

# **MEASURING THE SOCIAL, ENVIRONMENTAL AND ETHICAL PERFORMANCE OF PENSION FUNDS**

**James Gifford**

Pension funds<sup>1</sup> constitute one of the largest investment sectors with more than USD 14 trillion under management globally and growing fast (Watson Wyatt, 2004). They are controlled by trustees who are required to act in accordance with their fiduciary duty to beneficiaries – that is, to maximise financial returns, whilst keeping risk at an acceptable level.<sup>2</sup> Trustees in turn hire consultants and fund managers to invest funds in domestic and international capital markets, predominantly in equities, bonds, and property.

These investments ultimately finance various activities of companies, many of which impose significant social and environmental impacts on society. Pension funds must therefore share some responsibility for the impacts of investee companies. While there has been important progress in the reporting and rating of social, environmental and ethical (SEE) impacts of companies themselves, there has been little focus on pension funds and the responsibility they bear for the impacts of their investments.

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1 The term 'pension fund' is used loosely to refer to any institutional arrangement for the provision of retirement income where capital is invested on behalf of members. In Australia, the term superannuation is used to describe such arrangements.

2 Different jurisdictions have different requirements as to the level of risk permitted and the types of investments allowed.

This article discusses the reporting and rating of the SEE performance of pension funds and their agents and proposes a number of ways to address the problems associated with the current reporting frameworks.

As background, it is important to briefly expand on why pension funds have started to take SEE issues into account.

### **Member Democracy and Extended Fiduciary Duty**

The concept of workers regaining control of the means of production through their pension funds has been around for some time (Drucker, 1976). Robert Monks, one of the leading US shareholder activists, expands on this idea by extending the concept of 'fiduciary duty' beyond just delivering the best possible financial returns. He promotes the idea that apart from a good retirement income, members of pension funds also want to live in a clean, safe and secure world (Monks, 2001). Pension funds therefore have a responsibility to take into account any impacts that the investments might have on members. Given the ubiquity of pension fund membership, especially in the developed world, it can also be argued that the interests of members of funds are broadly consistent with those of the society in which the members live. Since a large proportion of the negative social and environmental impacts are due to the activities of publicly listed companies, of which pension funds have significant holdings, it can be argued that an obligation exists for pension funds to minimise these impacts.

### **Externalities**

The ubiquity of pension fund holdings has implications for the distribution of the costs of environmental damage. Because of the sheer size of the large pension funds, they are limited in their ability to divest stocks without distorting the market (i.e. reducing the price of those stocks and therefore the value of their holdings). For this reason funds generally prefer indexing strategies, in which they invest in almost every stock in the market to match a major market index.

Therefore, if one company causes environmental damage, another company will often suffer, and that company will also be in the fund's portfolio so it is a zero sum game for the fund (Monks, 2001). Similarly, if the environmental cost is externalised onto the taxpayer (i.e. to clean up a toxic waste site), those taxpayers will most likely also be members of the fund.

According to environmental economists, the most efficient way to deal with environmental impacts is to internalise the cost – often called the 'polluter pays principle'. Because pension funds invest across the whole market, it makes sense for them to demand the internalisation of environmental costs by investee companies, even if that is at the expense of a particular company in the portfolio.

### **Connection Between SEE Performance and Financial Performance**

It was the campaign against Apartheid, led by churches and civil rights activists, that provided the 'icebreaker' issue that opened up the space for pension funds to pressure companies on SEE issues. A number of large US pension funds demanded that investee companies pull out of South Africa (Sparkes, 2002:53).

In the early 1990s, environmental risk became an important issue of concern for pension funds, a key driver being the Exxon Valdez oil spill (Hoffman, 1996). The head of the New York City pension fund summed up her response to this disaster: "...as long term investors pension funds should practice responsible investment – avoiding environmental risk is part of their fiduciary duty" (in Sparkes, 2002:61).

These issues laid the foundation for the rise of the concepts of sustainability and corporate social responsibility (CSR), ushering in a new paradigm where social and environmental performance were considered not incidental, but fundamental, to the long-term financial success of an enterprise.

As the evidence of a relationship between CSR and long-term financial performance continues to grow (Waddock and Graves, 1997; Repetto and Austin, 2000; Orlitzky, Schmidt and Rynes, 2003), it can be argued

that trustees who *do not* take into account long-term sustainability issues are potentially breaching their fiduciary duty to members. A recent survey showed that a significant proportion of UK pension fund trustees believed that 'effective environmental management', 'good employment practices' and 'communication and transparency on social and environmental practices' are likely to have positive impacts on market value (Gribben and Faruk, 2004:2).

### **Encouragement from Governments**

Traditionally, the fiduciary duty of trustees was interpreted very narrowly to exclude consideration of SEE issues. During the 1990s, there was a recognition, both amongst the legal fraternity and by governments that taking SEE criteria into account could be consistent with the fiduciary duty of care and prudence (see Sparkes, 2002:8). Since July 2000, U.K. pension funds are required to disclose in their Statement of Investment Principles (SIP) "the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments," and "their policy (if any) in relation to the exercise of the rights (including voting rights) attaching to investments" (Just Pensions, 2004).

The introduction of this legislation in the UK, which has been followed in a number of other jurisdictions including Australia, did not mandate the consideration of social and environmental issues by pension funds. However, it did give the green light to socially responsible investment by clarifying that consideration of SEE issues in investment decision-making was within the scope of trustees' fiduciary duty. It also put the focus on funds that do not consider SEE issues to provide an explanation to their members as to why they do not.

### **Socially Responsible Investment (SRI)**

SRI is the integration of SEE issues into investment decision-making. Pension funds have applied SRI in a number of ways and many funds

now offer members an SRI option. The main SRI approaches are as follows.

### **Negative Screening**

Negative screening is the practice of avoiding or divesting the shares of companies with poor SEE performance. It was practised by the Quakers in the 17<sup>th</sup> century, involving their avoidance of the arms trade (Kinder and Domini, 1997). A modern example of this approach is the exclusion by most large Dutch pension funds of tobacco stocks from their portfolios (Eurosif, 2003). Negative screening is traditionally associated with 'ethical investment'.

### **Positive Screening**

This practice involves actively investing in companies that have good SEE performance. It is sometimes called the 'corporate sustainability approach'. It involves investing in companies which are moving towards long-term sustainability by taking steps to improve their SEE performance in tune with changes in society (Anderson, 2000; Dunphy, Griffiths and Benn, 2003). It sometimes involves selecting the best companies in each sector (best-in-class screening) so as to maximise opportunities for diversification. Positive screening could also involve sustainable venture capital, ie. direct investment in an environmental technology firm.

### **Community Investing**

Community investing is another form of positive screening that involves funding small-scale community projects that would otherwise have difficulty accessing capital. A well-known form of community investing is the provision of small loans (also called micro-credit) to people in the developing world to start their own businesses.

### **Shareholder Activism**

Shareholder activism, also called shareholder engagement or advocacy, involves investors using their power and influence as owners to seek improvements in companies' operations. It started with the Apartheid campaign and is now increasingly used to pressure companies on a range of SEE issues, from climate change to sweatshops (for the latest US trends, see IRRC and ICCR, 2003).

### **Rating the SEE Performance of Pension Funds**

The preceding sections provided a background to pension funds' consideration of SEE issues. A further question is how these efforts can be judged.

The investment sector is different from most other industries because of its enabling role in the activities of almost all other companies. Whereas mining and manufacturing companies often have large direct impacts on the environment, investment companies (including pension funds) have relatively small *direct* impacts – those arising from office procurement, energy use, business travel etc. However, without investment capital, mining, manufacturing and other companies that have negative social and environmental impacts would not have the opportunity to create these impacts. As stated above, investors, therefore, must share some of the responsibility for the SEE impacts of investee companies. But measuring the impacts of investors in a systematic way is difficult.

### **Who Needs these Measurements?**

There are many different players who want to be able to assess the SEE performance of pension funds, their agents and investee companies:

- Members need to judge their pension funds for governance and consumer-choice reasons and to ensure that their long-term interests are being protected;

- Pension fund trustees need to judge the investment products of their fund managers to ensure those products are appropriately reflecting fund policy. They also need to judge the performance of companies they directly invest in;
- Governments need to understand the impacts of the investment sector and the points of leverage to formulate the most efficient and effective regulatory responses to environmental and social problems;
- Non government organisations (NGOs), the media, and civil society need to judge which investors and companies should be held to account for their actions. They also need to know who to reward for positive contributions to society and the environment.

### **Disclosure Requirements, Reporting Frameworks, and Rating and Benchmarking Systems**

Reporting is an essential first step. It allows members of funds and other stakeholders to examine the fund's impacts. Reporting can be mandatory or voluntary. The mandatory disclosure requirements recently introduced in a number of jurisdictions only demand disclosure of investment policies or proxy voting records, and fall far short of a comprehensive reporting framework of the type that is taken for granted in financial accounting.

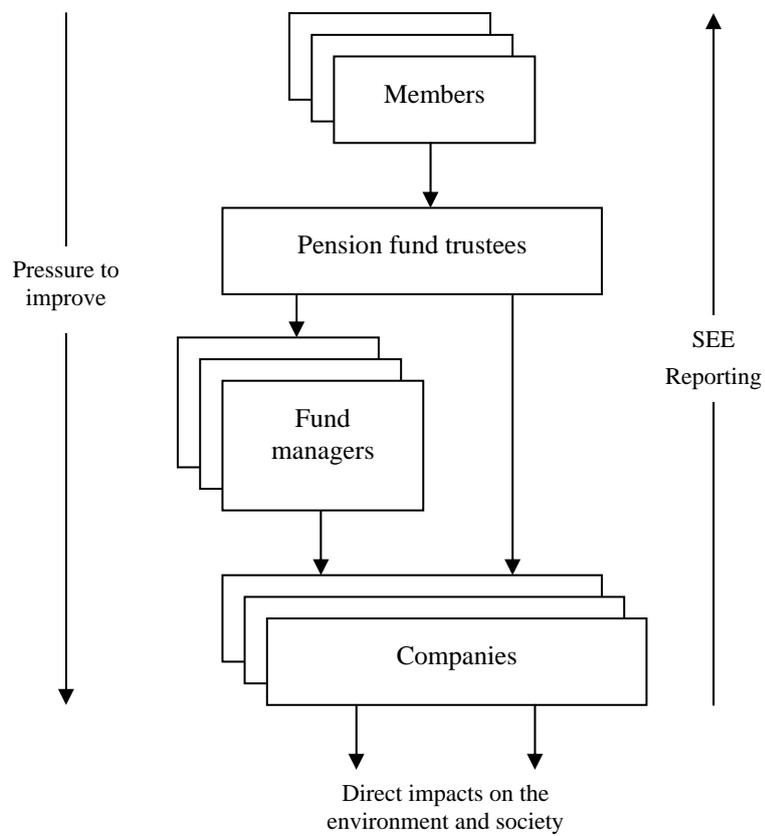
On the voluntary side, The Global Reporting Initiative (GRI) is an example of a reporting framework. It is sponsored by the United Nations Environment Programme and the US-based Coalition for Environmentally Responsible Economies (CERES). The GRI aims to 'develop and disseminate globally applicable sustainability reporting guidelines'.<sup>3</sup>

Once funds are reporting adequately, the next step is to distil this information into a form that allows comparisons to be made between institutions and over time.

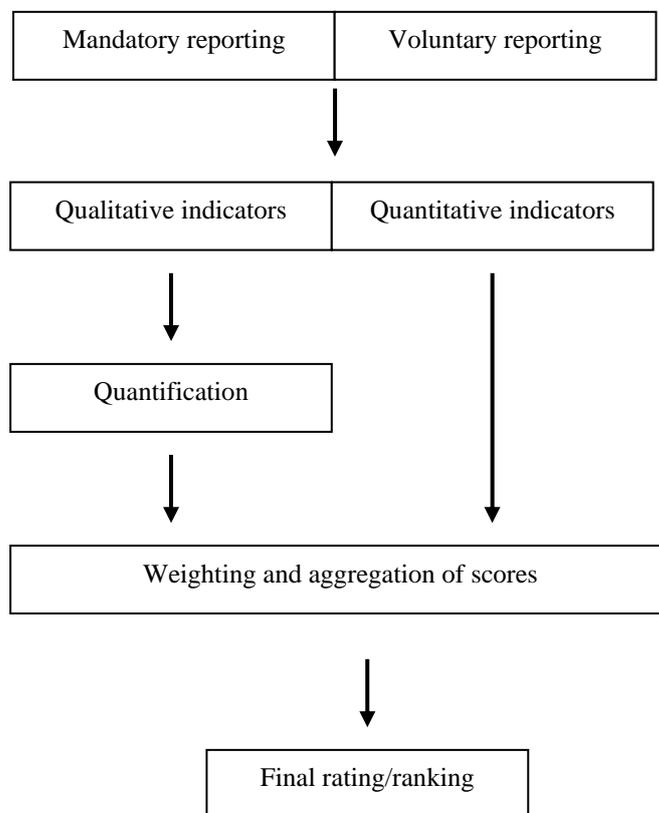
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3 See <http://www.globalreporting.org/>

**Figure 1: Relationships Between Pension Funds, their Members, Fund Managers and Investee Companies**



**Figure 2: The Reporting and Rating Process**



Funds cannot judge their own performance in an independent way. Nor can they quantify their qualitative indicators, as this requires subjective judgements and comparisons. The task of rating companies is usually done by independent rating organisations (commercial, academic or NGO-based) that use surveys and publicly available information to rate and then rank companies. These ratings can be used to create tradeable indices such as the Dow-Jones Sustainability Index, Domini400 Social Index or the FTSE4Good. They can also be published as corporate social responsibility indices to allow consumers and civil society to judge companies.<sup>4</sup> However, because most pension funds are not listed companies traded on stock exchanges, they are not rated by these organisations, resulting in less attention being paid to their SEE performance.

### **Existing Reporting Guidelines for Investors**

Current regimes for mandatory reporting of SEE issues are considered by many stakeholders as inadequate. This has led to a number of voluntary initiatives – that include indicators and reporting guidelines for investors – to be developed. *Table 1* contains a summary of the current indicators as they relate to investors.

### **Categorisation of Indicators**

When considering the issue of development of SEE indicators, two broad types of indicators emerge:

1. qualitative disclosures about policies, processes, activities and impacts;
2. quantitative indicators relating to specific and measurable aspects of a company's SEE performance.

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4 See <http://www.reputex.com.au> and [http://www.bitc.org.uk/programmes/key\\_initiatives/corporate\\_responsibility\\_index/](http://www.bitc.org.uk/programmes/key_initiatives/corporate_responsibility_index/)

**Table 1: Summary of Existing SEE Indicators for Asset Management**

<p><b>GRI Social Sector Supplement</b><sup>5</sup></p> <ul style="list-style-type: none"> <li>Asset Management Policy (socially relevant elements) (Qualitative; Text) Describe the social criteria applied by the reporting organisation in Asset Management. Criteria can cover products to foster social capital as well as the handling of sensitive issues in the business area. Examples for sensitive issues in asset management may be: responsible marketing (best advice), screening of portfolios against social criteria. The company may give examples on how the policy is implemented regarding sensitive issues.</li> </ul> <p><b>Fostering Social Capital</b></p> <ul style="list-style-type: none"> <li>Assets under Management with High Social Benefit (Quantitative; \$ and %) Report on provision of tailored and innovative products and services applying special positive ethical/sustainability criteria. Includes such investments in developing countries. Report on total amount and percentage of total Assets Under Management.</li> <li>SRI Oriented Shareholder Activity (Qualitative; Text) Describe activities with companies invested in, where CSR issues either are raised in communications with board and management or explicitly considered when exercising shareholder rights.</li> </ul>
<p><b>CERES</b><sup>6</sup></p> <ul style="list-style-type: none"> <li>Distribution of investments / managed assets: geographical, sensitive sectors (Qualitative) Products/ services designed for improving environmental performance or creating environmental benefit (Qualitative)</li> </ul>
<p><b>EPI-Finance</b><sup>7</sup></p> <ul style="list-style-type: none"> <li>Assets under green management, exclusion criteria (\$, %)</li> <li>Assets under green management, positive criteria (\$, %)</li> <li>Investments in unlisted environmental pioneer companies (#, \$, %)</li> </ul>
<p><b>Forge</b><sup>8</sup></p> <ul style="list-style-type: none"> <li>Level of holdings in environmental funds (\$)</li> <li>Funds subjected to environmental analysis (%)</li> <li>Breakdown of funds subjected to environmental analysis (\$, %)</li> </ul>

5 <http://www.globalreporting.org/guidelines/sectors/spi2001.asp>

6 [http://www.ceres.org/our\\_work/01\\_fin\\_form.doc](http://www.ceres.org/our_work/01_fin_form.doc)

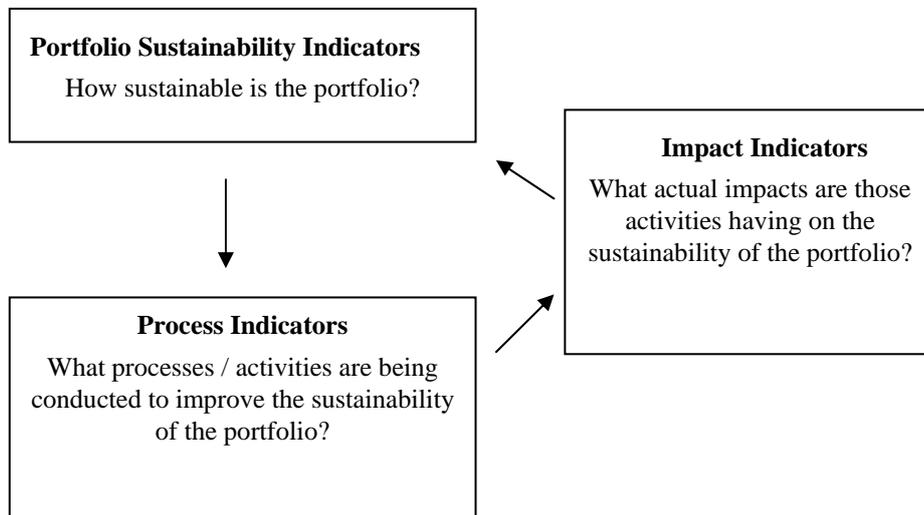
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8 [http://www.pwcglobal.com/gx/eng/about/svcs/environment/pwc\\_forge\\_text.pdf](http://www.pwcglobal.com/gx/eng/about/svcs/environment/pwc_forge_text.pdf)

As *Figure 2* above illustrates, qualitative information must be converted into quantitative data and weighted in order to rank funds.

Apart from being either qualitative or quantitative, SEE indicators for investors fall into three broad categories illustrated in *Figure 3*.

**Figure 3: Categorisation of Indicators**



**Portfolio Sustainability Indicators**

Portfolio sustainability indicators attempt to reflect the SEE performance of the portfolio as a whole. If a fund invests in environmental technology companies, these indicators would be high. If the fund invests predominantly in resource companies, they would most likely be significantly lower.

Examining the current initiatives in *Table 1*, it is the indicators describing the screening of portfolios that attempt to reflect the sustainability of the portfolio. Indicators such as “Assets under green

management” (EPI-Finance) and “Level of holdings in environmental funds” (Forge) attempt to reflect how ‘green’ or ‘socially responsible’ a portfolio is.

### Problems With Indicators that Describe the Extent of Screening

There are significant problems with using the amount and proportion of funds under social or green management as a proxy for the sustainability of a portfolio.

Take, for example, most Dutch pension funds, which exclude tobacco from their entire portfolios. They can claim 100% of investments are under a social screen, even though they screen out less than 1% of the market. Another fund might only apply a screen to 10% of its portfolio, but this may be a very strict screen that excludes 90% of the market.

If screening indicators only consider the *proportion of the portfolio under screening*, then they ignore an essential element required for judging the screen – that is, the extent or ‘strictness’ of the screen itself. One way to take into account the strictness of the screen is to multiply the proportion of the fund to which the screen applies by the proportion of the market screened out. This would result in an *effective* percentage of the fund under screening and would be a more appropriate measure of the overall extent of screening applied by a fund.

**Table 2: Comparing Screening Approaches**

	% of Fund Under Screening	% of Market Screened Out	<i>Effective % of the Fund under Screening</i>
<b>Fund A</b>	100	1	1
<b>Fund B</b>	50	50	25
<b>Fund C</b>	10	90	9

Although this is an improvement, there are still serious problems with using the extent of screening as a proxy for the sustainability of a fund. Screening indicators are of no use in judging those funds that do not use SEE screens – all of which are not equally *unsustainable*. Nor do they

attempt to distinguish between different types of screened funds with similar percentages under screening – all of which are not equally *sustainable*.

### **Using Third Party Ratings to Determine Portfolio Sustainability**

A better way of rating the sustainability of portfolios is to aggregate the sustainability indicators of the investee companies within that portfolio.

The leading sustainability rating organisations, if given the portfolio weightings of listed companies in a fund, should be able to compile a set of aggregated indicators for the fund based on the weighted average SEE performance of investee companies. These indicators would present a much clearer picture of the sustainability of the portfolio. It does, however, rely on the cooperation of rating organisations (and added cost).

A simple way for funds themselves to calculate the aggregated SEE performance of their portfolios would be to take the final rankings of companies published by a reputable rating organisation and calculate the weighted average ranking of their portfolio. This would allow the SEE performance of portfolios to be easily compared. This approach offers a superior way of representing the overall sustainability of a portfolio and would allow better comparisons to be made, not only between screened funds but also between non-screened funds. This, of course, would only be applicable to publicly listed companies, as they are the only ones included in these indices. The problem with this approach is that the current rating and benchmarking services are still in their infancy and their ratings are incomplete across markets and many are not publicly available. But in time, it is likely that comprehensive, robust indices that rank entire stock markets will be available.

### **Process Indicators**

Process indicators – also called input indicators – describe those activities undertaken by companies which are important inputs into the management and reporting of SEE issues. These indicators call for disclosure of environmental, labour and human rights policies, and systems such as shareholder engagement processes and screening methodologies. They require disclosure of various charters and codes of conduct to which a company has committed, and descriptions of monitoring, evaluation and auditing processes. Process indicators would also include descriptions of efforts that a fund has made to change the behaviour of investee companies (see the GRI indicator ‘SRI-related shareholder activity’ in *Table 1*). Quantifying these indicators involves judging the adequacy of these efforts.

Of the three types of indicators for asset managers, process indicators are the easiest to develop and the easiest to report on. But if these processes do not actually lead to any impacts, then, in themselves, they are of little use. That said, assessing portfolio sustainability and the actual SEE impacts of investment strategies is difficult, and therefore process indicators will remain the most important disclosures used for measuring the SEE performance of funds.

### **Impact Indicators**

Impact indicators – which could also be called output indicators – describe the actual impact on the environment or society. For investors, this generally means to what extent have they, through their activities, influenced the SEE performance of investee companies. Rather than looking at investors’ SEE performance as a passive reflection of the sustainability of the portfolio, impact indicators measure *what difference the investor actually made* through their actions (or inaction).

### **Impact indicators for shareholder engagement**

The GRI indicator ‘SRI-related shareholder activity’ can be seen as a process indicator, but it also has some impact aspects. If a fund had a successful negotiation with a company’s management on a SEE issue that led to changes in behaviour, this would count as an impact.

Since the purpose of shareholder engagement activities is to improve SEE performance of investee companies, the corresponding impact indicator should capture the effectiveness of such efforts.

The corporate governance lobby has recognised the importance of measuring the effectiveness of shareholder engagement activities. The UK-based Institutional Shareholders’ Committee<sup>9</sup> has published ‘The Responsibilities of Institutional Shareholders and Agents – Statement of Principles’. It states:

Institutional shareholders and/or agents should set out the circumstances when they will actively intervene and how they propose to measure the effectiveness of doing so. (Institutional Shareholders’ Committee, 2002)

The following indicators could be used to measure the effectiveness of shareholder activist/engagement activities:

- evidence of improvement in investee company SEE performance due to investor activities;
- number of shareholder resolutions withdrawn after successful negotiation with company management;
- proxy voting percentages achieved by SEE resolutions submitted or supported by the fund.

The effectiveness of engagement efforts is not easily measured for two main reasons. First, dialogue with companies is often conducted in private, and companies are reticent to admit that pressure from investors

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<sup>9</sup> Members in 2002: the Association of British Insurers; the Association of Investment Trust Companies; the National Association of Pension Funds; and the Investment Management Association.

is responsible for a change of behaviour. Second, it is very difficult to establish causation between the specific shareholder activity and the change in behaviour (Gillan and Starks, 2003).

On the first point, there must be a balance struck between the ability to conduct private dialogue and the desirability of openness and transparency. Private dialogue must not be removed as an option, as it can be very effective (Carleton, Nelson and Weisbach, 1998). But confidentiality must not become an excuse for denying members the information they need to make informed judgements about their pension funds and fund managers. One solution would be a confidential evaluation of the effectiveness of private dialogue by an independent third party (see Carleton *et al.*, 1998, for an evaluation of the effectiveness of private engagement in a leading US pension fund). Rating organisations would be well placed to provide such a service.

In judging investors' SEE performance, it is as important to measure *inaction* as it is to measure *action*. Passive investors in poorly performing companies should be held accountable for allowing poor behaviour to continue unchecked. If, for example, a responsible environmental resolution were to be submitted by another shareholder – and the fund abstained or voted against it – then the fund should be held accountable for supporting the continuation of the poor behaviour that led to the resolution. An important impact indicator would be the number of *losing* SEE resolutions *not supported* by the fund.

### **Impact Indicators for Screening**

Impact indicators also put screening activities in perspective. Funds that mostly employ screening approaches would only score well on their impact indicators where the screening strategy can illustrate changes in corporate behaviour. In equities markets, this would only be the case where the screening or divestment of stocks has an impact on the cost of capital or share prices. In large, efficient markets, stocks are good substitutes for each other. The effect of divestments and screening on the cost of capital and share prices, therefore, is likely to be insignificant unless a large proportion of investors agree to include or exclude a large

proportion of stocks in a market (Holthausen, Leftwich and Mayers, 1987; Holthausen, Leftwich and Mayers, 1990; Heinkel, Kraus and Zechner, 2001; Knoll, 2002).

However, if we consider screens that involve investments in sustainable venture capital that result in verifiable benefits to the environment or society, these would represent positive impacts.

Possible impact indicators for screened funds could include:

- evidence of SEE impacts that are due to the screen;<sup>10</sup>
- evidence that the cost of capital has decreased or increased for an investee company because of the investment (this would apply, in particular, to sustainable venture capital in unlisted companies or in companies in relatively illiquid markets where investment/divestment can significantly impact the cost of capital or share prices).

Indicators that measure the extent of screening were discussed above in the context of portfolio sustainability. Can they also be used as impact indicators if the impacts on the cost of capital are taken into account? One way of estimating the impact of screening is to include a variable that represents the extent to which the marginal investment into that market can impact the SEE performance of companies. For example, in a large, highly liquid market such as a major global stock market, the impact of screening is likely to be much lower than in a market for sustainable venture capital. For this exercise, one way of measuring the impact of screening is outlined below. The variable could be called the Marginal SEE Impact of Investment (MSII).

*Table 3* illustrates that when the impacts on the cost of capital are taken into account, a different picture emerges of the relative merits of various screening approaches.

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<sup>10</sup> See the case of Petrochina, where a boycott of a float of the company had a massive impact on the amount of money raised (see Simpson, 2002).

**Table 3: Assessing the Impact of Screening Strategies**

	Percentage of Portfolio Under Screen (PPUS)	Percentage of Market Screened Out (PMSO)	Marginal SEE Impact of Investment (MSII)	Impact of Screening Strategy
<b>Fund A</b> Listed companies in large stock exchange	100	1	0	0
<b>Fund B</b> Listed companies in small stock exchange	50	50	10	2.5
<b>Fund C</b> Listed companies in large exchange but with sustainable venture capital component	10	90	80	7.2

Note:  $PPUS \times PMSO \times MSII = \text{Impact of screening strategy}$

### Weighting of Indicators and Incentive Effects

When these indicators are quantified and aggregated by rating organisations, value judgements must be made about the relative importance of each indicator.

The different approaches to SRI are likely to yield vastly different results depending on which indicators are given higher or lower weightings. As discussed above, negative screening in large markets will improve portfolio sustainability indicators but may have little impact on corporate behaviour. Conversely, shareholder activists who focus on poorly performing companies may improve corporate behaviour but their portfolio sustainability indicators would remain relatively low.

In weighting the different types of indicators to come up with a single ranking for funds, the question must be asked: are these indicators

equally important? Is it more important to have an ‘ethical’ portfolio that doesn’t include ‘sin stocks’<sup>11</sup> or an SRI approach that changes corporate behaviour?

One of the goals of rating and benchmarking is to provide incentives for improvement in SEE performance, not only on the part of companies but also on the part of their owners – pension funds and fund managers. It could therefore be argued that weightings of indicators should be focused on those impacts that create the greatest incentive for change. That would lead to the conclusion that impact indicators should be weighted significantly higher than either process or portfolio sustainability indicators.

## **Conclusion**

Measurement of the SEE performance of pension funds is difficult, but it is becoming increasingly important given the expansion of the notion of fiduciary duty and the incorporation of SEE considerations into investment decision making. A tool or measurement device must be developed for pension funds and others involved in the investment process so that fund members, trustees, governments and civil society can make informed decisions about governance, policy and consumer choices.

Current indicators of portfolio sustainability that focus on the extent of screening are problematic because they do not take into account the diversity of impacts associated with various screening approaches. Alternative indicators have been proposed that more closely reflect the sustainability of portfolios and the actual impacts of investors’ activities.

When indicators are being combined for benchmarking purposes, the three types – portfolio sustainability indicators, process indicators and impact indicators – should be weighted in a way that reflects the goals of the reporting and rating process. If one of those goals is to create

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11 ‘Sin stocks’ refer to companies involved in such industries as tobacco and armaments, which have traditionally been excluded from most screened funds.

incentives and drivers for corporate change, then impact indicators are the most important and should be weighted accordingly. Given the size of pension funds and their widespread use of indexing strategies, the only way they can practically address SEE issues is through shareholder engagement activities. Preferencing impact indicators would not only put pension funds on a level playing field with niche SRI funds, but it would align the goals of the reporting and rating process with those of the rest of the sustainability movement – that is, to improve the environment and society.

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