financial criteria.

We would like to add two additional issues to our discussion of the legitimacy and appropriateness of public pension funds' investments taking into consideration the long-term impact of socio-economic, environment and sustainability-related factors in selecting corporations as investment vehicles.

3. *Types of SRI-based investments to be included in public pension funds:* There are many investment choices, based solely on financial criteria that would not be considered appropriate for public pension funds given their risk-reward profile and the needs of retirees who are the funds' shareholders/beneficiaries. Therefore, just as not all non-SRI investment choices would be suitable for pension fund investing, the same logic would hold for selecting SRI-based investment choices. The

question for consideration should be on the suitability of particular types of SR investments for different types of pension funds, and not on SR investments *per se*.

4. *Increasing size of pension funds and their ability to make changes in their investment portfolio:* The very large pools of capital to be invested by the pension funds severely restricts their freedom to move in and out of individual stocks without risking a destabilization in the affected security's prices. Thus pension funds must strive to improve their returns in line with macro-economic factors that impact the general health of the economy. The appropriate question to be asked is how best public pension funds and other large institutional investors can accomplish this objective by incorporating the long-term impact of socio-economic and environmental concerns on individual corporation and industry performance?

Fiduciary responsibility of pension funds and SRI investing

Inclusion of SRI-based investment choices (i.e. socio-economic, environment, sustainability, and corporate governance issues) presents some unique challenges given the nature of fiduciary responsibility on the part of pension fund trustees. However, these challenges do not alter the fundamental rationale for using these criteria in selecting investment vehicles.

For example, in the case of self-directed pension plans, there is nothing wrong in including funds that consider SRI-based measures in their stock selection strategies, among the basket of choices available to the investor provided that the investor is adequately informed about the characteristics of the measures as well as all other funds included in the basket. TIAA-CREF's Social Choice Fund is an example of this class of funds. This is now a common practice and investors can choose from a multiplicity of mutual fund companies.[10] Many companies with defined contribution plans also include SRI type funds in their investment choices, e.g. Gap and Ford Motor Company. This approach also has the approval of the U.S. Department of Labor so long as the SRI option can demonstrate comparable financial performance.

Where investment choices are directed by a plan's trustee, the fiduciary responsibilities require that its choice of investment vehicles among corporations should be based on a careful assessment of long-term risks and benefits of such investments. This approach does not *a priori* exclude any and all companies that are affected, over the long term, by socio-economic and environmental factors. On the contrary, as I shall argue in a latter part of this paper, SRI-based measures, as defined above, should become the dominant criteria for selecting pension plan portfolios.

There are three arguments advanced by the critics of pension funds of investing in companies on the above-mentioned basis, which they consider to be non-financial and subjective.[11] They argue that the trustees of pension funds have a strict legal obligation to selecting investments based solely on financial considerations. Pension fund trustees have no mandate from their shareholders to redefine their fiduciary responsibility. Personal preferences of pension fund trustees have no place in investment decisions that impact the life savings of current and future retirees. In short, a pension fund trustee must maximize financial returns on the fund's investments to the exclusion of all other criteria. What is left unsaid, however, is the definition of "maximization", over what time period and what types of risks are being explicitly or implicitly recognized or ignored; and, the nature of entry and exit barriers, to name a few. Although, the critics concede that risk assessment may require a long-term investment horizon, they hold that it must also be assessed on strictly financial measures, i.e. discounted current value of future cash flows.

These arguments have superficial validity when viewed in absolute and static terms. Their absolute logic, however, does not hold when examined in the dynamic context of financial markets, the changing role of financial intermediaries, the socio-political environment that effects private sector's long-term performance, and the constraints imposed on the pension fund trustees because of the sheer size of their investment needs and growth prospects over the long term.[12] It should also be noted that our criticism of exclusive or even substantive reliance on these financial intermediaries and advisors is not limited to public pension funds. It applies equally to all institutional investors – public and private – that have large pools of investing capital. Following the

recent SEC requirement that mutual funds disclose their voting record on various proxy proposals, it appears that many mutual funds, including the largest, e.g. Fidelity and T. Rowe Price, voted their shares with the company's management even on an issue where there was widespread opposition by the shareholders. It would also appear that in some cases they may have been dissuaded because of the 401K and other revenue producing business that these funds received from the companies where they voted with the management. More recent information about Mutual funds' disclosure of their votes, subsequent to the SEC's mandate, clearly demonstrates these funds' sensitivity to the concerns of the funds' shareholders in that many of the disclosed votes have gone against the management recommendations.

Critics of pension funds' consideration of socio-economic, environmental and governance-related measures in investment selection criteria speak as if it were established truth and incontrovertible fact that trustees' investment choices will be politically motivated, corrupt, uninformed, and without sufficient accountability. In large measure, this reflects political dogma and a biased perspective of the critics since instances of misconduct are at best ''instances'' and cannot measure up to indicate any type of universality.[13] By implication, it also assumes, without offering much by way of hard evidence, that corporations paying attention to operational conduct impacting corporate social responsibility issues as defined here, somehow do so at the expense of profitability and returns to shareholders.[14] However, as we shall demonstrate in a latter part of this paper, an increasingly large number of companies have initiated actions and public reporting thereof, on SRI-related issues. These changes may have been initiated in response to external pressure, but the real and substantial efforts underway demonstrate growing appreciation on the part of corporations and their management that these actions are economically justifiable and socially necessary.

Pension fund trustees can and do make bad choices or poorly informed decisions. There have also been instances of self-dealing and corruption among pension funds, e.g. the Teamsters. Similarly, there has been controversy when some public pension funds' investments were targeted toward creating employment in the local communities in the 1980s and early 1990s. Generally known as ''Economically Targeted Investments'' or ETIs, these investments were primarily devoted to real estate and construction businesses in the local communities and were often found to be of questionable economic viability.

Trustee incompetence, political influence, and conflict of interest, however, are not confined solely and even primarily to SRI-based investments of pension funds. They apply equally to decisions made solely on market-based considerations. As a matter of fact, quite often it is the financial sector intermediaries that play an important role in directing pension fund trustees towards inappropriate investment choices, which are otherwise more profitable to the financial advisor.[15] The problem, therefore, pertains to improving the conduct and accountability of pension fund trustees, and not merely their decisions with regard to SRI. The issue, therefore, is not pension fund investing in socially responsible companies *per se*, but the type of measures and issues that are incorporated in the selection criteria, and the selection and accountability standards of pension fund trustees.

Shortcomings of current approaches to maximizing returns

The notion of maximizing returns in the current context essentially means short-term returns because it is embedded in the way financial markets are structured, and, the reward system of the financial intermediaries. In selecting companies for investment, pension funds depend on the advice of financial intermediaries. These generally include banks, financial consultants, brokerage firms and investment companies, and the analysts associated with them. They also include independent accounting firms who certify the integrity of financial statements provided by the companies to the public. These advisors develop their recommendations based on traditional, but well-established financial tools. The recommendations must also meet the investment criteria and risk profile of the pension fund. The reality, however, is quite different. Pension funds' total dependence on market-based institutions for making investment choices is not necessarily, or even always, consistent with meeting their fiduciary obligations by way of making investment choices that are in the best long-term interest of pension funds' beneficiaries.

Financial intermediaries are supposed to provide independent and objective advice to their pension fund clients as well as other investors who seek their counsel. Recent evidence, however, shows that this advice, more often than not, is tainted by the vested interest of the financial intermediaries to enrich themselves at the expense of their clients.[16] Recent disclosures of corporate scandals seemed to have engulfed some of the largest and most prestigious financial institutions, law firms, public accounting firms and analysts who seemed only too willing to enhance their profits at the expense of their clients. These scandals have also ensnared some of the most prestigious and largest institutions, e.g. Citigroup, Bank of America, CSFB (Credit Suisse First Boston), American Express, Merrill Lynch, to name a few. The fact that these intermediaries are legally liable for their misconduct is of little consequence to the clients since the choices between those who were caught and those who were not may lay only at the margin of ''how far the envelope was pushed'', and the recovery of damages seldom reaches full restitution in terms of time and money.[17]

A related issue has to do with the quality of returns, which is also over stated by the conventional financial analysis. A company's profits may come from increased sales (better products and consumer loyalty), reduced expenses (production efficiencies), or externalizing costs to society (poor pollution controls). While the first two are quite apparent, it is the third one that can have serious negative consequences for corporate profitability over the long term, with increasing public awareness and resulting in regulatory fines and restitution costs, imposed through legal and judicial mandates. A company or industry that depends for its profitability on creating negative externalities has no sustainable competitive advantage and both its current profits and future growth prospects must be considered with a large measure of skepticism.

The second problem related to the questionable independence and objectivity of financial intermediaries and consultants lies in their reward system. Financial intermediaries and consultants, for the most part, are paid on the basis of the performance of their recommended investment choices. However, this performance is rarely measured in the long-term, 5–10 years. There are good arguments for this approach. It keeps advisors on their toes to constantly demonstrate their acumen in stock picking. Efficient markets constantly adjust and reflect long-term risk evaluation in the current stock prices through discounted current value of future cash flows.

The performance evaluation system, as currently construed, has an inherent bias toward underestimating future risks and over-estimating future rewards. This is especially true where future risks are hard to measure because of their novel character, uncertain magnitude, lack of disclosure on the part of corporations as to their potential liability, and unforeseen circumstances. The tendency is to exclude from one's calculations, these long-term risks, so as not to jeopardize one's short-term performance when compared with other financial intermediaries who may be less inclined to do so. This approach is also reflected inside corporations. Given the current reward system and emphasis on meeting the Wall Street expectations as to quarterly numbers, top managers are under extreme pressure, and also have every incentive, to understate their long-term risks and liabilities – particularly long-term environmental risks and liabilities, and political risks in foreign operations, to name a few. As a matter of fact, the accounting and financial reporting scandals of the last 5+ years point definitively to the ''pressure for meeting the numbers and thus earn performance bonuses based on earnings growth'' as one of the important reasons for corporate misconduct.[18]

Even a cursory examination of available information would indicate the high magnitude and frequency of misconduct on the part of the financial intermediaries. The enormous fees and blatant conflict of interest on the part of a large number of fund managers speak volumes for the inadequate and rigged system of control and insufficient disclosure. It is ironical that critics of the SRI movement have been so accommodating and forgiving the conduct of other, strictly financially oriented, mutual funds. It is so because these instrumentalities epitomize competitive and self-regulating markets that SRI critics would be reluctant to criticize. It should be apparent that our ''competitive and self-regulating markets'' have serious structural problems that are endemic to the entire system of financial markets.[19]

And who is to say that these purely financially-oriented institutions would not have performed better and with greater prudence if they had also been obliged to consider other factors e.g. long-term

sustainability of a company's products and services; the level of public hostility currently being engendered by corporate conduct, potential law suits, damage to corporate reputation, and their future negative impact on a company's financial performance, etc. It is also quite reasonable to expect that greater transparency and higher disclosure requirements would make these companies more prudent in their investment decisions and their shareholders better informed as to the appropriateness of their investment choices.

The luxury of being a free rider and enjoying extra profits by creating negative externalities is at best a short-term phenomenon and cannot succeed if every company follows a similar course of action. Large asset holders, i.e. pension funds, and large corporations or major industries, cannot afford to become free riders without risking the viability of the entire economic system. Instead they must focus on improving the climate of enterprise in a manner that minimizing the opportunities for exploitation of the commons on the part of the free rider firms.

Pension fund trustees have a broad mandate and discretion, which must encompass socio-economic as well as environment-related issues in so far as they meet the criteria of the long-term improvement in micro corporate performance, and also the macro socio-political and economic environment, which is essential to the growth of private enterprise. By the same token, companies that engage in practices that put them in conflict with broad societal consensus of acceptable conduct increase the risk and volatility of their future stream of earnings. Hence, it is reasonable, even necessary, that pension funds take these factors into consideration in making their investment choices.

Financial performance of SRI-based investments

There is growing evidence to suggest SRI-based funds' performance is no different than similarly placed funds, and also when compared with certain benchmarks, e.g. S&P 500 index.[20] There is a growing body of literature evaluating the role of social as well as environmental and sustainability-based measures both as they pertain to individual company performances and that of mutual funds.[21] For example, the performance of Domini 400 Social Index compares quite favorably with S&P 500 Index. Moreover, the methodology applied by Domini in stock selection also takes into account financial performance criteria, which is quite similar to S&P 500 Index.

Comparing the performance of socially responsible investments with a narrowly based financial index is, however, not very illuminating since it short-changes the very elements of analysis that make SRI relevant and pertinent in the first place. Therefore, the real social benefits associated with investments that consider issues of social responsibility are in the nature of free "public goods", created by the system, which both the individual investor and society-at-large can freely enjoy.[22]

The current direction of debate on the relevance and justification of SRI is inadequate and inconsequential. This would be true even if all the criticisms heaped upon SRI were taken at face value. It should be apparent to the adherents of the *status quo* that the current economic system and its governance and oversight institutions have generally failed in meeting the advocated standards of economic performance, fealty to shareholders, accountability for performance, and commensurate management rewards. The current system has created a situation that allows for excessive and unjustifiable financial rewards to the corporate management and financial intermediaries disguised under the rubric of the so-called "control by competitive markets." As we have pointed out elsewhere in this paper, the fealty to shareholders on the part of corporate managements, and to their clients on the part of financial intermediaries and financial consultants, quite often takes a secondary position to the intermediaries' self-interest. The markets apparently are unable to correct this situation since all intermediaries are driven by similar considerations and "competitive checks and balances" do not seem to operate effectively.

Let's accept for the sake of argument that SRI funds have high cost of operations; that research is faulty; filtering screens are less than perfect; and that an injection of non-financial criteria leads to less than optimal returns to the investors. We are not conceding even for a moment that this an accurate description of the situation, but simply to point out the vacuity of the SRI critics. Why should this be a surprise during the formative stages of a new institution?

The S&P as one benchmark is merely a baseline measure – no more no less. There are many other equally valid measures on which investor decisions could be based. A majority of funds that invest solely on the basis of short-term financial measurements, and which account for over 85% of all investments in mutual funds, also fail to consistently meet or exceed this benchmark. And yet the investors continue to pour money in these funds even when the front-end loads, commissions, transactions costs, and other fees, considerably enrich the fund management companies at the expense of their investors. In part, this behavior by investors could be justified by different time horizons and by their propensity to take risk. Thus a perennially poor performing fund may yield double or even triple digit returns in a given time period and vindicate the decisions of those who chose to invest in that fund.[23]

Let's also accept for the sake of argument that mutual funds – with social choice orientation – as currently constituted are essentially serving market niches, e.g. shareholders of conscience or investors with particular aversion to certain types of business activities. Why is it wrong for these investors to choose alternative investment vehicles even though they are less than perfect – provided that they have received adequate disclosure and have consciously accepted the notion of receiving somewhat lower returns? Socially responsible investing as a phenomenon is evolving and is consistently improving. In part this is due to extensive public scrutiny by the movement's critics. This is a positive outcome.

Our primary assertion with regard to socially responsible investing is that it is not antithetical to the notion of maximizing returns to shareholders. Instead, it complements the prevailing financial criteria of measuring returns, which are essentially short-term oriented, and have a bias towards understating, if not completely ignoring, many long term trends. These trends have the potential for significantly and adversely affecting the financial well being and survival of both individual companies and specific industries. When allowed to perpetuate, their cumulative effect may be catastrophic and may threaten the entire system of private enterprise, free and competitive markets, rule of law, and democratic capitalism.

The necessity of incorporating SRI-based measures can also be seen in the inadequacy of current SEC disclosure requirements with regard to social and environmental criteria. And for reasons provided elsewhere in this paper, corporations are actively ignoring or skirting even the current requirements that are currently on the books. Despite a large increase in ''social responsibility or sustainability reports'' published by corporations, it is still quite difficult to obtain data on broad areas of corporate social and environmental performance. The pressure by socially responsible investors helps to increase the demand for such data and demonstrate the necessity of strict regulatory requirements for disclosure in this area.

There are two other, somewhat related, issues that raise the ire of its critics. SRI research is considered subjective and less rigorous and that it fails to deliver what it promises.[24] We would concede this point at least in part and argue its transitional stage. To wit, the research quality of socially responsibility investing has considerably improved over the last five years and will surely improve in the future propelled by the demands of prospective investors and competitive pressures from the suppliers of research. Lastly, it is argued that SRI criteria result in reducing the financial returns of the investment choices when compared with stocked picked solely on financial criteria given a comparable risk and return profile preferences of the potential investor.

The sum and substance of the critics' argument can now be succinctly stated. SRI criteria are largely non-financial, subjective and arbitrary. There is no evidence to suggest that (a) investors receive guidance by way of investment choices they had asked for; (b) investors are short-changed in terms of maximizing their financial returns, and (c) it cannot be shown that companies and industries had any measurable impact on their conduct. The remainder of this paper will focus on these issues.

Types of social responsibility measures that should be considered appropriate for investments to be included in public pension funds

There is an urgent and critical need for substantial new research on various measures of socio-economic, environment, sustainability, and governance measures which could be used to

evaluate the performance of individual companies as well as industry sectors both at the national and international level. It is in the interest of pension funds to sponsor and encourage such research, if they wish to achieve their goal of identifying and supporting corporations that seek to earn sustained long-term profitability. Such profitability can only be achieved in an economic system that is protective of the environment, subscribes to sustainable development; and, operates under conditions of minimizing negative externalities.

The current level of SRI-oriented research, although improving, is still at a nascent stage. Given the scarcity of resources, it has taken two directions. One type of research classifies all companies on certain baseline criteria or indicators of corporate social responsibility. An investor using this research can select a number of companies that would meet a given level of SRI standards and also provide comparable financial returns.[25] The second type of research focuses on what is generally known as ''exclusionary'' screens, i.e. it identifies companies which fail to meet certain qualifications deemed so important by the potential investor as to exclude them as investment choices.[26] The measurement scales may be highly quantitative and objective, but the criteria on which the measurements are based are almost invariably subjective and reflect individual or group preferences for certain types of corporate conduct. Even under the best of circumstances these measures, as currently practiced, are at a rudimentary state and do not compare well in terms of conceptual rigor and methodological sophistication of more traditional financial criteria of corporate performance.

Three important reasons account for the slow growth in the development of more elaborate and rigorous measurements of SRI-based performance variables.

1. Corporations and industry groups are reluctant to undertake such research because it would force them to take an account of future uncertainty, which would likely lower corporate performance based on current financial criteria. It would adversely affect management compensation and stock prices. It would also expose them to more pressure from public interest groups[27] who would want to change corporate conduct in a manner that corporate management would consider imprudent, hasty, or otherwise undesirable. Increased recognition of these factors would give greater leverage to political and regulatory bodies to restrain or modify corporate conduct, which the companies might consider ill advised, expensive, and socially and economically unjustified.[28]
2. Major financial and lending institutions are also reluctant to promote such research because its long-term consequences makes it difficult to find common ground for estimating their potential impact on corporate and industry performance. Given the uncertainty of some of these measures, it is always tempting to make overly optimistic assumptions for fear that a less scrupulous competitor would gain a competitive advantage for painting a rosy picture which the corporate management would be only too willing to embrace.
3. Most public pensions have been on the defensive in pushing their concept of the importance of SRI-based investment criteria lest they be accused of shirking their fiduciary responsibility.[29] In a sense, SRI's critics have articulated the tenor of debate on the desirability of SRI-based investment criteria and pension funds have been slow to respond in a persuasive manner. The challenge for public pension funds and other large institutional investors is to cooperate and advance the need for SRI-based research. They should also consider providing financial support for such research.

It would be inappropriate for the pension funds to use exclusionary screens among the measures for selecting or rejecting individual companies for their investment portfolio. These screens reflect the strongly held moral beliefs or social values of small minorities. In a large pool of investors, it is equally likely that investors would include both individuals who subscribe to these screens and also those who are adamantly opposed to them.

The current group of SRI-related indices is also of limited value.[30] While these indices incorporate some of the long-term environmental and sustainability concerns, these measures lack depth because detailed data on these issues is not being generated especially as it pertains to individual companies, industry sectors, and across different political and

geographical regions. Where data exist on other socio-political issues, e.g. human rights abuses, corruption, acceptance of the corporate enterprise on the part of local community, degree of engagement with relevant stakeholders, these data are not linked to individual companies and industry sectors. These data are also quite fragmented, collected in different and often incompatible formats, and by agencies and groups with wide disparities in quality.

Pension funds and other large institutional investors can play a critical role in (a) identifying the important SRI-based attributes on which data should be collected, and, (b) in bringing together individuals and groups, notably the academic community, to create measures by which such data should be collected in a manner that its quality and objectivity is assured. Initially, such efforts should be limited to data creation and collection at the macro level or political and geographical regions, and industry sectors. Once the demand for such data has been established and enough progress made at the macro level, it would encourage other players, e.g. financial organizations and privately-owned research entities to fill the gap by creating links between macro data and individual corporate characteristics. We should expect that corporations would also take the initiative to generate appropriate information on similar dimensions to make them attractive investments choices by the institutional investors. The practical ramifications of these approaches are discussed in the next section.

Growth of pension funds and their role in improving the quality and size of investment choices

In an earlier part of the paper, we discussed the shortcomings of the current financial intermediaries in providing independent, objective advice to the pension funds in selecting suitable investment vehicles. We also discussed the limitations in evaluating corporate performance because of the paucity of available data that would reflect more accurately the long-term risks of investing in publicly held corporations.

The rationale for using SRI-based criteria for pension funds is even stronger for long-term investments, which must also be their preferred strategy. Pension funds and other large institutional investors have become significant investors with an increasingly large percentage of outstanding stock in major corporations both in the United States and other countries. Between 1990 and 2003, the share of all mutual funds in retirement accounts increased from 19% to 36%, and from 25% to 45% among long-term funds. Retirement funds invested in mutual funds reached US $2.7 trillion by the end of 2003. Of these, employer-sponsored defined contribution plants accounted for almost 51%. Between 1990 and 2003 the total U.S. retirement market increased almost threefold from US $3.989 trillion to US$12.064 trillion, and the state and government pension plans increased from $810 billion to US $2.320 trillion (Table I).[31]

The collectivity of investment assets controlled by pension funds and other large institutional investors has become so large that their fortunes are affected to a significantly higher degree by global economic and socio-political events. Individual corporate actions play a much smaller role in the overall performance of their investment portfolios. With their incredibly large pools of money, pension funds must hold fairly large equity positions in individual corporations and industry sectors.

Corporate management and agency costs

Despite holding large equity positions, pension funds and other institutional investors have been until recently been passive investors generally voting with corporate management on issues of board nominations and overall corporate strategy. When confronted with poor performance, they have opted to sell their stock and buy shares in other companies with potentially more promising performance. This option, however, has significant drawbacks because market discipline appears to have failed in restraining agency costs and inducing corporate management to focus on enhancing shareholder value – something that SRI critics take in as a matter of fundamental conviction despite substantial evidence to the contrary.[32]

Recent scandals have amply demonstrated that senior management has effective control of corporate assets which they mobilize primarily with an eye to maximizing their own compensation and only

TABLE I
U.S. Total Retirement Market, 1990–2003 (billions of dollars)

Year	IRAs	Defined contribution plans[a]	State and local government pension plans	Private defined benefit plans	Federal pension plans[b]	Annuities[c]	Total
1990	$637	$889	$810	$924	$340	$388	$3989
1991	776	1058	878	1075	382	420	4590
1992	873	1160	971	1100	426	470	5000
1993	993	1319	1063	1214	468	519	5576
1994	1056	1404	1103	1307	512	523	5904
1995	1288	1711	1320	1494	541	570	6924
1996	1467	1950	1515	1616	606	605	7758
1997	1728	2332	1842	1786	659	628	8974
1998	2150	2619	2085	1930	718	778	10280
1999	2651	2975	2262	2119	776	878	11662
2000	2629	2944	2331	2008	799	878	11590
2001	2619[p]	2702	2226	1816	862	944	11170
2002	2445[e]	2409	2013	1599	897	884	10247
2003	3007[e]	2897	2320	1858	959	1024	12064

e = estimated p = preliminary

[a] Defined contribution plans include private employer-sponsored defined contribution plans (including 401(k) plans, 403(b) plans, and 457 plans).

[b] Federal pension plans include U.S. treasury security holdings of the civil service retirement and disability fund, the military retirement fund, the judicial funds, the Railroad Retirement Board, and the foreign service retirement and disability fund. These plans also include securities held in the National Railroad Retirement Investment Trust and the Federal Employees Retirement System (FERS) Thrift Savings Plan (TSP).

[c] Annuities include all fixed and variable annuity reserves at life insurance companies less annuities held by IRAs, 403(b) plans, 457 plans and private pension plans. Some of these annuity reserves represent assets of individuals held outside retirement plan arrangements and IRAs; however, information to separate out such reserves is not available.

Note: Components may not add to total because of rounding.

Source: ''Mutual Funds and the U.S. Retirement Market in 2003'', Investment Company Institute Vol. 13/No. 2, www.ici.org (June 2004).

secondarily towards increasing shareholder value. A highly diffused shareholder base gives individual shareholder little incentive to seek changes in corporate conduct – a situation that is further exacerbated by the reluctance of institutional holders to challenge management.

Competitive markets have failed to curb management excesses, i.e. to control agency costs because corporate managers have little incentive to compete with each other in a manner that would adversely impact all of them. This would be true regardless of whether we are looking at short-term or long term.

The most compelling example of this phenomenon can be seen in the size of CEO compensation, which has continued to increase despite overwhelming evidence of the disconnect between corporate performance and shareholder returns. Conversely, a strong correlation can be found between absolute corporate size and CEO compensation where size may also be negatively correlated to 'economic value added' and return on total corporate assets.[33] The increasing size and rate of CEO compensation has also resulted in a widening gap between top management compensation and those of the corporation's other employees.[34]

At the micro-level, this approach requires that pension funds and other institutional investors must become more actively involved in improving the conduct of the entire private sector and thereby create a larger pool of companies that are well managed and make good investment prospects.

Thus breaking with the conventions and traditions of the marketplace, henceforward pension funds must behave as active shareholders with the mission of reducing agency costs by making corporate management more accountable to shareholders. This would also require linking top management compensation more closely with a company's real performance rather than easily manipulative measures of increase in stock price, short-term sales growth, growth in corporate assets through mergers and acquisitions, to name a few. There is also the need for improved measures of corporate governance through a more independent and knowledgeable board, greater transparency and communications of corporate actions, and real engagement with all of a company's stakeholders so as to create a more hospitable and sustainable economic and socio-political environment for corporate operations in particular and private enterprise in general.

SRI and corporate conduct: the short-run

The phenomenon of short-run is not an isolated event but one link in a chain of multiple short-runs that eventually become a long run. In the short-run, we suffer from the tyranny of small decisions. Throwing trash on the street when nobody is watching may be an eyesore, but it won't kill us. Small short cuts in maintaining quality or to cut corners under competitive pressures, when taken in isolated circumstances can go unnoticed for a long time. Unfortunately, others soon imitate the short-run advantage by one actor. When similar acts are performed by large number of actors, over a long period of time, their cumulative effect is substantial. When that happens, a problem is born. The cumulative effect of such individual actions creates unintended consequences, which had we known earlier and could act collectively, we would have wanted to avoid.[35]

Corporate actions and SRI movement provide an illustration of this chain of events. Each corporation acting solely in its own interest, and regardless of its consequences on others, collectively creates socially undesirable behavior, which must be corrected. SRI with its insistence on identifying and changing individual corporate actions, and through its patronage of "good" corporations, acts to slow down the collective degradation of the entire socio-economic fabric.[36] As such, it serves an important social purpose that extends beyond its limited goal, i.e. identify and create investment vehicles that meet the "social" acceptability criteria of various classes of investors. Given the very large and liquid market for equities, even a relatively small SRI fund, can achieve reasonable economies of scale, and deliver an acceptable level of financial performance, while also meeting the investors' preference of socially responsible conduct.

SRI and corporate conduct – the long-term positive impact

Competitive markets may make businesses efficient, but they do not make them virtuous. If good ethics is good business, then we won't have to worry about business conduct. Business people, being rational, would willingly opt for good ethics because to do so makes good business sense.[37] The fact of the matter is that businesses consistently try to create imperfect markets because it provides them with the opportunity to extract additional rent which is above and beyond the normal cost of capital – a condition that would prevail when markets approach perfect competition. The situation is euphemistically called "pricing power" which means that businesses can impose higher prices without fear of losing customers or market share. This situation may arise due to technological innovations, entrepreneurship, or other unique attributes for which consumers are willing to reward the business through higher prices.[38]

There may be good and unavoidable reasons for imperfect markets to exist and for society to accept some of its consequences in terms of non-normal profits being earned by businesses in the short to intermediate run when these practices yield benefits to society of new innovations, entrepreneurial activity, and lower costs and better consumer choices through economies of scale and scope.

Businesses earning above normal profits arising from conditions of imperfect markets must justify those profits through better performance and accountability to other stakeholders who are unable to receive their fair share from market-based transactions. When undertaken voluntarily, these actions

may be called "corporate social responsibility or accountability."[39] They generate greater public trust and thus offer legitimacy to corporate earnings under conditions of imperfect markets. However, when companies refuse to take such actions voluntarily, they give rise to conditions of public hostility, stakeholder activism, pressure of further regulation of business, and increase future business risk.

The second situation occurs where through consolidation, market power, or other means businesses are able to externalize some of their costs to other members of society, e.g. pollution; discharging untreated wastewater into the sewage system;[40] unsafe working practices and exploitation of workers through illegal or unethical wages and working hours practices; human rights abuses, forced labor and repression of the rights of indigenous peoples, and, exploitation of consumers through false and misleading advertising and other illegal or unethical business practices.[41]

It is this second condition that SRI movement has concentrated its efforts toward improvement through proxy voting and shareholder activism. It is also the area where public pension funds and other large institutional investors can and must play an important role. Corporate actions through negative externalities in the areas of environment, consumer protection and human rights can also be seen as a type of pillaging the commons. Society's capacity to absorb such externalities is limited. And yet, in the initial stages, "commons" being the free good creates maximum incentive for individual companies to exploit to the fullest lest other competitors are able to gain additional advantage at the expense of more responsible companies.[42]

We can see this phenomenon – described as the "tragedy of the commons" – all around us and with equally disastrous consequences.[43] To remedy this situation, requires some sort of social contract. Under normal circumstances, governments or political institutions provide such enforceable mechanisms. Unfortunately, in this new era of globalization, governments have become increasingly less effective in providing enforceable mechanisms to ensure the survival of the commons.[44]

Market-based mechanisms, e.g. property rights, have also become less effective because the ownership of resources and means of production have become increasingly disjointed from the buyer of these resources. The buyer feels no compulsion to maintain the commons so long as it can compel its usage with little or no cost to itself. Thus we are left with less palatable options, which depend on the quality of institutional leadership in terms of enlightened self-interest, moral rectitude, and ultimately fear of losing its social franchise by large scale rejection of the current business model by the body politic.

Pension funds, large institutional holders, and SRI activism: a mixed picture of progress

In an earlier section, we referred to SRI critics' contention that SRI-criteria related investments have had no discernible impact on corporate conduct as a consequence of meeting or failing to meet SRI-based standards. In this section, we analyze changes that are currently taking place in corporate conduct and indicate the influence, both direct and indirect, of SRI-related actors and their agenda for corporate reform.

Corporations have been forced to contend with two potent forces. The first one is the large institutional holders of corporate stock. These institutions provide the countervailing power to curb management abuse of corporate resources and to protect their investments for the long-term and stable returns for their beneficiaries. The second force can be seen in the emergence of NGOs as a potent force to represent the interests of other stakeholders who cannot speak for themselves but are adversely impacted by the actions of corporations and other business entities.

A careful assessment of the nature and scope of corporate responses to the aforementioned pressures would indicate that SRI-critics have overlooked the many changes that have been taking place across the entire spectrum of businesses society relations. Our overall assessment suggests that the current picture is a mixed one, with halting progress in some areas while resistance to change in others. Nevertheless, two trends toward positive action have emerged and appear irreversible.

1. There is widespread acceptance that corporations and industry groups must assume their share of responsibility in the areas of environmental pro-

tection, sustainable development, and conduct their operations in a manner that is not exploitative of workers and avoids human rights abuses.
2. Business institutions have also conceded the need towards engaging all relevant stakeholders in the conduct of their operations.

One set of issues relate to improved measures of corporate governance in the traditional sense of responding to shareholder concerns of greater accountability and transparency, board composition and independence, and greater shareholder input into board selection.

The second set of issues deal with the impact of NGOs and other stakeholders groups to change corporate conduct, which have long-term adverse consequences on the environment sustainability, minimizing negative externalities, and protecting the interests of groups who suffer from the unintended consequences of corporate actions.

An important component of these issues revolves around the new wave of globalization and, in particular, the operations of multinational corporations in poor countries in the developing world. They include not only significant environmental and sustainability issues, but also stress worker exploitation and human rights abuses.

Changes in corporate governance

The Sarbanes-Oxley Act of 2002 has initiated a number of fundamental changes in the U.S. structure of corporate governance, director independence, responsibility of CEO and other corporate officials for financial reporting, expanded scope of SEC authority, and expanded duties of public auditing firms.[45] The long-term impact of these changes is as yet uncertain. Most corporate and industry spokespersons agree that some changes are necessary and will have a salutary effect on corporate governance, improved and timely public disclosure of financial information, and, prevention of abusive and self-serving management practices. At the same time, corporate and industry representatives have also decried these reforms in terms of increased costs, in time and money, for such compliance.[46] In particular, CEOs have resisted SEC proposals that would make it marginally easier for shareholders to nominate one or more directors, even where the precondition for such action has to be the evidence of corporate misconduct and substantial shareholder dissatisfaction with the current board.[47]

Some pension funds, public interest groups, and financial institutions, have created their own systems for rating corporate boards as to their relative independence, experience and competence. These rating systems are having some impact as companies receiving poor scores are responding to their low ratings by modifying their governance practices.[48] More institutional holders are voting their proxies against the management on issues of management compensation and board independence. In a number of cases, beneficiaries of pension funds have urged these votes.[49] Similarly, a number of state-sponsored pension funds have created uniform proxy guidelines to facilitate collective action in submitting shareholder resolutions.[50] These actions demonstrate that pension funds and other institutional holders that advocate SRI-based investment criteria are having some impact in changing corporate conduct.

Corporate reporting on environmental and sustainability issues

In response to public pressure and also pressure from pension funds and institutional investors, many companies have initiated reporting their performance on various measures of environment and sustainability.[51] A large number of corporations, especially those in the extractive and other environmentally sensitive industries, have been publishing corporate environmental and sustainability reports. Using a framework similar to annual financial reports, companies have been reporting their progress in controlling air emissions as a means of minimizing use of scarce resources and maintaining bio-diversity in their operations.[52] This pressure has been especially strong in Europe where it has been encompassed by EU and national government agencies.

To date, sustainability and environmental impact reports contain a large measure of ''SRI-related information'' whose veracity is often questionable because of lack of inconsistent reporting and independent external monitoring.[53] However, once these reports become common practice, it is hoped that normal competitive forces and public pressure would make them more substantive and meaningful.

Changes in corporate culture and internal decision-making process

In response to the Sarbanes-Oxley Act, companies have strengthened their internal training programs about ethical conduct. Many companies have appointed compliance and ethics officers. These changes are a positive step. However, their long-term impact is as yet uncertain. Corporations have also stepped up their communications with shareholders about the need for taking a long-term view of investment strategies, the importance of recognizing the legitimate interests of other stakeholders, and cultivating a stable and business-friendly community environment.

Corporate and industry codes of conduct

Industry groups and companies are increasingly creating voluntary codes of conduct, which indicate a company's or the industry's commitment to a certain level of socially responsible conduct in issues emanating from their operations and which are of concern to society.[54] In addition, international and multinational organizations have also created codes of conduct for various industries.[55] Various studies indicate that almost one-half of large corporations in industrially advanced nations in North America and Western Europe have some type of code of conduct covering all or some parts of their operations.[56] Unfortunately, despite their promise of creating voluntary response, most of these codes are aspirational in character and lack measures of performance or compliance verification. The result is that with few exceptions, they are regarded as "PR" exercises and are treated with disdain by public at large including the corporate community.[57]

Nevertheless, there is a ray of hope in that some companies and industry groups are gradually, albeit reluctantly, moving in the direction of greater specificity, accountability, and transparency in areas of code creation and implementation. Furthermore, there is increasing pressure from NGOs, pension funds, and even regulatory agencies toward greater voluntary action on the part of the business community.

Some concluding remarks

The emerging global economic order has once again brought capitalism and its principal actor, the large corporation to the apex of social institutions. While this new world economic order, views the large corporations as agents of positive change; underneath a thin veneer of hope and expectation, lies the ever present danger of the unaccountable power of the corporate behemoth and its potential for doing harm through abuse of that power.

The large corporation must become an active agent for social change if it is to make the world safe for democracy and, indeed, for capitalism. For the latter can survive only in an environment of unfettered individual choice voluntarily exercised in the political and economic arena. As a dominant institution in society, it must assume its rightful place and contribute to the articulation of the public agenda. In today's pluralistic society, corporate participation in social policy formulation is not a luxury but a necessity; it must receive the attention of top management, as well as the corporate resources to do it right and to do it well.

Pension funds and other large institutional holders can play a critical role in improving the overall quality of corporate conduct, i.e. make them SRI-appropriate, by taking a holistic approach to evaluating corporate performance from a long-term perspective. The goal would be to make all corporations meet the minimum benchmark standards of the impact of their activities on society. After all business cannot flourish in a rancorous and hostile socio-political environment. Nor can it grow where the cumulative impact of current and past negative externalities has increased to the extent that it adds substantially to the cost of meeting regulatory requirements.

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Notes

[1] CalPERS: $165.8 billion (www.calpers.ca.gov/), Federal Retirement Thrift: $133 billion (www.ifebp.org), Florida State Board: $120 billion (www.sbafla.com/), New York State Common: $115.7 billion (www.osc.state.ny.us), CalSTRS: $100.53 billion (www.calstrs.com), Texas Teachers: $76.60 billion (www.trs.state.tx.us), New York State Teachers: $72.4 billion (www.nystrs.org), TIAA-CREF: $307 billion (www.tiaa-cref.org).

[2] The European association is called EuroSIF.

[3] Cited in Gay, G. R. and Klaassen, J. A. ''Retirement Investment, Fiduciary Obligations, and Socially Responsible Investing'', Gay, G. R. and Klaassen, J. A. ''Retirement Investment, Fiduciary Obligations, and Socially Responsible Investing'', paper presented at the seminar ''Socially Responsible'' Investing and Pension Funds: *Welcome Reform or Fiduciary Nightmare?*'' organized by American Enterprise Institute for Public Policy Research, Washington DC, http://www.aei.org/events (June 7, 2004), Mr. Gay, et al. in turn have attributed this definition to Keefe, J. F., member of the Board of Directors of Social Investment Forum (www.socialinvest.org), an industry association, www.newcirclecom.com.

[4] Cited in Timothy Smith, '''Social Investing: Challenging Institutional Investors to Meet their Fiduciary Responsibilities'', in the conference on ''Socially Responsible' Investing and Pension Funds: Welcome Reform or Fiduciary Nightmare?'' organized by American Enterprise Institute for Public Policy Research, Washington, D.C., www.aei.org (June 7, 2004).

[5] Dunfee, T. W. ''Social Investing: Mainstream or Backwater?'' Journal of Business Ethics, Vol. 43, No. 3 (March, 2003), pp. 247–252. See also, Introduction to the conference on '''Socially Responsible' Investing and Pension Funds: Welcome Reform or Fiduciary Nightmare?'' organized by American Enterprise Institute for Public Policy Research, Washington, D. C., www.aei.org (June 7, 2004); Graff, G. M. ''Social Investing'', John Harvard's Journal, www.harvardmagazine.com, (July–August, 2003).

[6] Entine, J. ''The Myth Of Social Investing: A Critique Of Its Practice And Consequences For Corporate Social Performance Research'', Organization & Environment, Vol. 16, Issue 3 (Sep. 2003), pp. 352–368.

[7] FTSE4Good (http://www.ftse.com/ftse4good/index.jsp), Dow Jones Global Sustainability Index (http://www.sustainability-indexes.com/), Domini Social Investments (http://www.domini.com/) and Calvert (http://www.calvert.com/sri_calvertindex.asp).

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[9] The debate on the beneficial effects of the current wave of globalization has yet to develop a consensus even among leading economic scholars. The differences exist both as to its impact on overall wealth creation and, in particular, its distributive effect among various factors of production on the one hand and between the rich and the poor within and between nations on the other hand. The questioning becomes even more intense when political and environmental considerations are factored into the equation. For a cross-section, and by no means completely representative of scholarly debate, please see, Arnott, R., Greenwald, B., Kanbur, R., and Nalebuff, B., ''Economics for an Imperfect World: Essays in Honor of Joseph E. Stiglitz'', The Massachusetts Institute of Technology Press, Cambridge (2003); Barrientos, S., ''Globalization And Ethical Trade: Assessing The Implications For Development'', Journal of International Development, Vol. 12 (2000), pp. 559–570; Bhagwati, J., ''A Stream of Windows: Unsettling, Reflections on Trade, Immigration, and Democracy'', The MIT Press, Cambridge (1998); Buckley, P. J., ''The Changing Global Context of International Business'', Palgrave Macmillan Ltd., (2003); Hodgson, B. J. ''Can the Beast Be Tamed?: Reflections on John McMurtry's *Unequal Freedoms: The Global market as an Ethical System*'', Journal of Business

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[10] See for example: Calvert Social Investment Fund Equity Portfolio (CSIEX), American Trust Allegiance, Ariel Fund, Domini Social Equity Fund (DSEFX): Retail, Parnassus Equity Income Fund, PAX World Growth Fund and Walden Social Equity.

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