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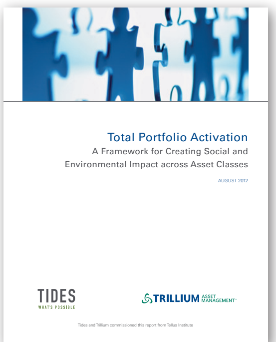
Total Portfolio Activation:
A Framework for Creating Social and Environmental Impact across Asset Classes

This summary is edited and condensed from the original paper which was prepared by Joshua Humphreys, Ann Solomon, and Christi Electris at Tellus Institute with research assistance from Jaime Silverstein. Visit www.trilliuminvest.com to download the complete paper.

Interest in investment that pursues social and environmental impact has exploded in recent years. Although opportunities for impact investing have emerged across asset classes, most impact-investment activity has remained largely confined to a limited array of private investments, touching only a small percentage of investor portfolios[1] For organizations and individuals seeking greater impact and better alignment between their investment activities and their mission or values, there remains a pressing need for tools to help investors identify and seize opportunities to activate more of their assets for social and environmental benefit.


Total Portfolio Activation
A Framework for Creating Social and Environmental Impact across Asset Classes
AUGUST 2012
TIDES
TRILLIUM ASSET MANAGEMENT
Tides and Trillium commissioned this report from Tellus Institute

Prepared by Tellus Institute, an interdisciplinary not-for-profit research and policy organization based in Boston, MA – with the guidance and close collaboration of Trillium and Tides – Total Portfolio Activation (TPA) provides concrete steps to help institutional investors begin working toward a fuller activation of their portfolio in support of their mission.

Building upon the long-standing work of socially responsible money managers, corporate accountability researchers, community investors, and institutional investors from the philanthropic and faith communities, as well as more recent efforts of impact investors and Slow Money advocates, TPA provides both a framework and a set of analytical tools to help mission-driven investors understand the specific impact opportunity set that can be pursued across every asset class in their portfolios.

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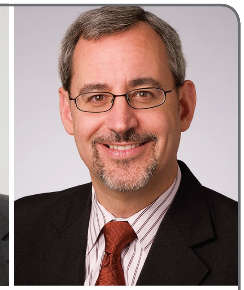
1. See Yasemin Saltuk, Amit Bouri, and Giselle Leung, Insight into the Impact Investment Market, J.P. Morgan and the GIIN, December 2011, available at http://www.thegiin.org/cgibin/iowa/resources/research/334.html (accessed April 13, 2012), which found that private debt and private equity collectively account for 90% of impact investments in asset-weighted terms. Additionally, the investor survey found that High Net Worth Individuals projected allocating a median of 10% to impact investments in 10 years time, while institutions projected a 5% allocation to impact.

Dear Reader

by
Melissa Bradley, CEO of Tides,
&
Matt Patsky, CFA, CEO



For decades, our organizations have been proponents of an investor's responsibility to leverage ownership for positive social and environmental impact – across all asset classes. We know that every decision we make, whether as donors, consumers or investors, has an impact. We may not be aware of the impact, or be able to measure it, but the impact, nevertheless, exists.

The concept of making investments to solve social or environmental challenges while generating financial returns isn't new, but investors' attention to "impact" has grown rapidly in the past few years. There remains a need for tools to help investors identify and seize opportunities to activate more of their assets for social and environmental benefit.

To help fill this gap, Tides and Trillium recently engaged Tellus Institute to write a paper that could be used by investors who are seeking to generate greater environmental or social value in their portfolio.

The Total Portfolio Activation (TPA) framework – which was recently published in guidebook form – provides an analytical recognition of the specific activities that increase the potential for social and environmental impact both within and across asset classes.

To help mission-driven investors pursue impact across asset classes in these ways, TPA involves ten key steps that take investors from evaluation and analysis to identification of opportunities, and then from implementation to ongoing assessment. The underlying tools in TPA can be tailored to specific investment types: whether private-equity investments in sustainable businesses or public-equity investments in listed securities; from debt investments in micro-finance institutions, bond funds and other fixed-income instruments to highly liquid, money market investments in community development financial institutions; and from real estate investments in the built environment to investments in other real assets such as timber and farmland.

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An enormous un-tapped opportunity for impact lies in the public equity asset class, which is often one of the largest allocations in an investment portfolio. Relatively small shareholders in large publicly traded corporations routinely catalyze networks of like-minded investors to press for substantial changes in the way companies do business, impacting the lives of hundreds of thousands of employees, stakeholders and consumers. Investors have enormous and unrealized opportunities to pursue impact through public policy. Whether through financial reform and regulation, strengthening reporting requirements related to ESG issues, defending shareholder rights, or bolstering government support for community investment, investors can have impact in policy decisions.

By adding active ownership strategies to existing ESG investment analysis and selection – as outlined in this paper – investors can exponentially increase the positive social and environmental impact of their investments.

TPA walks investors through a deliberate process to identify the specific impact opportunity set tailored to their areas of social or environmental concern – and then to revise their Investment Statement and re-allocate their portfolios accordingly.

The TPA concept works, not only for donors and foundations, but for any investor seeking positive social and environmental impact or alignment across every asset class.

We look forward to a day when individual and institutional investors talk equally about their impact returns and their investment returns.

Melissa Bradley

Melissa Bradley, CEO of Tides, is known for creative and innovative leadership within the social entrepreneurial landscape. Under Melissa's leadership, Tides has made over 1100 donor contributions, distributed over 3300 grants, providing over $96M in grant dollars in the last year. Prior to Tides, Melissa founded and served as managing director of New Capitalist, an organization leveraging human, financial and social capital to create economically profitable and sustainable individuals, businesses and communities. She facilitated over $20M in venture capital for seed stage companies. She got her start in the private sector as a VP at UBS in the Private Client Group, and as a Financial Regulatory Affairs Fellow with US Department of Treasury.

Important Disclosure

TRILLIUM
ASSET MANAGEMENT®

Investing for a Better World®
711 Atlantic Avenue
Boston, MA 02111
617-423-6655
lmackinnon@trilliuminvest.com

Editor
Randy Rice

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If you would like to receive this publication via email, please send a request to rrice@trilliuminvest.com.

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Is "Too Big to Fail" Too Bad to Own?

Seth Magaziner

One year ago, tens of thousands of people took to the streets across the United States to protest the behavior and influence of the world's major financial institutions. Their frustrations were well founded. Over the past decade, Wall Street behemoths inflated one of the greatest asset bubbles the world has ever seen, and when their risky gamble finally popped, taxpayers were left footing the bill. Far from expressing regret for their actions, many banking industry titans used bailout money to hire armies of lobbyists to fight against financial reform in Washington, and on generous bonuses for themselves. As America slowly recovers from a recession that destroyed over eight million jobs and $16 trillion of household wealth, the role of "Too Big to Fail" banks has emerged as one of the most pressing social issues of our time.

Too Big to Fail Banks (TBTFs) pose an interesting conundrum for socially responsible investors. On one hand, there are proven economies of scale in banking. The ability to spread costs across a large number of customers has allowed banks with over $1 billion in assets to achieve a higher return on assets than their smaller peers over the last two decades, while often providing more affordable loan terms to their customers.[1] Large banks offer the convenience of widespread branch and ATM networks and a broad array of product offerings. As in all industries however, there is a tipping point beyond which greater size becomes a disadvantage. A good argument can be made that the world's largest financial institutions have become so big and so complex that they are now "too big to manage" even for those executives who have the best of intentions. This is especially troubling because, as we are all now painfully aware, when a financial institution reaches a significant size, its failure threatens the health of the entire economy.

What is a socially responsible investor to do? For those who choose to invest in a focused portfolio, like Trillium's Sustainable Opportunities model, which is free to deviate from the industry weightings of a benchmark index, it is possible to avoid the TBTFs and focus instead on smaller banks that have demonstrated superior growth, profitability and social awareness. Responsible regional banks like Oregon-based **Umpqua Holdings** (NASDAQ: UMPQ), which offers a green lending program to finance energy efficiency retrofits for homes and offices, and **Webster Financial** (NYSE:WBS), which was recently profiled on ABC News for its efforts to modify rather than foreclose on the loans of struggling homeowners[2], have both significantly outperformed both the S&P 500 Index and the KBW Regional Bank Index over the past year.[3]

For benchmarked products like Trillium's Large Cap Core and All Cap Core models, which have stock holdings designed to mirror the industry weightings of the S&P 500 and 1500, respectively, the task of choosing which bank stocks to incorporate is far more challenging.

The ten largest banks in the United States together account for greater than forty percent of the financial sector's representation in the S&P 500.[4] Simply excluding the TBTFs from a product benchmarked to the S&P 500 or S&P 1500 is not a viable option because they make up too large a share of both indices.

TBTFs are large and complex organizations, and a number of factors must be examined in identifying the social leaders and laggards among them. For now, let's focus on three factors that have especially profound social impacts.

Executive Compensation. The oversized compensation awarded to executives of the largest banks has rightfully received a great deal of public scorn. However, it is not just the size of pay packages that should draw careful scrutiny but also the composition of those packages.

Bank executives best serve their shareholders and society at large by pursuing policies that will lead to steady, sustainable growth. Far too often top bankers are compensated based on the short-term performance of their company's shares, thus incentivizing the types of misrepresentation and risk taking that became all too prevalent in the years leading up to the 2008 market collapse.

In order to align management incentives with the best interests of shareholders and society, compensation should consist mainly of stock that vests gradually over a long time period, with strong claw-back policies for misbehavior. Bank managers must be required to live with the long-term consequences of their actions.

HSBC (NYSE:HBC) is an example of a large bank with a stronger than average executive compensation policy. As much

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1. Federal Deposit Insurance Corporation Quarterly Banking Profile data, Q1 1990-Q2 2012.

2. http://abcnews.go.com/US/bringing_america_back/bank-thing/story?id=15208640

3. Price data as of September 20, 2012.

4. As of September 20, 2012, the ten largest U.S. banks by assets had a combined market capitalization of roughly $825 billion, compared to a total market cap of $1.95 trillion for the S&P 500 Financials Index.

Total Portfolio Activation *(continued)*

Continued from page 1

The TPA framework is applicable to any investor seeking to generate greater environmental or social value, and its underlying tools can be tailored to very specific issue areas of concern, whether they be climate change or human rights, women's empowerment or affordable housing, nature conservation or Lesbian, Gay, Bisexual, Transgender, and Queer (LGBTQ) equality, economic development among Native Americans or fair trade with small farmers in low-income countries. We believe that the tools are particularly helpful to foundations, endowments, faith-based investors, nonprofits, and other mission-driven organizations looking to align their investments with their programmatic goals and values.

A Note on Inspiration: Although the concept of "Total Portfolio Activation," as elaborated here, is new, it owes important debts to earlier notions rooted in concerns about aligning philanthropy and finance, such as Jed Emerson's "total foundation asset management and the unified investment strategy" and Carol Newell's more geographically targeted notion of "whole portfolio activation." The framework of Total Portfolio Activation aims to extend the concerns of these pioneering philanthropic concepts to the portfolios not simply of donors or foundations but of any investor seeking greater social and environmental impact across every asset class in a portfolio.

The framework also provides an analytical recognition of the specific activities that increase the potential for social and environmental impact both within and across asset classes — from private-equity investments in sustainable businesses to public-equity investments in listed securities; from debt investments in micro-finance institutions, bond funds and other fixed-income instruments to highly liquid, money market investments in community development financial institutions; and from real estate investments in the built environment to investments in other real assets such as timber and farmland.

We have prepared TPA as a guide that provides concrete steps to help any institutional investor begin working toward a fuller activation of their portfolio in support of their mission, drawing upon specific examples of investors who have already activated assets in certain asset classes. In the report, we highlight the efforts of numerous mission-driven institutional investors that have begun to seize opportunities for greater impact within their portfolios.

In this newsletter, we have included three of the TPA case studies including The Dominican Sisters of Hope, a Roman Catholic religious congregation in New York; Equity Foundation, a community foundation in the Pacific Northwest supported by donors drawn from the LGBTQ community and the Oneida Trust, a Native American institution responsible for managing the trust funds of the Oneida tribal nation in Wisconsin.

Asset classes are the central focus for the Total Portfolio Activation framework because each has distinctive social and environmental functions, as emerging research has begun to show[2]. TPA concentrates on five asset classes commonly found in a diversified investor's portfolio:

- Cash and cash equivalents;
- Fixed income;
- Public equities;
- Private equity; and
- Real property.

We identify four related areas of activity where opportunities for impact can be readily seized within each asset class:

1. Investment selection – incorporating environmental, social or governance (ESG) issues and impact into investment review, decision-making and performance analysis. Investors will have specific criteria related to environmental or social issue areas or targeted geographies around which they structure their investment selection process and then monitor their impact.

2. Active ownership – exercising the stewardship rights and responsibilities, voice and votes, that often accompanies owning an asset. Investing in assets can often open opportunities to engage in activities as an owner, whether directly or indirectly.

3. Networks – joining wider groups and coalitions of stakeholders around common environmental and social issues of concern, in order to leverage collective power to generate greater impact than any single investor could on its own.

4. Policy – engaging in public-policy activities as an investor in order to tap government resources and incentives or encourage regulatory oversight and intervention in support of impact objectives. Policy activity acknowledges the potential role government support, regulation and intervention can play in the investment process to encourage positive social and environmental outcomes.

Each activity area can be applied within each asset class, although the relative importance of each activity for increasing potential impact will vary for each asset class and depend on the investor's specific social or environmental concerns or goals. The process of selecting an investment because of its impact attributes is key for every asset class, but we have also found meaningful opportunities to increase the potential for impact in the other

Continues on page 5

2. See, for example, Steve Lydenberg, "Beyond Risk: Notes toward Responsible Alternatives to Investment Theory," working paper, September 28, 2009, available at http:// www.unpri.org/files/Lydenberg_PRI2009.pdf; David Wood and Belinda Hoff, Handbook on Responsible Investment across Asset Classes, Institute for Responsible Investment, Boston College, Carroll School of Management, 2007, available at http://www.cof.org/files/images/ExecEd/bcrespinvesthndbk.pdf; and "Investing for Impact: Case Studies across Asset Classes," Bridges Ventures and Parthenon Group, n.d. [2010], available at http://www.parthenon.com/ThoughtLeadership/InvestingforImpactCaseStudiesAcrossAssetClasses (accessed April 13, 2012).

Total Portfolio Activation *(continued)*

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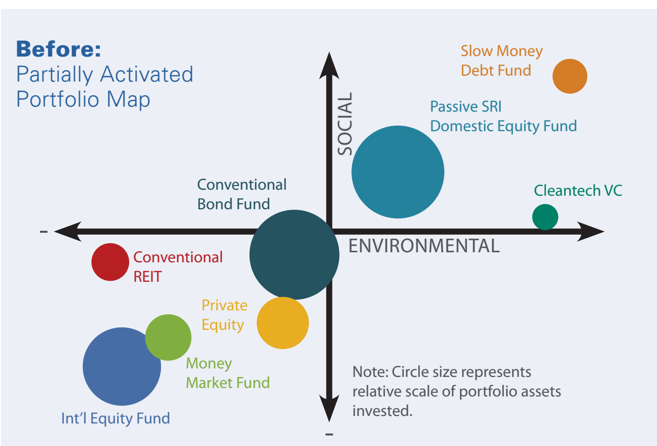
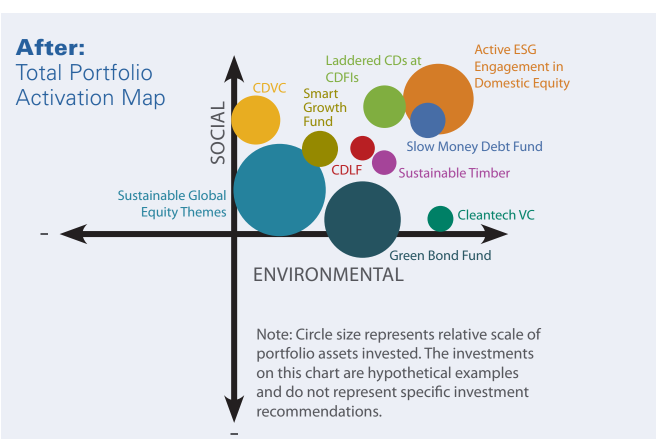
activity areas as well: by taking more active ownership of assets, joining with other stakeholders in networks of common concern, and using policy tools and strategies.

Specific asset classes are also better suited for generating particular kinds of impact, so investors with targeted issue areas of concern will need to place greater stress on the activities and investments that align with their impact objectives. Cash and fixed-income investments in community development financial institutions, for example, are particularly useful ways to support affordable housing in targeted, low-income geographies. Active ownership initiatives, by contrast, appear particularly germane to investments in public and private equity and real assets, though they take very different forms in each asset class, ranging from high-impact shareholder engagement with publicly traded companies, to directly influencing companies through a board seat in private equity, to sustainably managing timberlands in real assets.

Consequently, an institution might work on multiple issues related to its core mission, but vary the focus across the portfolio to match the specific opportunities presented by each asset class.





For example, a local environmental organization may find geographically targeted investment opportunities to finance green building or regional land conservation efforts in cash and real property asset classes, but pursue broader national or global climate-related investing strategies using active ownership in public equities, while supporting renewable energy innovation through cleantech venture capital in private equity.

Ultimately, each investor will therefore need to assess the primary social and environmental issue areas that are core to its mission and then evaluate the activities within each asset class that are most appropriate for increasing its potential for impact in those areas. The TPA framework provides a clear process for identifying what we term an investor's "impact opportunity set," by assessing the impact activities and investment opportunities within each asset class of its portfolio that are most relevant to increasing potential social or environmental impact.

Additionally, TPA indentifies ten key steps that investors can take in order to implement the TPA framework:

1. Take an inventory of environmental and social issues of concern;
2. Evaluate the impact of current investment activities across asset classes;
3. Identify the Impact Opportunity Set specific to issues and asset allocation;
4. Conduct a "gap" analysis between current activities and the Impact Opportunity Set in order to identify new areas of activity that will increase impact potential;
5. Identify specific investment opportunities that fill the gaps analyzed;
6. Revise Investment Policy Statement to reflect new strategy of Total Portfolio Activation, specifying how impact issues shape investment selection, active ownership, network participation, and policy initiatives across asset classes;
7. Conduct a capacity analysis in order to determine which investment activities can be taken directly by the investor and which should be delegated to experienced impact asset managers;
8. Re-allocate assets to higher impact investment opportunities identified;
9. Monitor portfolio performance according to impact objectives; and
10. Continually assess ongoing Total Portfolio Activation impact opportunities according to Investment Policy Statement.

TPA also guides investors through the kinds of opportunities that exist across asset classes commonly found in a diversified portfolio, before turning to an example of how a mission-focused investor can use the 10-step process of identifying its impact opportunity set and re-allocating assets across its portfolio.

Total Portfolio Activation: A Framework for Creating Social and Environmental Impact across Asset Classes can be downloaded at www.trilliuminvest.com

Dominican Sisters of Hope:
Expanding Ownership Impact Opportunities Through Networks

The Dominican Sisters of Hope, a congregation of Roman Catholic nuns based in Ossining, New York, have managed to enhance their influence over major corporations on a wide range of social and environmental issues by working with experienced asset managers like Trillium and through networks of like-minded investors like the Tri-State Coalition for Responsible Investment. Promoting social justice is core to the congregation's work and the Sisters have developed a set of policy positions on social and environmental issues they believe are particularly critical to their mission, including immigration reform and stances against the death penalty, genetically modified crops, nuclear weapons, and human trafficking. The Sisters' investment activities are guided by these concerns and the congregation regularly participates in shareholder resolutions and dialogue activities when it can generate impact on these issues.

In 2011, the Sisters worked in collaboration with the Interfaith Center on Corporate Responsibility and End Child Prostitution and Trafficking USA (ECPAT-USA) to persuade Delta Airlines (NYSE:DAL) to be the first airline to sign the Code of Conduct for the Protection of Children from Sexual Exploitation in Travel and Tourism. Signatories of the Code commit to establish ethical policies on the commercial exploitation of children, to include language on child trafficking in their supplier contracts, and to provide trainings to their employees on this issue. The proactive work of corporations like Delta is a vital component to curtailing this atrocious industry. More recently, the congregation has been actively involved in a campaign to compel GEO Group (NYSE:GEO) to adhere to the Universal Declaration of Human Rights in the management of its 116 prisons globally.

Equity Foundation:
Supporting Diversity Through Shareholder Engagement

Portland-based Equity Foundation was founded in 1989 by a group of LGBTQ Oregonians who, in the wake of local homophobic ballot initiatives, sought "to eradicate prejudice against gender and sexual minorities" and "build communities that advance dignity and the worth of all people." As a philanthropic foundation, Equity Foundation initially focused on realizing its mission through grantmaking in Oregon and southwest Washington but soon came to view its endowment investments as an "untapped potential" for expanding the foundation's impact. Working in partnership with Trillium Asset Management, its investment manager, Equity Foundation's investment activities have helped catalyze substantial changes in corporate policies and practices with broad impact for LGBTQ people. Equity Foundation has further magnified the impact of its investment activities through networks, by providing a platform for the foundation's donors to work in concert with other organizations and wider social movements.

When Equity Foundation learned in 2010 that Target (NYSE:TGT) and Best Buy (NYSE:BBY) had made contributions to a political action committee supporting a Minnesota gubernatorial candidate outspoken in his opposition to same-sex marriage, the Foundation felt compelled to divest from both companies. However, Equity Foundation continued to engage in dialogue with the companies about its concerns. Working alongside a wider campaign that included consumer boycotts, petitions, and flash-mob protests, Equity Foundation was able to raise its distinctive voice as an investor and ultimately gained a receptive hearing. Within months of the campaign's start, Target's CEO apologized for the shortsightedness of its political contribution and committed to re-evaluate the company's political spending guidelines.15 As a result, Target is now back on the Foundation's "buy list."

In 2011, Equity Foundation took a more direct active ownership approach to advance LGBTQ rights at Lowe's (NYSE:LOW), the hardware retail giant. Equity Foundation's public campaign in combination with Trillium's 30-years of experience with shareholder activism led to a swift adoption of the proposal made in the Foundation's shareholder resolution—the addition of "gender identity or expression" to the corporation's Equal Employment Opportunity policy. By establishing a protection of gender expression at Lowe's, Trillium and Equity Foundation created an immediate impact in the lives of LGBTQ workers at Lowe's, which employs over 200,000 people across North America. Equity Foundation's shareholder advocacy continues in an ongoing campaign to compel AFLAC, Inc. (NYSE:AFL) to offer domestic partner benefits. Equity Foundation's successful activism demonstrates that even an investor with relatively small stakes in large publicly traded corporations can activate its portfolio in strategic ways to create real impact through investment.

TPA CASE STUDIES

The Oneida Trust: *Stewardship of Native American Assets*

The Oneida Nation of Wisconsin's Trust Committee was founded in 1974 to oversee management of assets awarded to the Oneidas by the US federal government after the settlement of nearly 200 years of disputed treaties and land claims. The Oneida Trust's funds are now directed toward a number of benefits for tribe members ranging from pensions for elders to scholarships for higher education to Oneida language revitalization efforts. In 1999, the Oneidas began a process of re-aligning the Trust's investment policy statement around the core values of the tribe, and since then the Trust has worked with its investment managers, Trillium Asset Management and Walden Asset Management, to incorporate socially responsible investment analysis and selection into the management of its funds and its activities as a shareholder. As part of its overall investment strategy, the Trust Committee incorporated explicit language about its social and environmental goals, recognizing "the responsibility to invest in a manner that does not enable harm to the environment or the spiritual and cultural values of Native Americans. The Trust Committee prefers to invest in companies that make positive contributions to alleviating the problems facing society and the environment."

The investment policy goes on to specify community development investments as an important strategy to generate positive impact. Consequently, the Trust's cash allocation includes deposits in Lakota Funds, a community development financial institution that makes micro-loans to entrepreneurs and small businesses on the Pine Ridge Indian Reservation in South Dakota. The Lakota Fund's investment and technical assistance activities, capitalized by depositors such as the Oneida Trust, have consistently increased real incomes and wealth in one of the most persistently impoverished Native American areas while creating wider social benefits.

The Trust also instructs its managers to support shareholder resolutions "of particular importance to the Oneida Nation and to other Native American groups or lands." However, the Oneidas' active ownership activities go well beyond this statement in their investment policy. Since the late 1990s, the Oneida Trust has leveraged its public equity investments to realize positive change by working with Trillium and Walden to file or co-file shareholder resolutions and engage in dialogue with several companies in solidarity with Native American advocacy efforts around the country and with indigenous peoples internationally.

In 2005, the Trust became concerned about the pollution of Onondaga Lake near Syracuse, New York, a Superfund Site described as one of the nation's most polluted lakes due to industrial contamination from the operations of Allied Corporation, which had merged with Honeywell (NYSE:HON) in 1999. Onondaga is a brethren Tribe of the Oneida in the Iroquois Confederacy who live near the lake and consider it sacred. The Trust contacted Trillium to see if there was a way to file a resolution with Honeywell International in order to support the historical land claims of the Onondaga Nation and to help clean up Onondaga Lake. Trillium identified a client which held shares in Honeywell and filed a resolution on their behalf. In this way the Trust helped amplify the marginalized voices of the Onondaga Nation in its negotiations with Honeywell over the ongoing cleanup of the lake.

The Trust is also actively involved with networks like US SIF's Indigenous People's Working Group, First Nations Development Institute, and the Interfaith Center on Corporate Responsibility (ICCR) to engage with companies not only on Native American issues but also on human rights, environmental impact and indigenous peoples concerns internationally, including engaging with ConocoPhillips (NYSE:COP) over environmental damage from legacy oil and gas operations in Ecuador.

Trillium Asset Management is pleased to announce that David W. Walker, CFA, CMT has recently joined the firm as an equity analyst. Mr. Walker brings over 20 years of investment experience, having earned a Chartered Financial Analyst designation in 1993 and a Chartered Market Technician designation in 2002. Prior to joining Trillium, Mr. Walker was a Financial Advisor with UBS' Boston office. Earlier in his career he co-managed the Morningstar five star Van Kampen Emerging Growth Fund and the Van Kampen Aggressive Growth Fund.

"David is great addition to Trillium's investment team", said Matt Patsky, Trillium's CEO. "His experience complements our existing team and ensures that the firm remains well positioned to provide investment products that are tailored to reflect the environmental, social, and governance concerns of our clients."

Trillium Asset Management, LLC
711 Atlantic Avenue
Boston, MA 02111

Too big or too bad? *(continued)*

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as 60 percent of an HSBC executive's annual compensation is awarded based on financial and nonfinancial metrics that look back over a three year period and cannot be claimed for five years or until retirement, whichever comes last. While this policy still allows pay packages to be quite large, the structure of HSBC's pay packages promotes a "long-termism" that other banks should emulate.

Risk Posed to the Stability of the Financial System. Measuring the risk that large banks pose to the financial system as a whole is a complex and controversial endeavor. Some experts, like MIT Professor Simon Johnson, focus largely on the size of banks in measuring their contribution to systemic risk. Researchers at New York University have devised a ranking system based on projections of how much capital financial institutions will have available to absorb losses during times of market turmoil. The Basel committee, an international consortium of financial regulators, recently introduced a complex framework for measuring a financial firm's contribution to systemic risk that considers size, footprint, interconnectedness, complexity of operations and how easily each institution's business lines can be replaced by other firms.

All of these frameworks are useful in gauging a bank's contribution to the riskiness of the financial system. However, when judging a bank's risk profile it is important not only to look at a single snapshot in time, but also at a trend across time. Most of the TBTFs engaged in risky behaviors before the financial crisis, but which have taken the strongest measures to clean up their act since 2008?

Citigroup (NYSE: C) was unquestionably one of the bad boys of the financial crisis and would almost certainly be out of business today had the bank not received more than $40 billion in government bailouts. Since 2008, however, Citi's management has successfully reduced the troubled assets on their balance sheet from over 30 percent of total assets to 10 percent and falling. They have exited many of the riskiest business lines that brought them to the brink during the financial crisis and are doubling down on traditional retail and investment banking, particularly in emerging market countries. Citi's risk profile is still a long way from perfect and its performance on the recent Fed stress tests indicates further room for improvement, but the positive strides made in just three years are encouraging.

Environmental Profile of Loan Portfolios. The environmental footprint of a bank's everyday operations is minor compared to firms in other sectors like manufacturing, energy production or mining. However, the TBTFs make trillions of dollars of loans to companies operating in these industries, and thus can have a significant indirect environmental impact. Banks that rely on financing environmentally or socially harmful projects for a significant portion of their revenue place themselves in a precarious ethical and financial position, as the sustainability of their borrowers' business models are threatened by the potential for scandal, litigation and shifts in regulation. Trillium prefers investing in banks that integrate environmental factors and community impacts into the due diligence they perform on new lending opportunities, and we especially favor those banks that require their borrowers in sensitive industries to implement environmental and community impact policies that go beyond legal minimums.

Royal Bank of Canada (NYSE: RY) earned the praise of the Rainforest Action Network and other environmental advocacy groups last year after unveiling a new policy on Environmental & Social Risk Management for its capital markets business.[5] Under this policy, detailed environmental diligence will be a required part of all financing decisions for projects in high-impact industries such as energy, forestry, mining and chemicals. The policy also includes strong language on indigenous people's rights, including an affirmation that projects will only be financed if they have documented free, prior and informed consent of affected native peoples. Since unveiling the new policy, RBC has outperformed the S&P/TSX Toronto stock exchange index by over 17%.[6]

There are a number of other factors that must be considered in identifying social leaders and laggards among Too Big To Fail banks, including foreclosure-related abuses, promotion of payday-lending type products, excessive and misleading customer fees, and policies regarding political spending and lobbying. All of these issues play a crucial role in Trillium's investment decisions for the banking industry.

The protesters of the Occupy Wall Street movement brought the excess and irresponsibility of modern banking to the attention of the world. The banking industry needs sweeping change, both regulatory and cultural, to adequately protect shareholders and society from undue risk. In the meantime, socially responsible investors can and must do their part, by separating the bad from the ugly by favoring banks that are better aligned with a sustainable future.

5. http://understory.ran.org/2010/12/22/rbc-takes-a-step-away-from-tar-sands/

6. Price data as of September 20, 2012.