

BARC Response to the ALA Council Regarding the Resolution on Socially Responsible Investments for the ALA Endowment Fund

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During the Midwinter 2018 meeting, ALA Council referred the Resolution on Socially Responsible Investments for the ALA Endowment Fund to BARC. Since February, BARC, the Finance and Audit Committee, and the Endowment Trustees have researched the financial implications of the resolution and provide the following information for ALA Council and the Executive Board.

Increase the percentage of Endowment funds invested in socially responsible portfolios in a practical manner every year for the foreseeable future.

As of 4/30/18, 25.3% of the Endowment is invested in ESG (Environmental, Social, and Governance) classified funds. Since 2002, the Endowment ESG ratio has steadily increased while maintaining a diversified portfolio to help the Endowment withstand market volatility. The Endowment Trustees continue to consider the mix of investments to provide the greatest return on investments while being socially responsible. The Endowment was \$45.9 million at the end of 2017, funding critical services and initiatives advancing the association. Mandating an even larger investment in ESG during an unpredictable financial market will place the investment earnings at risk. The Endowment Trustees have been steadily increasing ESG investments and will continue to do so in a prudent manner as the market and options continue to evolve. BARC agrees with the Endowment Trustees that the proposed directive to the Endowment Trustees will negatively impact Endowment earnings affecting the availability of resources for the ALA budget.

Exclude from the Environmental, Social and Governance/Socially Responsible Investments (ESG/SRI) portfolios all fossil fuel investments, notwithstanding any socially responsible designations by any company or organization.

The Endowment Trustees work closely with their investment advisor Merrill Lynch to determine the mix of investments supporting the goals of ALA. Within the ESG investment sector, many energy companies in the portfolios include both renewable and fossil fuel energy, further complicating the ability to fully separate certain investments within mutual funds.

Clearbridge Investments, the primary (20.5% as of 4/30/18) ESG vehicle held by the Endowment, developed its own definitions regarding fossil fuel investments that

represent stricter criteria than most other ESG fund definitions, thus providing a greater confidence in companies included in the Clearbridge portfolio.

The Resolution also suggests that customized client screens might be utilized to further separate fossil fuel holdings in Clearbridge. While this appears to be a simple way to address one of the key concerns expressed in the resolution, Clearbridge Investments and Merrill Lynch have shown this is not prudent. Removing specific stocks within mutual funds requires those assets be invested in cash only rather than rebalanced in other investments within the fund. This will result in a negligible return from the cash portion of the fund and will negatively affect the fund's performance. Finally, decreasing the performance of a portion of the Endowment's holding will result in a negative investment return for the ALA Endowment as a whole.

Report on progress made towards these goals at least annually to the ALA Council and membership.

The Endowment Trustees provide regular reports to the ALA Council, Executive Board, BARC and Finance and Audit Committee. These reports are posted on the ALA Treasurer's webpage. The reports already provide ESG investment details. BARC does not see the need for additional reporting since ESG details are already included within existing reports.