

fi360®

Keeping Your Mind on Money While Listening to Matters of the Heart

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Topics



- Terminology and focus of this webinar
- Why advisors should ~~not~~ engage in Sustainable and Responsible Investing (SRI)
- Fiduciary responsibility and SRI
- Best practices for SRI

Terminology and Focus



Environmental, Social, and Governance (ESG) Integration: The process of taking account of ESG data and information in investment research and decision-making processes. *

Responsible Investing: An approach to investment that explicitly acknowledges the relevance to the investor of ESG factors, and the long-term health and stability of the market as a whole.*

Sustainable Investing: Assessing how financial, governance, environmental, and social risks and opportunities interact for the long-term viability of an investment. **

* UN PRI “Fiduciary Duty in the 21st Century” (2015)

** PricewaterhouseCoopers “Do investors care about sustainability?” (2012)

Examples of Environmental Issues*



- Climate change and carbon emissions
- Water pollution
- Biodiversity
- Deforestation
- Energy efficiency
- Waste management
- Water scarcity

* CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

Examples of Social Issues*

- Customer satisfaction
- Data protection and privacy
- Gender and diversity
- Employee engagement
- Community relations
- Human rights
- Labor standards

* CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

Examples of Governance Issues*



- Board composition
- Audit committee structure
- Bribery and corruption
- Executive compensation
- Lobbying
- Political contributions
- Whistleblower schemes

* CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

Why ~~Not~~ Engage in SRI?

- Client/investor demand
- Added value
- Fiduciary obligations
- Available data

* CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

Why Consider ESG Issues?



• Help manage investment risks	63%
• Clients/investors demand it	44%
• ESG performance is a proxy for management quality	38%
• It's my fiduciary duty	37%
• To help identify investment opportunities	37%
• My firm derives reputational benefit	30%
• Regulation requires it	7%
• Other	5%

* CFA Institute "Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals" (2015)

Risk Implications of SRI

- Reputational (Nike, Gates Foundation)
- Operational/financial (insurance companies)
- Legal/regulatory (Enron)
- Competitive (ASICS, Linde)
- Physical (BP)
- Stranded assets (coal mining)
- Externalities impacting “universal owners” (bad behavior by some companies in a diversified portfolio can affect performance of other portfolio holdings)

Client Demand and Growth of SRI

- Ten-fold increase in SRI assets from 1995 through 2014*
- \$6.2 trillion U.S.-domiciled assets held by institutions that apply ESG factors at the start of 2014*
- 76% increase in assets between 2012 and the start of 2014*
- 73% of CFA designees working as portfolio managers and research analysts use ESG in their research and decision-making**
- SRI using ESG has gone mainstream – represents application of generally accepted investment principles

* US SIF Forum for Sustainable and Responsible Investing

** CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

Performance Implications of SRI



- “88% of the research shows that solid ESG practices result in better operational performance of firms and 80% of the studies show that stock price performance of companies is positively influenced by good sustainability practices” *
- “Early findings provide no evidence to suggest that these mission-aligned [private equity] exits draw depressed financial outcomes. In fact, the data show that mission-aligned exits...can provide strong returns.”**
- “ESG Tilt” and “ESG Momentum” strategies outperformed the global (MSCI World) index

* Report by the University of Oxford and Arabesque Partners (Clark, Feiner, and Viehs 2014) quoted from CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

** Wharton, University of Pennsylvania, Social Impact Initiative study “Great Expectations: Mission Preservation and Financial Performance in Impact Investing” (2015)

*** MSCI “Can ESG Add Alpha: An Analysis of ESG Tilt and Momentum Strategies (2015)

Fiduciary Responsibilities and SRI



- Duty of loyalty: Managing the potential conflict of collateral benefits
- Duty of care: Due diligence and the matter of generally accepted investment theories
- Prudence: Weighing risk, return, and time horizon considerations
- Proof of process: Documentation of what matters, why, and how decisions are reached

Fiduciary Duty of Loyalty



- Obligation is to act in the client's financial best interest
- The economic interests of investors must not be subordinated to “collateral benefits” (such as to serve a worthy societal cause)
- DOL Interpretive Bulletin 2008-1 asserted that “consideration of collateral, non-economic factors in selecting plan investments should be rare”
- New IB 2015-01 replaces IB 2008-1 which “unduly discouraged fiduciaries from considering economically targeted investments (ETIs) and environmental, social, and governance (ESG) factors”
- IB 2015-01 acknowledges that consideration of ESG issues may yield economic benefits for investors and be used proactively in due diligence

Duties of Care and Prudence



- “For investment professionals, a key idea in the discussion of ESG issues is that systematically considering ESG issues will likely lead to more complete analyses and better-informed investment decisions.”*
- “Sustainability is an important factor in the long-term success of a business. Therefore, as with any other issue related to the prudent management of capital, considering sustainability is not only important to upholding fiduciary duty, it is obligatory.”**

* CFA Institute “Environmental, Social, and Governance Issues in Investing: A Guide for Investment Professionals” (2015)

** UN PRI “Fiduciary Duty in the 21st Century” (2015)

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- ✓ Added value
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Data Challenges

- Institutional investors use both proprietary and vendor-provided research and data
- There are a dozen or so ESG data providers, including
 - Thompson Reuters
 - MSCI
 - Sustainalytics
 - Bloomberg
 - FactSet
- Morningstar plans to will start providing ESG scores for funds
- Greater access to high quality data will make consideration of ESG factors even more compelling

Best Practices (not just) for SRI



Seven Fiduciary Precepts

- Know applicable standards, laws, and trust provisions
- Diversify assets
- Prepare an investment policy statement
- Use prudent experts and document due diligence
- Control and account for investment expenses
- Monitor the activities of prudent experts and service providers
- Avoid or manage conflicts of interest in clients' best interests



1. Rules



2. Diversify



3. IPS



4. Due Diligence



5. Expenses



6. Monitor



7. Conflicts

Best Practices Specifically for SRI



- Study the growing body of knowledge
- Adhere to governing documents and applicable law
- Recognize the special importance of investment time horizon
- Include coverage of an ESG philosophy in the IPS
- Document due diligence; include traditional and ESG factors
- Seek expert input as needed for specialized ESG analysis
- Educate clients
- Establish specialized expertise and renown in the field

Questions

Additional information on fiduciary trends can be found at

fi360 Fiduciary Talk Podcast

www.fi360.com/fiduciarytalk

Also available on iTunes

and

fi360 Blog

www.fi360.com/blog

Questions about CE can be directed to support@fi360.com

How to make fiduciary concepts more meaningful to clients

Three Ingredients For A Successful Presentation*

1. **Passion:** Make it personal
2. **Logic:** Present specific and compelling information
3. **Credibility:** Establish yourself as an authority

* See *Talk Like TED: The 9 Public-Speaking Secrets of the World's Top Minds* by Carmine Gallo

The Nature of Fiduciary Responsibility **fi360**[®]

Stewardship

The careful and responsible management of something entrusted in one's care.



Lessons from Forestry for Fiduciaries



The Landowner's IPS-equivalent



The screenshot shows the 'My Land Plan' dashboard for the American Forest Foundation. At the top, there's a header with the logo and a search bar. Below this is a navigation bar with options like 'Enjoy it', 'Protect it', 'Make it healthy', 'Profit from it', and 'Pass it on'. A green box on the left asks 'What do you want to do with your land?'. A welcome message says 'Welcome back to My Land Plan!'. The main section is titled 'Dashboard' and 'MY PROPERTIES'. Under 'MY PROPERTIES', there's a section for 'THE CABIN' which includes a satellite map, a list of 'FEATURES AND POINTS OF INTEREST' (trail to fire pit, water source, Stand 2, trail, 2nd water source), 'GOALS FOR THE CABIN' (Make it a great place to hike and camp, Improve wildlife viewing), and 'THINGS TO DO' (Thin to improve forest health and diversity). Each item has a green circular icon with a white arrow.

American Forest Foundation
My Land Plan
The woodland owner's resource

Keyword Search

What do you want to do with your land?

Enjoy it Protect it Make it healthy Profit from it Pass it on

My Profile My Land My Goals and Actions My Forest Journal

✓ Welcome back to My Land Plan!

Dashboard

MY PROPERTIES [Add a property](#)

▼ THE CABIN

Google
Satellite Survey, USDA Farm Service Agency

FEATURES AND POINTS OF INTEREST

- trail to fire pit
- water source
- Stand 2
- trail
- 2nd water source
- [Add feature](#)

GOALS FOR THE CABIN

- Make it a great place to hike and camp
- Improve wildlife viewing

THINGS TO DO

- Thin to improve forest health and diversity

“Advice You Can Trust”



Finding Help

Just as you would use a financial adviser to achieve your retirement goals, a professional forester can guide you in reaching your goals for your forest.

Source: <http://extension.psu.edu/natural-resources/forests/private/tending-your-forest/finding-help>



Select Service Providers Wisely



The Importance of Diversification



The Result of Poor Stewardship: Multi-generational Damage



The Legacy of Good Stewardship



Following a Fiduciary Ethic



“Ethical behavior is doing the right thing
when no one else is watching, even
when doing the wrong thing is legal.”

— [Aldo Leopold](#)

See the Big Picture

fi360®



The Professional Advisor's Mandate: Do what is right, skillfully and profitably

fi360's mission is to help our clients gather, grow, and protect assets through better investment and business decision-making.

Our job is to help advisors fulfill their professional mandate.