Domini

Domini Impact Investments
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SHIFTING THE INVESTMENT PARADIGM: Domini's System Project

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CONTENTS

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SHIFTING THE INVESTMENT PARADIGM:
Domini's System Project

> ***Significant transformations***
> … will be necessary to keep 21st century economies and societies prosperous.

> "A system is an interconnected set of elements that is coherently organized in a way that achieves something."
> — ***Donella H. Meadows, Thinking in Systems: A Primer***

Dear Fellow Investors:

Today, more than ever before, investors are concerned with their impacts. At Domini, we have always understood that investments have impact and sought to make portfolio-level decisions that have positive impact. But while investment decisions affect the financial system, they also affect every social and environmental system, because no system is unchanged by the flow of capital and business decisions. The effect on systems can be positive or negative, but always occurs. Consequently, **we have embarked on this project to manage our impacts beyond the portfolio-level**.

The systemic effect of investment decisions was undeniable in the wake of the 2008 financial crisis. Decisions as apparently as simple as how housing is financed created a failure that impacted all asset classes triggering a system-wide meltdown. This impact was a stark reminder that every choice can send tremors around the world or offer paths for sustainable development. **We are now working on how investors can understand their systemic effects and intentionally create positive influence on systems.** Over the mid- and long-term, this influence should benefit people, planet and portfolios.

The development of the UN Sustainable Development Goals (SDGs) further reinforced the need for a system level approach to achieving our goals. Adopted by 193 countries of the UN General Assembly in September 2015, the SDGs are an incredible set of interlinked social, environmental, and economic goals for systems-level change including "no poverty," "zero hunger," and "good health and well-being" (see page 10). The emergence of these goals presents the investment community an opportunity to play a catalytic role in the realization of this vision. But to achieve the SDGs, major paradigm shifts in the way the business operates will be necessary. Investors will need to acknowledge their responsibility for the impact that their decisions have and work intentionally to minimize long-term risks and maximize opportunities for sustainable returns.

This project sought to move from targeting systems arbitrarily or peripherally to intentionally influencing the systems we rely on for the long-term health of our portfolio and our world. To do so,

- We used tools from the field of systems dynamics, which provide an approach to breaking down complex problems and tracing a symptom of a problem back to its fundamental drivers.
- We selected challenges, ranging from overfishing to forced labor, that resulted from the unsustainable paradigm.
- We focused on what leverage points we, as investors, might use to shift the paradigm.

This report shares our early efforts towards understanding and directing our influence on paradigm shifts. We understand that positive investor influence on systems is a critical component to build a healthy world and sustainable portfolios. **Our goal is to share our efforts, promoting debate and discussion among investors as to the best way to further this process.** Through collaborative action, we believe investors can shift current paradigms to create a sustainable future for all.

Very truly yours,

Carole Laible, CEO

Executive Summary

As investors, we rely on the stability and sustainability of societal, environmental, and financial systems within which we operate. Yet a dominant paradigm in the investment community today—a single-minded focus on the maximization of returns—can introduce short-term behaviors that expose investments to non-diversifiable risks such as climate change that are potentially harmful to shareholders' long-term interests. Systems thinking provides an innovative approach to bridging this gap in investors' risk management.

This report details Domini's pilot project to understand how to augment the current investor paradigm with considerations that lead to sustainable outcomes. Our process was:

1. ***Develop Investment Beliefs Statements:*** *We clarified our investment philosophy, specifically as it relates to system-level considerations and published a formal statement. See page 16 for our Investment Belief Statement.*
2. ***Identify Focus and Action Areas:*** *We identified focus areas where the current paradigm leads to undesirable outcomes and actions areas on which to concentrate our efforts. See Figure #1.*
3. ***Create Issue Groups:*** *Within each area, groups worked to identify investors' actions that could influence the underlying paradigm that is leading to unsustainable outcomes. The groups reported out on their process and actions. See Part Two for a discussion of each issue area and our work.*

We are providing this report, which includes both our work and insights gained, so that the investment community may benefit from our initial project and to inspire collective action. We are working to plan our next steps to enhance and refine our process. ***We extend an invitation to all to collaborate on this pioneering work.***

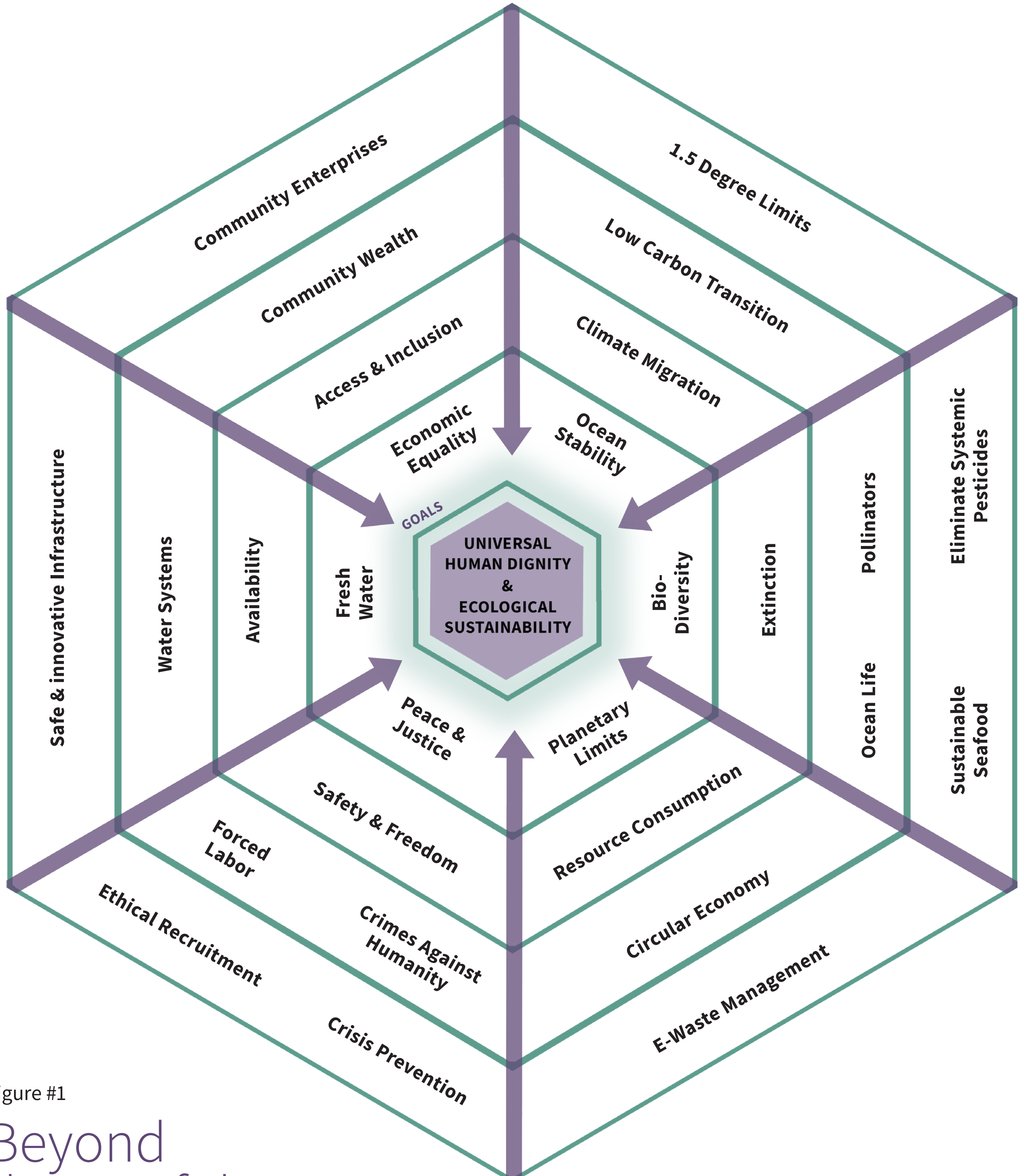

Figure #1

Beyond the Portfolio

System-level Work

We selected a range of issues where the current paradigm is causing poor outcomes. This web illustrates how our micro-level action areas tied back through macro issues to our ultimate goals of advancing ecological sustainability and universal human dignity.

The United Nations Sustainable Development Goals:
System-level Targets

The United Nation Sustainable Development Goals (SDGs) are a landmark set of 17 interlinked development goals for economic, social, and environmental progress by 2030. The SDGs, ratified in 2015, are the first widely accepted vision for global development and are truly systemic goals. Successfully reaching these goals would be a massive breakthrough in human well-being, but will depend on investors not only not hindering environmental and social progress, but contributing to it.

> “Business will play a critical role in achieving the SDGs.”

> “The case is clear. Realizing sustainable development goals will improve the environment for doing business and building markets.”

Chart #1

Connecting our work with the UNSDGs

Our system-targeting work areas, shown in green, are contributing to the following goals:

Community Wealth
Community and Municipal Enterprises

10 REDUCED INEQUALITIES

11 SUSTAINABLE CITIES AND COMMUNITIES

Water Systems
Safe and Innovative Infrastructure

6 CLEAN WATER AND SANITATION

Forced Labor
Ethical Recruitment

8 DECENT WORK AND ECONOMIC GROWTH

Circular Economy
E-waste

12 RESPONSIBLE CONSUMPTION AND PRODUCTION

Crimes Against Humanity
Crisis Prevention

16 PEACE, JUSTICE AND STRONG INSTITUTIONS

Ocean Life
Sustainable Seafood

14 LIFE BELOW WATER

Low-carbon Transition
1.5-degree targets

13 CLIMATE ACTION

Pollinators
Eliminate Systemic Pesticides

15 LIFE ON LAND

PART ONE:
Targeting Sustainable Systems

Investors need to acknowledge and manage risks and rewards at the ***system level***.

INTRODUCTION:
Confronting Systemic Problems

At Domini, we have worked for 25 years to advance universal human dignity and ecological sustainability while generating competitive returns. The scale and complexity of the challenges facing the world today make it increasingly necessary for institutional investors to also pay attention to these concerns. Due to its size and clout, the investment community influences the societal, financial, and environmental systems within which it operates. This influence makes understanding and intentionally managing systemic risks and rewards extremely powerful, as well as key to a sustainable future.

> The investment community the social, financial and environmental systems within which it operates.

An emerging understanding of this dynamic has led to the recent growth in impact investing and the integration of social, environmental, and governance factors into stock selection and asset allocation. However, to fundamentally shift away from the aspects of the current investment paradigm that produces unsustainable outcomes, we believe that we as investors need to take the next step of acknowledging and managing the potential for systemic risks and rewards. Failure to do so can contribute to instability in the systems that are crucial to the long-term sustainability of investments. As we have approached this challenge, we sought to identify and use a range to tools that can move environmental, social, and financial systems towards sustainable equilibriums.

Significant transformations in the practice of finance will be necessary to help keep 21st century economies and societies prosperous, and investors can play a large role in these changes. We must find ways that the preservation and enhancement of environmental and societal systems can be balanced with sustainable and competitive financial returns. Investors have the potential to positively influence systems by intentionally integrating a systems approach to mitigating risks and enhancing investment opportunities. Over the course of this report, we detail our process and initial attempts to apply this system-level theory of change.

Emerging Investor System-Level Action

Institutional investors are beginning to understand the effects of their decision-making frameworks on macrosystems. Further, many actors are simultaneously becoming cognizant of the need to manage system-level environmental and societal risks to ensure sustainability of their operations. This management has taken a variety of forms:

- ***Pension Funds:*** Norge Bank Investment Management believes that, "managing environmental, social and governance risks is an important aspect of safeguarding our investments. We take a systematic approach to risk monitoring."[1] The California's Public Employees Retirement System asserts in its Investment Belief Statement that long-term value creation requires effective management of three forms of capital: financial, physical and human."[2]
- ***Insurance:*** The British insurance group Aviva is a strong advocate for the United Nations Sustainable Development Goals (SDGs) and has played a catalytic role in the creation of the World Benchmarking Alliance (WBA), a global initiative to create benchmarks against which the progress of the largest global corporations' contributions to the SDGs can be measured.[3]
- ***Investor Coalitions:*** Recent collaborative initiatives by institutional investors have become global in scope and ambitions. Climate Action 100+, launched in December 2017, represents more than 275 investors with $30 trillion in assets under management pledged to engage with the 100 largest corporate emitters of greenhouse gases (GHG) over a five-year period, using guidelines developed by the global Task Force on Climate-related Financial Disclosures.[4] It seeks systematic change among the largest corporations in the world in how they manage their GHG emissions.[5]
- ***Practitioner Groups:*** One of the six primary goals set forth by the Global Impact Investment Network (GIIN) in its *Roadmap for the Future of Investing* is to "change the paradigm that governs investment behavior and expectations" and address the "overarching paradigm governing the purpose and responsibilities of finance."[6] In September 2017, the GIIN published *Achieving the Sustainable Development Goals: The Role of Impact Investing*, urging "all investors to contribute directly to the SDGs' success."[7]

These efforts will serve as a model for the range of investor actions that result from a systemic approach. As large investors become more active in this work, its impact will grow.

[1] *Responsible Investment: Government Pension Fund Global: 2016.* (Oslo: Norge Bank Investment Management) 2016:5).

[2] California Public Employees Retirement System. *CalPERS Beliefs: Our Views Guiding Us into the Future.* (Sacramento, California: California Public Employees Retirement System) 2014:7. https://www.calpers.ca.gov/docs/board-agendas/201702/pension/item7-01.pdf Last visited May 21, 2018.

[3] See the website for the World Benchmarking Alliance at https://www.worldbenchmarkingalliance.org/alliance/ Last visited on May 21, 2018.

[4] See the website of Climate Action 100+ at http://www.climateaction100.org/ Last visited May 21, 2018.

[5] See the website of Climate Action 100+ at http://www.climateaction100.org/ Last visited May 21, 2018.

[6] *Roadmap for the Future of Investing: Reshaping Financial Markets* (New York: The Global Impact Investing Network) 2018:5.

[7] *Achieving the Sustainable Development Goals: The Role of Impact Investing.* (New York: The Global Impact Investing Network) 2017:5.

DOMINI'S JOURNEY:
Systems Initiative Development

Given our long history of work on environmental, social, and governance (ESG) issues, and the increasing main-streaming of the related impact management practices demonstrated by institutional investors, we began to develop a project to act on the root causes of ESG issues. The project evolved through three main phases:

STEP ONE: Investment Beliefs Statements

- We developed a core Systems Team to develop an Investment Belief Statement embodying our understanding of how financial markets function and their relation to system-level considerations. This process was informed by a previous publication by the Initiative for Responsible Investment.[8] *See Page 16*
- Preliminary IBS draft was circulated for review by external experts and comments were incorporated
- Executive management approved and adopted IBS

STEP TWO: Focus Systems

- We reviewed best practices in environmental, social and governance (ESG) reporting by asset owners and managers and analyzed our own current and historical standard-setting and advocacy work.
- We surveyed our staff on the issues they believed were most important to Domini's mission, values, and the performance of our funds and that were related to Domini's two core values: universal human dignity and ecological sustainability.
- Through this process, our core Systems Team focused on nine prospective issues and selected issue areas where we had seen unsustainable environmental and social outcomes resulting from an investment paradigm favoring wealth extraction over creation.[9] The result was Figure #1.

STEP THREE: Issue Groups

- We introduced this project throughout the firm by creating groups to focus on each issue. The groups developed action plans for each issue to positively influence outcomes, as well as impact the investment system's paradigm at key leverage points.
- In early 2017, the groups, each with two or three members and a group coordinator, began creating their strategies and tactics. We established general guidelines for the groups and timelines for reporting.
- To train staff on systems thinking, we circulated two books: *Big World, Small Planet*, by Johan Rockström and Mattias Klum on interconnected Earth systems and planetary boundaries and Donella H. Meadows' *Thinking in Systems*, an essential primer on systems dynamics.[10]
- The reporting of each groups' work is found in Part 2 of this report.

[8] Steve Lydenberg, *Investment Belief Statements: IRI Working Paper* (Cambridge, Massachusetts: Initiative for Responsible Investment, Hauser Center for Non-Profit Organization at Harvard University) October 2011. Available at http://iri.hks.harvard.edu/files/iri/files/iri_investment_beliefs_statements.pdf Last visited May 23, 2018.

[9] The committee reviewed the four criteria that TIIP had called out as appropriate for identifying system-level concerns appropriate for long-term investors in its publication *System-Level Considerations and the Long-term Investor: Definitions, Examples and Actions*, including consensus, relevance, effectiveness, and uncertainty. Available at https://tiiproject.com/wp-content/uploads/2017/03/Systems_Level_Considerations_Long_Term_Investor.pdf Last visited May 23, 2018

[10] Johan Rockström and Mattia Klum, *Big World Small Planet: Abundance within Planetary Boundaries* (New Haven, Connecticut: Yale University Press) 2015. Donella H. Meadows, *Thinking in Systems: A Primer*) Diana Wright: editor. (White River Junction, Vermont: Chelsea Green Publishing) 2008

PROJECT STRUCTURE
Paradigm Shifts

This project sought to fill a gap in current investor approaches to risk and uncertainty mitigation. We now understand that current approaches do not trace problems to their underpinnings. Because we believe that fundamental change to the investment system's mindset is necessary to generate positive social, environmental, and economic outcomes, the ultimate goal of our approach was paradigm change. This target was derived from Donella Meadows, who identified twelve places to intervene in a system but singled out transcending or changing "the mindset or paradigm out of which the system — its goals, structure, rules, delays, parameters — arises" as the most effective leverage point for system change.[11]

Paradigms are defined in science as the philosophical and theoretical frameworks within which theories, laws, and generalization are formulated and derived.[12] Expanding that definition, Meadows says, "a paradigm shapes language, thought, and perceptions— and systems."[13] She explains further, "[P]aradigms are the sources of systems. From them, from shared social agreements about the nature of reality, come system goals and information flows, feedbacks, stocks, flows and everything else about systems."[14]

Domini is concerned that unsustainable outcomes are being generated by today's system-level market paradigm. This paradigm, responsible for much of the short-termism in the markets, portrays investors as separate and distinct from the overall market in which they participate; therefore they cannot influence it. Investor are told their goal is to outperform that market; to have returns in the better half or top quartile relative to their peers, which is to play a zero-sum game with a loser for every winner. A zero-sum game promotes a culture of short-term profit-taking—capitalizing on information asymmetries, technological advances, reversion to the mean, and other similar tactics to exploit weaknesses or mistakes of others—an approach that generates more wealth extraction than wealth creation.

"are the sources of *systems.*"

Domini is seeking to shift toward a paradigm where wealth creation can thrive through management of system-level risks and consideration of long-term rewards, while still achieving competitive returns. This is a paradigm that can result in additive, healthy outcomes and produce a rising tide of shared investment opportunity. This report documents Domini's efforts to alter the lens through which investors regard issues of social and environmental concern in order to promote this change.

[11] The ways to intervene are:

1. The power to transcend paradigms.
2. The mindset or paradigm out of which the system — its goals, structure, rules, delays, parameters — arises.
3. The goals of the system.
4. The power to add, change, evolve, or self-organize system structure.
5. The rules of the system (such as incentives, punishments, constraints).
6. The structure of information flows (who does and does not have access to information).
7. The gain around driving positive feedback loops.
8. The strength of negative feedback loops, relative to the impacts they are trying to correct against.
9. The lengths of delays, relative to the rate of system change.
10. The structure of material stocks and flows (such as transport networks, population age structures).
11. The sizes of buffers and other stabilizing stocks, relative to their flows.
12. Constants, parameters, numbers (such as subsidies, taxes, standards).

Donella H. Meadows, *Thinking in Systems: A Primer,* Diana Wright: editor. (White River Junction, Vermont: Chelsea Green Publishing) 2008.

[12] Simon Bell and Stephen Morse, *Sustainability Indicators: Measuring the Immeasurable?* (London, UK: Earthscan) 2008.

[13] Donella H. Meadows, *Thinking in Systems: A Primer,* Diana Wright: editor. (White River Junction, Vermont: Chelsea Green Publishing) 2008.

[14] Ibid.

Process and Tools

Domini's issue groups for each action area evaluated the relationship of the underlying investment paradigm to the current outcomes in the area. For example, how is the depletion of global fish stocks related to wealth extraction? They looked to develop and implement a better understanding of how investors can intentionally act to move the investment system away from current practices and toward sustainable outcomes.

> Although few of the largest institutional investors can have system-level influence on their own, investors can amplify their influence by ***working together***.

To characterize the varied techniques of these groups, we draw on language developed by The Investment Integration Project (TIIP). TIIP has identified a set of ten "tools" that investors can use to intentionally influence systems. The tools fall under three categories: field-building, investment enhancement, and opportunity generation. TIIP describes these categories in its *Measuring Effectiveness* report:

> Field building tools help to create the infrastructure that addresses the challenges of collective action to influence complex systems … Investment enhancement tools extend traditional investment activities to exert influence on key leverage points within a system … Opportunity generation tools [aid in enhancing] the richness of capital within a system.[15]

These tools helped describe how our actions are part of the larger framework of system-level influence. Most useful to our work were the tools of Self-Organization, followed by Standard Setting and Interconnectedness.

[15] William Burckart, Steve Lydenberg, and Jessica Ziegler, *Measuring Effectiveness: Roadmap to Assessing System-level and SDG Investing*. (New York: The Investment Integration Project and the IRRC Institute) 2018: 14-15.

Figure #2

The Ten TIIP Tools of Intentionality

TOOL CATEGORY	TOOL DEFINITION
Field Building	**Self-Organization** Leading the creation and management of on-going organizational structures that build the capacity of the investment community to address system-related considerations and strengthen the overall resilience of the financial system.
	Interconnectedness Increasing the flow of information and communications about environmental, societal and financial systems among peers, clients, and the public at large.
	Polity Substantially engaging in public policy debates—directly with governmental bodies and regulators or less directly through collaboration with civil society organizations or peers in the investment community—to create stronger, more resilient financial, environmental or societal systems on which long-term investment can build.
Investment Enhancement	**Solutions** Pursuing investments that seek to resolve system-level societal and environmental challenges.
	Standards Setting (1) Setting absolute standards for the inclusion of securities (primarily public and private equities or fixed income) based on widely accepted norms; or (2) Leading the setting of standards for conduct by corporations in areas of social or environment concern for specific industries or issues.
	Diversity of Approach (1) Developing a diverse set of investment products or services to serve clients with differing ESG concerns (asset managers); or (2) Utilizing a diverse range of investment tools to address complex system-level social or environmental concerns (asset owners and managers).
Opportunity Generation	**Additionality** 1) Adding to the value of the societal and environmental systems, while also creating economic value, in ways that would not otherwise be funded; 2) Investing in underserved regions or populations, or; 3) Funding projects that are not currently being funded by any others and are in effect breaking new ground and creating new markets.
	Locality Strengthening the environmental, societal and financial systems within a geographic region—be that a city, state, region or country—to create a series of interrelated investments that address sustainability issues and support and enhance each other.
	Evaluations Valuing difficult-to-price aspects of environmental, society and financial systems that generate potential long-term investment opportunities.
	Utility Maximizing the alignment of specific asset classes with the societal functions that those asset classes were designed to serve.

OUR INVESTMENT BELIEFS

At Domini, we believe that investments made today will shape tomorrow. We therefore apply environmental and social standards to all our investments. In doing so, we seek to capture sources of opportunity and risk often overlooked by conventional financial analysis. Our evaluations also provide us with insight into the quality of corporate management teams, which is a key component of future success.

Our Beliefs:

1. Investments have systems-level impact on finance, society and the environment. Investors have an ethical obligation to acknowledge these consequences.
2. Investors that strengthen the resilience and integrity of these critical systems create lasting value. Investors that fail to do so cause harm.
3. Long-term investment performance depends upon the above principles.

Our Objectives:

1. To serve our clients' financial well-being while preserving and enhancing the environment and society through responsible asset management.
2. To measure and report our financial, societal and environmental impacts.

Our Strategies:

1. As investors, we participate in the capital markets using financial, social and environmental standards in all of our investment decisions.
2. As owners, we engage with issuers, civil society organizations and policy makers to create financial, environmental and societal value.
3. As neighbors, we seek to help build strong, sustainable communities by directing capital to where it is needed most.

PART TWO:
Issues and Actions

Working to Shift the Investment System

This project has been a learning process. We are continuing to work to gain an understanding how systems interact, why poor outcomes occur, and what steps can be taken to improve them. The following section of this report details our preliminary findings and work. Each issue area begins with a reckoning of how current underlying systems dynamics produce poor outcomes and our vision for change. **We evaluate how investors can impact the current paradigm, and why we believe they should, with an emphasis on the question of materiality.** Our definition of materiality is based on the work of the Sustainability Accounting Standards Board (SASB) and addresses why the issue is of concern for investors. Finally, using the TIIP tools, we categorize our actions within each area and explain how the actions can contribute to a shift in the investment paradigm.

Anchor Institutions and Community Wealth

The keystone of sustainable communities are often “anchor institutions,” wealth-creating enterprises that provide financing, housing, healthcare, and education, as well as support for small-businesses and job creation. We define anchor institutions as enterprises with a large, rooted presence in a region, motivated by a purpose to propel communities’ economic growth and well-being through programs, products, and services, and by playing a substantial role in the community as an employer and purchaser.

In a world of increasing inequality, community economic development that emphasizes wealth-building in historically underserved regions is vital. Many business practices that prioritize immediate returns, including predatory lending, deceptive marketing practices, and outsourcing to reduce wages, weaken the communities that companies rely on for employees, business partners, and customers. Healthy, resilient communities promote income and wealth equality and the preservation and enhancement of human and environmental capital. Such communities can adapt to external shocks and to dislocations of internal growth. These conditions mean communities can enhance financially attractive and sustainable opportunities for investors. Investors can participate in community wealth building through investments that promote increased access to capital and other crucial services like healthcare, sustainable energy, healthy food, and transportation.

Community wealth creation is material for investors because healthy, resilient communities that promote income and wealth equality and the enhancement of social and environmental capital can offer long-term and sustainable investment opportunities.

Actions:

Domini has recently focused on two types of anchor institutions that can help increase access to quality, affordable services for underserved communities. Financial institutions can improve access to critical community resources and needs through mortgage financing, small-business lending, project financing (including infrastructure projects), consumer financing, education loans, and financial literacy services. Healthcare institutions not only can provide acute and preventative health care—physical and mental—to community members, but also stable jobs and support for small businesses.

Interconnectedness:
Increasing the flow of information and communications about environmental, societal and financial systems among peers, clients, and the public at large.

Field Building via interconnectedness

To enhance peer and investor knowledge of the role of healthcare and financial services as anchor institutions in community wealth building, Domini researchers have shared our knowledge and experiences through presentations and reporting:

- Women Investing for a Sustainable Economy NYC (WISE-NYC): WISE-NYC is a community of women contributing to the impact investment industry with the purpose of connecting, deepening relationships and learning and sharing expertise. Domini researcher Shoko Sekiguchi organized and moderated a panel entitled "Unlocking Community Wealth" with Alison Omens of JUST Capital and Rose DeStefano of the New York City Mayor's Office of Workforce Development. The panel, which discussed social impact strategies in an urban setting, received a WISE award for "Best Creative Event 2017."
- Sustainatopia, Boston, MA: An event for impact investment professionals and advisors. Lionella Pezza, one of Domini's lead researchers, participated on a panel and explained community wealth creation to an audience of impact investing professionals and financial advisors.

Standards Setting:
1. Setting absolute thresholds for the inclusion of securities (primarily public and private equities or fixed income) on the basis of widely accepted norms; or **2.** leading the setting of standards for conduct by corporations in areas of social or environment concern for specific industries or issues.

Investment enhancement via standards setting

To send signals to issuers and our peers about the importance of community wealth creation by anchor institutions, we periodically revisit and revise our industry-specific key performance indicators (KPIs) for the financial services and healthcare industries. To encourage increased consideration of these factors by the investment community, we will publish a paper detailing how we use these KPIs for financial and healthcare institutions in our evaluation and decision-making processes.

Within the financial services industry, our standards favor banks that:

- offer products and services to underserved populations;
- operate community-based lending;
- provide financing to small- and medium-sized enterprises, renewable energy projects, and affordable housing;
- promote financial literacy programs; and
- have diverse management teams and boards of directors.

We seek to avoid abusive and potentially wealth-destroying practices such as:

- predatory lending practices including overcharging and illegal foreclosures;

- the sale of inappropriately risky products to customers; and
- taking excessive risk in the financial market.

Within the healthcare industry, our standards favor healthcare service providers that demonstrate:

- commitments to serving underserved populations;
- strong records of quality in outcomes;
- strong reputations for research and development;
- commitments to preventative care;
- positive employee relations;
- environmental sustainability initiatives; and
- teaching and training excellence.

We are concerned when firms have:

- controversies relating to patient health quality and outcomes;
- abuses in pricing and use of procedures;
- Medicare or Medicaid fraud;
- reductions in staffing and beds for treatment; and
- labor disruptions.

These KPIs have helped us confront challenging assessments, including the difference in the practices between non-profit and for-profit hospitals. We have found Community Health Needs Assessment (CHNA) reports, a requirement for nonprofit hospitals under the Patient Protection and Affordable Care Act, useful in these assessments. This data has played an important role in our evaluations of debt securities issued by non-profit hospitals for the Domini Impact Bond Fund.

Utility:
Maximizing the alignment of specific securities within an asset class with the societal functions that those asset classes were designed to serve.

Opportunity generation via utility

Government-issued bonds provide a notable opportunity for investment in public goods. We seek to maximize the underlying social utility of government fixed-income securities in community wealth creation by favoring those that do so particularly effectively. We believe that if increasing numbers of investors take a similar approach, further issuance of such bonds will be encouraged.

- Among the mortgage-backed securities issued by U.S. Government agencies, we favor securities that support affordable housing, especially for low- and very low-income populations, such as Designated Underwriting Securities (DUS).

- More generally, among municipal obligation bonds, we favor those that support basic infrastructure and transportation systems, business and job creation, and nonprofit education.

Forced Labor;
Ethical Recruitment

Forced labor occurs when workers are compelled to serve involuntarily and against their continuing free will under threat of punishment. It is characteristic of modern slavery, and occurs in the agriculture, fishing, domestic service, construction and manufacturing industries, among others. Today, 45 million people worldwide are victims of forced labor and slavery, according to The Global Slavery Index. Migrant laborers are particularly vulnerable to forced labor conditions.

Focusing solely on how companies can generate profits through cost cutting can cause investors to unintentionally contribute to forced labor in investee firms and their supply chains. Increased awareness and understanding of how fair labor practices can be balanced with profitable business models and competitive returns can help investors contend with this challenge.

Forced labor is material for investors because when a company fails to properly manage human rights issues in its supply chain, investors may bear the cost of reputational damage. **By ensuring companies adopt a strong supplier code of conduct, conduct labor and human rights audits, and maintain a credible remediation process, investors can benefit from the returns from firms operating in a society with a sustainable, productive and mobile workforce, and strong local communities.**

Actions:

Domini has recently focused efforts on the protection of migrant workers, particularly on helping to ensure they are recruited to their jobs ethically. By engaging with companies on adoption and enforcement of "No-Fees" initiatives in their supply chains, investors can help play a role in preventing unethical recruitment and forced-labor practices.

Field Building via interconnectedness

Seeking to increase the information flows among peers, we published a brief on migrant workers on our website and raise the issue in meetings with investors.

In addition, Domini staff spoke on ethical recruitment practices in numerous venues to raise awareness and facilitate engagement on the topic.

- We participated in and helped facilitate Apple Inc.'s participation in an Interfaith Center on Corporate Responsibility (ICCR) ethical recruitment panel.
- In separate ICCR meetings we spoke on a 'Supply Chain 101' panel and distributed questions to guide investor engagements.
- At the SRI conference in San Diego, CA and Consumer Goods Forum in Montreal, Canada, we spoke on panels on supply chain engagement.
- Researcher Lionella Pezza presented on a panel at the Sustainatopia conference in Boston, and on Domini's investment philosophy to an MBA class at Fordham University, emphasizing migrant worker rights and related engagements.

Investment enhancement via standards setting

To promote industry-wide standards, we advocated for the inclusion of indicators related to ethical recruitment in the Sustainable Accounting Standards Board (SASB) standards for the Consumption sector.

To emphasize the importance of such standards for individual corporations, we have engaged with companies on their current ethical recruiting practices, and sought their compliance with the Interfaith Center on Corporate Responsibility's "No Fees" initiative.

- Domini wrote to Nike, Tapestry (formally known as Coach), Michael Kors, Belle International, L Brands, Ralph Lauren, IBM, and Motorola Solutions to inquire about implementation of ethical recruitment policies.
- We participated in ICCR's ethical-recruitment engagements with 80 stakeholders, sending a letter to Broadcom, Canon, Cisco, EMC, Hitachi, Johnson Controls, Medtronic, and Microsoft.
- As a result of our ongoing engagements, Michael Kors has adopted ICCR's three pillars of ethical recruitment, and dialogues are underway with several other companies on adoption. Through advocacy for this type of standards, investor can help promote models of best practice within industries.

Crimes against Humanity; Crisis Prevention

Crimes against humanity are defined as systematic abuses or attacks against a general civilian population and, in the extreme, include genocide and war crimes.

A narrow focus on returns can cause investors to unintentionally lend legitimacy or revenue streams to governments committing human rights violations, even those as severe as genocide. With a broad appreciation of the context in which they are investing, investors can intentionally work to address human rights abuses before they escalate to such extreme levels.

Severe human rights issues are material for investors because operations in conflict zones and linkage to crimes against humanity presents physical and reputational risks to corporations, as well as ethical dilemmas for investors themselves. Moreover, investors can support actions by the international community to mitigate such conflicts and address genocide. **In addition, by addressing human rights abuses before they escalate further, investors can contribute to the preservation of investment opportunities as well as to national and regional geopolitical stability.**

Actions:

Due to widespread allegations of targeted killings, we have focused on implications of investors' involvement in Sudan, South Sudan, and Burma.

Self-Organization:
Leading the creation and management of on-going organizational structures that build the capacity of the investment community to address system-related considerations and strengthen the overall resilience of the financial system.

Field Building via self-organization and interconnectedness

To build capacity for joint investor action in crisis areas, we have continued our long-running collaborations the EIRIS Conflict Risk Network (CRN), a non-governmental organization helping to mitigate crises.

Shin Furuya, Impact Investment Strategist at Domini, serves on the steering committee of the CRN. CRN is a network of institutional investors, financial service providers, and related stakeholders working to mitigate conflict risk and increase responsible foreign investment in conflict zones, including South Sudan, in order to protect both civilians and investment.

To help increase the knowledge and capacity of investors to understand the issues of crimes against humanity as they relate to these two countries and how a concerned investor might mitigate its direct involvement, we have developed white papers on Domini's approach to this challenge.

- In 2017, we published a paper detailing our process for evaluating business activities in Myanmar/Burma as a resource for other investors and companies.
- We drafted a report, released in October 2018, explaining our process for evaluating business activities in South Sudan, with input from NGOs and think tanks. The report is a resource for other investors and companies operating in South Sudan and other zones. We also published an editorial in *Responsible Investor* on the topic.

Investment enhancement via standards setting

Standard setting, including divestment policies, are an important tactic for investors addressing crimes against humanity. Domini has adopted a policy of not investing in corporations that support the general operations of the governments of Sudan and Burma due to their historical and current involvement in genocide.

To emphasize the importance of such standards for individual corporations, we have engaged with several operating in conflict zones

- We have sent letters to a number of Japanese companies to communicate concerns about their mineral-extraction operations in Myanmar (Burma), seeking information on their due diligence efforts, and compliance with the UN Guiding Principles on Business and Human Rights.
- We held discussions with several other companies doing business in Myanmar, including Coca-Cola and Unilever.
- Previously, in response to conflict in Sudan, Domini participated in meetings with JPMorgan Chase, Citigroup and Merrill Lynch to discuss the banks' responses to the crisis in Darfur. The meetings—which included other impact investment firms, Amnesty International, and the Genocide Intervention Network—resulted in Citigroup adopting a formal policy on Sudan.

To help contend with human rights abuse issues relating to telecommunications and internet companies operating in countries with active controversies, Domini has sought to use field building through the tool of self-organization to create raise awareness of potential controversies and help companies address challenges at early stages.

- We were one of the founders of the Global Network Initiative (GNI), a multi-stakeholder organization dedicated to the protection and advancement of freedom of expression and privacy rights in the Information and Communications Technology sector (ICT). GNI offers a collaborative approach to responding to efforts by governments that seek to enlist companies in acts of censorship and surveillance that violate international standards.
- Recently we participated in a Global Network Initiative call with Facebook and Telenor, two members of the GNI, to discuss their response to the escalating crisis in Myanmar (Burma), and continue to raise the issue with Facebook.

Low-carbon Transition; 1.5-degree targets

Heat-trapping gases released from the burning of fossil fuels are causing dramatic changes in the Earth's climate, altering rainfall patterns, the frequency and intensity of extreme weather events, and the melting of polar ice caps. Around the world, people are already affected by decreased food security, more frequent natural disasters including hurricanes and heatwaves, and other destabilizing changes.

By focusing primarily on the current and projected market price for energy in stock valuation and other investment decisions, investors have failed to account for the costs of the extraction and use of those energy sources that markets have not incorporated—their externalized costs. Now climate change is one of humankind's greatest challenges and a non-diversifiable risk to portfolios across asset classes.

This issue is material for investors because shifting regulatory and policy actions, supply-chain disruption, stranded assets, and property and infrastructure damage are all climate-related risks that they increasingly need to account for, both to finance returns for their shareholders and to protect their employees, customers, and the communities they operate in.

The challenges of climate change also present opportunities to invest in forward-looking and innovative solutions through financing a diverse array of renewable energy sources and creating a diversified and sustainable energy-generating system.

Actions:

The main avenues to addressing rising sea levels are slowing climate change and adaptation. Domini has chosen to work on the former while there is still a window of opportunity, although adaptation work must also proceed given the inevitability of climatic changes. The Paris Agreement calls for limiting the increase in global temperature by the end of this century to no more than 1.5 to 2 degrees Celsius over pre-industrial levels.

Field Building via self-organization and interconnectedness

We are working to change the conception of investors' role in creating and responding to climate change through collaborative advocacy with other investors and groups. These groups seek to expand understanding of investors' responsibility through a variety of initiatives.

- Following the U.S.'s withdrawal from the Paris Climate Agreement, we joined mayors, governors, college and university leaders, businesses, and investors, collectively representing more than 127 million Americans and $6.2 trillion of the U.S. economy, in signing the "We Are Still In" Declaration in support of continued action to meet the goals of the Paris Agreement
- We support and are implementing the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD), a critical tool for assessing how the long-term risks of climate change will affect corporate value. As they developed their recommendations, TCFD considered a paper on the use of scenarios for long-term risk management, written by Domini's Steve Lydenberg, to be "required reading."
- We work with several coalitions of concerned investors to advocate for improved corporate environmental practices and climate-risk disclosure, including the Ceres Investor Network on Climate Risk and Sustainability, the United Nations-supported Principles for Responsible Investment (PRI), and CDP (formerly the Carbon Disclosure Project), among others.

We also share information that we believe can help change the understanding of investors' responsibility in respect to climate action.

- We published a concise fact sheet for shareholders and financial advisors on our climate change strategy and investment approach called "Taking Action on Climate Change."
- To reach a broader range of stakeholders, including those working in policy, science, and the arts, we hosted a Climate Week 2017 event on climate migration. The event highlighted the human impacts of climate-induced migration through a photo exhibit by photojournalist and filmmaker Ed Kashi, and a keynote talk given by Alex de Sherbinin, an associate director for science applications for the Earth Institute at Columbia University's Center for International Earth Science Information Network. [16]
- In support of the work done by TCFD, we advocated for corporate disclosure of scenario planning with regard to climate-related impacts on business operations, circulated a paper on the usefulness of scenario planning to the TCFD's Advisory Board, and presented on scenario planning at a TCFD event in New York as part of the lead-up to the issuance of the TCFD recommendations.
- We contributed to a study conducted by the Electric Power Research Institute (EPRI) to identify the priority sustainability issues affecting electric power companies in North America.

[16] See Domini, *Human Impact: A Gathering About Climate Migration*, December 19, 2017. https://www.domini.com/insights/human-impact-a-gathering-about-climate-migration, Last accessed June 8, 2018.

Investment enhancement via standards setting

Domini underscores its commitment to action on climate change through standards setting.

- In February 2017, we updated our key performance indicators for the Utilities and Municipal Electric Utilities industries to include, among other things, a policy to avoid investment in electric utilities that have announced plans for or started new construction of coal-fired power plants after January 1, 2014.
- We were a signatory to Banking on a Low-Carbon Future, a campaign organized by Boston Common Asset Management and ShareAction, to encourage banks to align climate-related disclosures in accordance with TCFD recommendations.
- We regularly engage with corporations to encourage better management of climate-related risks through 2-degree scenario planning, renewable-energy goals, science-based emissions reduction targets, and enhanced disclosure of climate-related risks.
- We joined the Climate Action 100+, [17] a five-year, investor-led initiative to engage with the world's largest corporate greenhouse gas emitters, working with them to curb emissions, strengthen climate-related financial disclosures, and improve governance on climate change. We are working with several large companies via this engagement.
- We also joined the Investor Decarbonisation Initiative organized by ShareAction in conjunction with The Climate Group and the We Mean Business coalition. As part of this collaboration, we participated in the RE100[18] and EP100[19] initiatives, which respectively seek to encourage companies to commit to 100% renewable energy usage and to double their energy productivity in the next 25 years.

[17] Climate Action 100 Plus, http://www.climateaction100.org/, Last accessed May 27, 2018.
[18] The Climate Group, RE100, https://www.theclimategroup.org/RE100, Last accessed May 27, 2018.
[19] The Climate Group, EP100, https://www.theclimategroup.org/project/ep100, Last accessed May 27, 2018.

Water Systems; Safe and Innovative Infrastructure

U.N. Sustainable Development Goal 6 is to “ensure availability and sustainable management of water and sanitation for all.” Reaching this goal, in lower-, as well as higher-income countries, requires a substantial increase in funding and innovation in water infrastructure and management.

By failing to confront the financial challenges of assuring the availability of adequate, safe water supplies, investors are exacerbating the emerging fresh water crises. The tens of billions of dollars needed to maintain and upgrade our water systems will not come from government funding alone. Other models of financing, as well as new, low-cost sanitation and distribution technologies must be developed and implemented.

The availability of fresh water is material to long-term investors, because having long taken water access for granted, it is now increasingly in doubt. Water security is under threat from numerous forces, including climatic changes, pollution, and depleted resources. Continued access to clean water is also threatened at a local level by inadequate investment in distribution, treatment, and reservoir infrastructure. Many systems, particularly in rural regions and low-income communities, are experiencing declines in water affordability, accessibility, and sanitation. Lack of water access severely limits business operations of any kind, and companies and municipalities may face backlash over poor water stewardship policies. **To ensure the continued viability of business operations, investors will need to be water stewards, invest in sustainable infrastructure and support multi-stakeholder management of water resources.**

Actions:

As part of our effort to promote investor recognition of the far-reaching benefits of investments in infrastructure, Domini has sought to identify how investors can promote and support safe and sustainable water infrastructure, specifically municipal water systems, and equitable management of these systems. Our first step has been to better understand the dynamics that led to the current situation, and to seek out a range of potential solutions.

Field Building via interconnectedness

- We participated in the Ceres Water Hub, an investors group working on water issue in investing and contributed to the Ceres Investor Water Tool Kit.[20]
- We also reached out to academics with expertise in the area to gain a better understanding of current problems facing municipal water systems, as well as potential solutions. To share this knowledge with other investors, we drafted a backgrounder on municipal water issues and solutions for publication.

Investment enhancement via standards setting

- We are considering improving and expanding our key performance indicators with respect to freshwater, and providing our financial sub-manager updated guidance on evaluating municipal water bonds.

[20] Ceres, *Investor Water Toolkit*, https://www.ceres.org/resources/toolkits/investor-water-toolkit, Last accessed May 27, 2018.

Circular Economy; E-waste

A circular economy is one in which natural resource materials are recycled and reused as much as possible in order to use closed loop production cycles to reduce their consumption.

Investors' pursuit of maximum short-term returns is driving unsustainable resource consumption that is exhausting the Earth's resources and generating enormous quantities of waste. Linear modes of production, wherein materials are extracted to create a product designed to have a short lifespan and then be disposed in landfills cannot meet the demands of a swelling global population. To combat this imbalance, businesses can develop product designs and manufacturing methods that reuse, repair, and recycle materials to produce the maximum value with minimum waste.

By failing to evaluate and address the implications of the resource management policies and practices of the companies, governments, and real estate in which they invest, the financial community can inadvertently contribute to the environmental challenges created by our current linear economy. Americans trash or recycle 142,000 computers and over 416,000 mobile devices every day, according to the EPA. Electronic devices such as cell phones contain precious minerals and rare earth metals that are in limited supply, costly and environmentally damaging to mine, and which are often extracted in unsafe and unfair conditions. Additionally, these compounds are often "conflict minerals" with disputed ownership whose sale is used to fund violent and illegal activity.

The circular economy is material because exhausting supplies of key natural resources, as well as the resulting waste, has the potential to disrupt corporate businesses, economies, and financial markets. **Investors will benefit from turning to responsible production and consumption models, and efficient use of resources and materials in support of a "circular economy" model.** Investors have an opportunity to encourage the innovation necessary for a transition to sustainable production and consumption models by investing in businesses with "cradle-to-cradle" product models and engaging with companies and governments about the benefits of these models.

Actions:

As Domini had not historically worked on issues relating to the circular economy or electronic waste, we worked to deepen our understanding of the interwoven systems involved in unsustainable consumption patterns.

Field Building via interconnectedness

- We sought information on the structure and behavior of the system from the Ellen MacArthur Foundation,[21] a leading proponent of the circular economy transition, As You Sow,[22] which has led engagements on e-waste and Step,[23] an initiative of the United Nations University that aims to bring stakeholders together to solve e-waste issues.
- We conducted research on consumer electronic trends, including product design, disposal avenues, and public policy. We have begun to evaluate potential leverage points we can use.

[21] See Ellen Macarthur Foundation, *What is a circular economy?*, https://www.ellenmacarthurfoundation.org/circular-economy Last accessed May 29, 2018.

[22] See As You Sow, *Electronic Waste*, https://www.asyousow.org/our-work/waste/electronic-waste/ Last accessed May 29, 2018.

[23] See Step, http://www.step-initiative.org/, Last accessed May 29, 2018.

Ocean Life; Sustainable Seafood

Sustainable fisheries are those where fishing practices do not deplete fish populations beyond their ability to regenerate.

By focusing solely on food industry profit margins, investors can inadvertently contribute to unsustainable exploitation of the world's fisheries. Seafood is the last major food source that is still caught in the wild, but the oceans cannot replenish fish at the rate they are being depleted. Climate change, pollution and destructive fishing practices, threaten both the viability of fish stocks and their quality for human consumption. An estimated two-thirds of the world's fish stocks are either fished at their limit or overfished, particularly large fish like tuna.[24] The World Bank estimates that the economic losses due to overfishing are approximately $50 billion per year.[25]

According to World Wildlife Fund (WWF), 53 percent of the world's fisheries are fully exploited, and 32 percent are overexploited, depleted, or recovering from depletion.[26] Unless more consumers diversify their seafood and protein choices and demand sustainable seafood, recovery of many fish stocks may be impossible.

Addressing overfishing is material for investors as it can mitigate supply chain risk and protect long-term opportunities for seafood-related investments. Work on sustainable seafood can also contribute to development of investment opportunities through identification of innovative seafood management practices and technologies. Collective action is paramount to sustainably managing the oceans and to the future of marine biodiversity.

[24] The World Bank, *14 Life Below Water*, http://datatopics.worldbank.org/sdgatlas/SDG-14-life-below-water.html, Last Accessed May 27, 2018.

[25] FAO Newsroom, *US$50 billion lost by marine fishing each year*, 9 October 2008, http://www.fao.org/newsroom/en/news/2008/1000931/index.html Last Accessed May 27, 2018.

[26] http://wwf.panda.org/about_our_earth/blue_planet/problems/problems_fishing/

Actions:

Our goal for this group was to understand how investors can promote and finance operations which protect the biodiversity of the world's oceans and support the needs of multiple stakeholders.

Field Building via interconnectedness

To build our internal knowledge base and identify key sustainable seafood challenges, we met with the Fish Tracker Initiative,[27] which investigates the role that financial institutions play in financing the trade in global fisheries, as well as with Aviva Investors, which published an investors' guide to sustainable seafood.[28]

We worked to raise awareness of ocean biodiversity loss with our shareholders and other investors through publication of an essay on sustainable seafood in our 2017 annual report and distribution of Monterey Bay Aquarium sustainable seafood guides at conferences and events.

Investment enhancement via standards setting

In conducting research for our sustainable seafood issue paper, we evaluated the food staples and retailing companies held in our fund portfolios regarding their policies for sustainable seafood management practices. We also evaluated companies in our investment universe with exposure to pet foods to determine their role in seafood consumption. We found that our risk exposures fell almost entirely within food retailers. We plan to expand on this research and assess current best practices as we engage with companies on sustainable seafood management.

[27] See Fish Tracker Initiative, http://fish-tracker.org/, Last Accessed May 27, 2018.

[28] Aviva Investors, *Why sustainable seafood matters for investors*, June 2016, https://www.avivainvestors.com/en-gb/media/insights/gri/why-sustainable-seafood-matters.html, Last accessed May 30, 2018.

Pollinators; Eliminate Systemic Pesticides

Pollinators, including managed and wild bees, butterflies, beetles, wasps, and a variety of other insects assist in the fertilization of flowering plants. In recent years pollinator populations have rapidly declined, especially wild populations. Since 2006, US beekeepers have lost about 30 percent of their colonies every year, with losses in some years as high as 42 percent.[29] Monarch butterfly populations have plummeted by 90 percent in the last decade.[30] Three species of native bumblebee are now extinct in Britain, with six more listed as endangered. These troubling trends are evident across Europe and Asia as well, and in other pollinator species. Given that three-quarters of food crops rely on wild pollinators, continued population collapse poses a major threat to global food security.[31]

By failing to confront the challenge of pollinator declines, investors miss an opportunity to help avert a global crisis in food security. The causes of pollinator decline are interrelated: destruction of natural habitat and food sources, widespread use of pesticides and fertilizers damaging populations' resistance to diseases and parasites, and climatic changes. Companies involved in agriculture and food production play a role in this decline though intensive pesticide use, conversion of natural habitat to farmland, and destruction of biodiversity. Manufacturers of pesticides and fertilizers, and companies that disturb large tracts of land including those in the real estate and extractive industries, also contribute to the loss of pollinators.

Pollinator decline is material for investors given agriculture's reliance on pollinators. Investors will benefit from addressing this issue by mitigating risks to

29 Steinhauer el al., *Colony Loss 2015-2016: Preliminary Results*. The Bee Informed Partnership. May 4th 2016. Available at https://beeinformed.org/results/colony-loss-2015-2016-preliminary-results/. Last accessed June 7, 2016.

30 World Wildlife Fund Mexico, *Monarch Population Status*. Monarch Watch. February 11, 2017. Available at https://monarchwatch.org/blog/2017/02/11/monarch-population-status-30/ Last accessed June 7, 2016.

31 See Garibaldi et al., *Wild Pollinators Enhance Fruit Set of Crops Regardless of Honey Bee Abundance*. Science. March 29, 2013.

the financial viability of food-related industries in their portfolios, as well as by identifying innovative investment opportunities in companies that are adapting well to this challenge. Investors can increase their valuation of the long-term productivity of the ecosystems that reduce the use of neonicinoid pesticides and encourage pollinator-safe alternatives. We aim to preserve and increase the population of pollinators for the sake of biodiversity and for the essential role they play in agricultural systems.

Actions:

Domini seeks to foster change by pushing companies to reduce use of chemicals known to be most harmful to pollinators, as well as promoting the restoration of natural habitat and food sources. We have focused on food producers and home and garden retailers as these companies have significant impact on pollinators.

Investment enhancement via standards setting

Our investment standards reflect our commitment to promoting solutions to systemic pesticide use. We avoid investments in companies that are major producers of synthetic pesticides and agricultural chemicals. For home improvement retailers, we view sale of organic, non-toxic and green products as a positive. For food retailers, we view sales of organic foods as a positive.

We are encouraging companies to develop and disclose comprehensive policies on pesticide use, with a preference for Integrated Pest Management techniques. In 2015, we convinced Lowe's to phase-out the sale of neonicotinoids. Friends of the Earth has been an important partner in our pesticide work. We are also endorsers of the Chemical Footprint Project and long-time members of the Investor Environmental Health Network.

> "The next phase of impact investing will use frameworks that intentionally influence ***root causes*** of systemic social or environmental risks."

CONCLUSION:
Lessons and Next Steps

Project Findings

Over the past year, as we explored how we might impact these essential environmental and societal systems that provide the context within which we invest, we remained flexible in our approach and learned from the challenges and insights we encountered. Below we share some of the lessons we learned from our first phase of exploration:

- **Understanding how paradigms cause systems' outcomes was a breakthrough.** Changing the paradigms that govern the behavior of systems is crucial to changing outcomes. System-thinking pioneer Donella Meadows has explained that mindsets, or paradigms, are the source of system behavior.[32] Encouraging change in paradigms can cause lasting shifts toward sustainable outcomes.
- In our issue areas, we found that the current investment system paradigm tips the scale toward short-term wealth extraction at the expense of non-shareholder stakeholders and unsustainability. This leads to unsustainable reinforcing loops that progressively degrade potentially productive social and environmental capital. Therefore, **we targeted actions that have the potential to shift the underlying paradigm toward one that fosters long-term wealth-creation.**
- Many of our focus issues, such as climate change, are areas where impact investors have already been active. We are currently evaluating whether a more influential use of our resources would argue for **taking a more prominent role in an important, but currently relatively neglected area.**
- **Many of the actions we have taken have focused on enhancing the interconnectedness of major actors within the investment community**—in particular, enhancing the flow of information by collecting and disseminating research, setting standards and engaging with multi-stakeholder groups.
- This process has been useful in **developing further integration of system-level considerations into our investment process** through refinement of our industry-specific key performance indicators (KPIs). These proprietary KPIs focus our research on the most relevant metrics and can serve as a basis for engagement. Development of additional system-level KPIs is a key deliverable for the next phase of our initiative.
- The process **helped us deepen our knowledge of important topics, including new and emerging issues.** For example, we gained a more in-depth understanding of how water risks and deficiencies in water infrastructure and distribution technology are impacting various industries and stakeholders across different regions and municipalities.
- **While investors often focus on risk mitigation, a system-level lens can draw attention to positive opportunities.** For example, our community wealth work identified the positive differentiators of local community development banks compared to large global banking groups.
- Training and practice in system thinking is essential in this endeavor. **Working on these issues at a systems level requires a different approach and way of thinking.** A concerted effort is necessary to make a system-level approach part of an investment organization.
- System thinking can be helpful in considering how to assess impact. We have focused on impact reporting at the portfolio level,[33] which includes policy and other broader considerations but **impact reporting at the systems level is a new approach to our work.**

[32] Donella Meadow, *Sustainable Systems*, University of Michigan Sustainability Lecture Series, March 18, 1999, Video. http://donellameadows.org/sustainable-systems-videos/ Last accessed May 29, 2018.

[33] See, https://www.domini.com/uploads/files/reports/Domini_Funds_2017_Impact_Report.pdf Last accessed October 9, 2018.

Conclusion and Next Steps

As we move toward the next phase of this project, we face a number of key questions about how best to proceed. We have only begun to confront the question of how to measure and report on progress to both issue-specific goals and the overarching goal of shifting the basic investment community paradigm. For our work to be ultimately successful, the current paradigm, which leads to policies and practices geared toward wealth extraction, must be shifted toward one geared toward long-term wealth creation. That can only occur through the development of social, human and natural capitals that can supplement the abundant resource of financial capital.

We also must now confront whether to devote our current resources to pursuing all nine of the issues areas, or limit them in order to explore more deeply what it means to take a system-level approach.

These challenges are part of the initial steps of a new approach, and our experience to date has helped us better understand how to more deeply confront macro risks that impact our investments and our world. The tentative answers we have found, and the questions that they raise, are finding their way into our daily practice, and we hope that they will prompt other investors to expand upon this work.

"For our work to be ultimately successful, the current paradigm, which leads to policies and practices geared toward wealth extraction, must be shifted toward one geared toward long-term ***wealth creation***."

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– Steve Lydenberg and Suzanna Buck

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