

The Social Investment Forum Priorities for Financial Regulatory Reform

In our January 2009 submission to the Obama transition team, among other priority items, the Social Investment Forum¹ urged the Obama Administration-elect to:

- Establish clear parameters and effective regulations for the financial system that seek to protect and further the public interest, not simply the often short-term interests of financial institutions;
- Require transparent assessment of financial as well as environmental, social, and good governance factors by all publicly traded companies;
- Support reform in executive compensation policies allowing for say on pay and access to the corporate proxy ballot so that long-term shareholders have a say in the nomination of corporate directors and in protecting shareholder value;
- Take a critical look at lending policies and create more accountability in the lending marketplace;
- Create more opportunities for financially struggling homeowners to restructure their mortgages, helping them stay in their homes and out of foreclosure².

Socially responsible or sustainable investors use capital to promote clear and responsible corporate governance; to increase disclosure and therefore accountability; to address corporate, environmental and social shortcomings—from outsized carbon footprints to human rights violations in the global supply chain; and to support community investing institutions that strengthen low-income communities through access to capital. SRI investors work to enhance the bottom lines of their portfolio companies and, in so doing, seek to deliver sustained long-term wealth to shareholders.

We believe that action on financial reform must support good governance, transparency, stronger regulations for investor and consumer protection, and concerted attention on environmental and social issues within businesses and financial institutions. We also believe that the recent marketing of financial instruments worth trillions of dollars with inadequate transparency and regulation has led to spectacular market failures. It is clear that allowing the industry largely to police itself and determine its risk levels is unacceptable.

We thus support the general direction and many of the specifics of the Obama Administration's efforts to strengthen transparency, disclosure and regulation in the financial system as outlined in: *Financial Regulatory Reform: A New Foundation*.

The financial reform priorities of the Social Investment Forum are:

- 1) **Improved Corporate Governance:** Corporate governance principles that are supported by SIF members include allowing board slates to be nominated by shareholders, separating the Chair and CEO board positions and mandating shareholder votes on executive compensation ("say on pay"). Several of these areas are covered by the Administration's proposal and we support H.R. 3269 – the Corporate and Financial Institution Compensation Fairness Act of 2009. We have submitted a comment in response to the SEC's Rule Amendments to Facilitate Rights of Shareholders to Nominate Directors and made clear our support for proxy access. We also urge passage of legislation that will ensure the ability of shareholders to nominate board candidates.

¹ www.socialinvest.org

² http://www.socialinvest.org/pdf/Obama_Policy_Pri_2009.pdf

2) **Disclosure on Environmental, Social and Governance Factors:** We believe that it is critical to require corporations to disclose environmental, social and governance (ESG) information to their shareholders and the public. The Social Investment Forum has submitted a proposal to the SEC, signed by more than 80 domestic and international organizations, calling for the SEC to set a uniform standard for mandatory ESG reporting using the Global Reporting Initiative's framework³. While ESG disclosure is not in the Administration's proposal, we believe this initiative complements the principles outlined in the document. Therefore, we urge the Administration to support this effort and to encourage the House and Senate to include mandatory ESG disclosure in their financial reform packages.

3) **Regulation and Oversight of all Investment Products:** All investment vehicles, including hedge funds, should be required to register with the appropriate agency, and their positions should be disclosed to those agencies. Hedge funds manage a substantial amount of funds using leverage and pose potential systemic risks to the financial system.

We are particularly concerned that unregulated derivatives create unnecessary risks for our clients, investors and the financial system as a whole. We believe that these investments should be registered and overseen by the appropriate agencies. The vast majority of over the counter (OTC) derivatives should trade on an exchange. Exchanges improve transparency of the market, increase liquidity, lower the costs to investors and allow for the monitoring of systemic risk.

4) **Providing Sufficient Resources to Regulators:** While improved regulations are imperative, we also believe that it is equally important that the regulatory bodies themselves be given the resources and political support to succeed at their jobs, and the appropriate oversight to assess their performance. Some of the biggest frauds perpetrated on investors were done inside regulated entities. In particular, we ask that the Securities and Exchange Commission (SEC) be given sufficient resources to carry out its mission of oversight of the securities markets and of financial professionals in order to protect and advocate for investors.

5) **Creation of a Systemic Risk Regulator:** SIF believes that a systemic risk regulator is another important level of protection, but it should not displace the oversight and accountability of other agencies to ensure the safety and soundness, fairness, transparency, and accountability of financial markets, participants, and products. If the responsible agencies perform those functions properly, then systemic risk will be far less of a problem.

An effective systemic risk regulator must identify and cure risks that could threaten the broader financial system, stopping institutions from creating systemic risk by growing to a certain size or complexity, becoming too interconnected, or engaging in certain activities.

6) **Better Consumer Protection:** We support the creation of a new agency that will allow for improved disclosure and regulation of consumer credit products and support the proposed Consumer Financial Protection Agency, including HR 3126. Predatory lending has been a major concern for our members, particularly community development financial institutions. Over the previous decade, unscrupulous lenders took advantage of low income borrowers by selling them inappropriate mortgages and lines of credit. Our industry promotes fair lending practices that enable low income people to own homes and to build businesses, and we have long supported community development financial institutions. An agency devoted to the regulation of consumer financial products will go a long way towards providing a better mechanism for improving consumer protection.

³ http://www.socialinvest.org/documents/ESG_Letter_to_SEC.pdf.

7) **Improve Rating Agencies:** The weakness of this system was made obvious by the fact that ratings agencies awarded AAA ratings to thousands of ultimately toxic subprime-related mortgage backed securities and collateralized debt obligations. Additionally, there are inherent conflicts of interest in the current business models for credit rating agencies, including the fact that issuers pay the credit rating agencies for their ratings and that they provide other consulting services to those same corporations they rate. Last, these agencies are largely immune from civil liability. SIF believes then that rating agencies need improved supervision and must be held to higher standards of accountability and changes must be made to their exemption of liability.

The Social Investment Forum and its members are committed to improving the functioning of the financial markets and system. We believe comprehensive regulatory reform is necessary to achieve this goal.

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