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The Social Responsability of Financial Institutions

CAHIER DE RECHERCHE

UNIVERSITÉ DE SHERBROOKE

Préambule

La gestion financière responsable vise la maximisation de la richesse relative au risque dans le respect du bien commun des diverses parties prenantes, actuelles et futures, tant de l'entreprise que de l'économie en général. Bien que ce concept ne soit pas en contradiction avec la définition de la théorie financière moderne, les applications qui en découlent exigent un comportement à la fois financièrement et socialement responsable. La gestion responsable des risques financiers, le cadre réglementaire et les mécanismes de saine gouvernance doivent pallier aux lacunes d'un système parfois trop permissif et naïf à l'égard des actions des intervenants de la libre entreprise.

Or, certaines pratiques de l'industrie de la finance et de dirigeants d'entreprises ont été sévèrement critiquées depuis le début des années 2000. De la bulle technologique (2000) jusqu'à la mise en lumière de crimes financiers [Enron (2001) et Worldcom (2002)], en passant par la mauvaise évaluation des titres toxiques lors de la crise des subprimes (2007), la fragilité du secteur financier américain (2008) et le lourd endettement de certains pays souverains, la dernière décennie a été marquée par plusieurs événements qui font ressortir plusieurs éléments inadéquats de la gestion financière. Une gestion de risque plus responsable, une meilleure compréhension des comportements des gestionnaires, des modèles d'évaluation plus performants et complets intégrant des critères extra-financiers, l'établissement d'un cadre réglementaire axé sur la pérennité du bien commun d'une société constituent autant de pistes de solution auxquels doivent s'intéresser tant les académiciens que les professionnels de l'industrie. C'est en mettant à contribution tant le savoir scientifique et pratique que nous pourrons faire passer la finance responsable d'un positionnement en périphérie de la finance fondamentale à une place plus centrale. Le développement des connaissances en finance responsable est au cœur de la mission et des intérêts de recherche des membres tant du Groupe de Recherche en Finance Appliquée (GReFA) de l'Université de Sherbrooke que de la Chaire Desjardins en finance responsable.

La finance responsable (ou durable) vise donc notamment à développer des modèles, des produits et des services ainsi qu'à orienter les marchés financiers et les décisions en matière de fiscalité dans une perspective durable et responsable. À cet effet, les Professeur(e)s Frank Coggins, Claudia Champagne et Lyne Latulippe ont publié en 2018 aux Éditions *Thompson Reuters* un recueil de textes s'intitulant « Éléments de la finance responsable : une approche multidimensionnelle ». Ce collectif contribue à mieux définir et délimiter la finance responsable en la décloisonnant dans une perspective multidimensionnelle. Il regroupe des textes d'universitaires de différentes disciplines ainsi que de spécialistes de l'industrie financière, propose des pistes pour tendre vers une meilleure finance, vers une finance plus responsable. Le présent cahier de recherche constitue l'un des textes (chapitres) tirés de ce collectif.

The Social Responsibility of Financial Institutions

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1. INTRODUCTION

Corporate social responsibility (CSR) has received special attention in recent years, from both companies and their stakeholders. In fact, 92% of the 250 largest global companies now disclose a CSR or sustainability report that contains extra-financial information,[1] and 80% of investors now consider extra-financial performance as well as the impact on the community of the firms in which they invest.[2] Although regulation plays an important role in corporate reporting, the growing interest of investors for extra-financial information is more likely explained by an increased social awareness. Also, from a more economic perspective, the impact of social responsibility on the value of the firm (Wu and Shen, 2013; Luo and Bhattacharya, 2009; El Goul, Guedhami, Kwok and Mishra, 2011) as well as the effect of corporate *irresponsibility* on the firm's risk profile (Sodjahin, Champagne, Coggins and Gillet, 2017; Oikonomou, Brooks and Pavelin, 2012; Lucas-Leclin, 2006) are also increasingly clear. For instance, we now know that social irresponsibility affects the risk profile of the company and can lead to the cessation of activities, significant lawsuit-related costs, complaints and sanctions. It can also increase reputational risk that can, in turn, lead to a reduction in expected returns as well as an increase in expected costs and idiosyncratic risks (Walter and Boatright, 2010).

However, while in certain sectors the impact of social irresponsibility is limited to direct stakeholders (such as shareholders, employees and customers), the effects of irresponsible behavior are larger for the financial sector because of the central role played by financial institutions (FI) in the economic and financial system. The objective of this chapter is to better understand the social responsibility of financial institutions (FISR). To do this, we first suggest a theoretical framework through which we can study FISR based on the theories that underlie corporate responsibility. We then identify

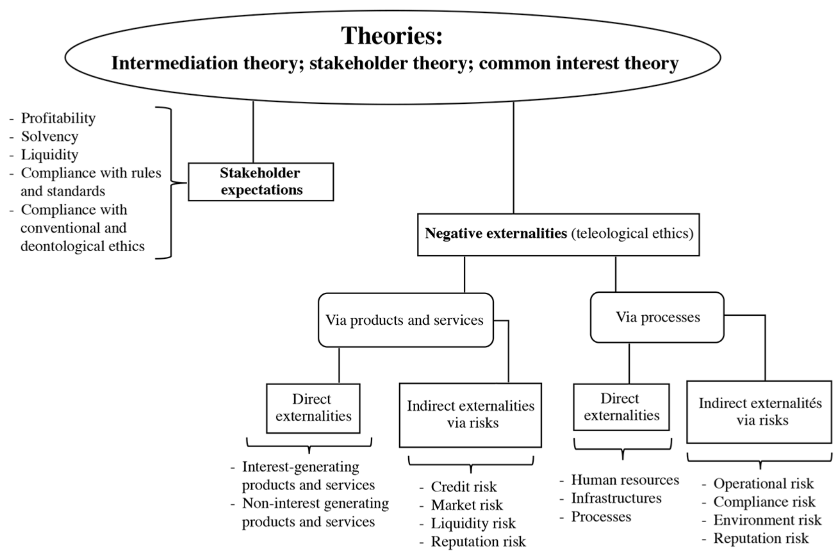
1. KPMG (2015), *KPMG International Survey of Corporate Responsibility Reporting 2015*.
2. ERNST & YOUNG (2015), *Tomorrow's Investment Rules 2.0.*

and discuss the main indicators available to assess FISR. Finally, we examine the social performance of FIs in recent years.

2. THEORETICAL FRAMEWORK FOR FISR

To analyze FISR, we rely on three existing theories that underlie corporate responsibility: i) financial intermediation theory, ii) normative stakeholder theory and iii) common interest theory. Intermediation theory defines the activities of FIs as well as their stakeholders and their expectations regarding the processes and risks associated with these activities. Normative stakeholder theory allows us to properly define and identify FI stakeholders. Finally, common interest theory allows us to define stakeholders' interests in the context of the common good. The three theories and their role in our analysis framework are described below and illustrated in figure 1.

Figure 1 – Theorical components of the social responsibility of financial institutions



2.1 Financial Intermediation Theory

According to financial intermediation theory, FIs have two essential functions: brokerage and the qualitative transformation of assets (Bhattacharya and Thakor, 1993). Brokerage activities are essential in bringing together providers and users of capital.

The qualitative transformation of assets changes either the quantity, the horizon or the risk of the capital according to the needs of suppliers and users.

For their brokerage activities, FIs intermediate between economic agents in order to adjust the offer to the demand of capital. In doing so, FIs facilitate the allocation and mobility of limited economic resources in space and in time in an uncertain environment. FIs design products and services and are involved in different markets that are characterized by the horizons and the risks of the offered products. Intervention in these markets takes place through investments, securities offering and issuing, or the providing of trading platforms that expose the FI to various types of risks. Risk evaluation and control (i.e. risk management) are therefore an essential part of financial intermediation (Merton, 1995). In addition, all the risks to which they are exposed are not directly managed by FIs (Allen and Santomero, 1997). Some risks are eliminated or avoided through improvement of business practices, some risks are transferred to other participants, while other risks are actively managed internally. To do so, FIs use various strategies such as the use of capital cushions, diversification (geographic, industrial, by customer or activity) or hedging. These strategies lead to a large portion of the risk being directly or indirectly transferred to other participants in the financial system such as customers, investors, financial markets, etc.

Therefore, to limit the risk associated with the transformation function associated with FIs, to protect depositors and savings, and to ensure the liquidity and solvency of the financial system, a prudential (micro and macro) supervisory approach has been adopted to regulate financial intermediation activities. This prudential approach is based on standards and principles such as capital requirements, liquidity ratios, accounting and provisioning standards, auditing and reporting standards, market entry rules or shareholding structures, market exit rules and disciplinary measures, protection of depositors as well as regulatory powers (Ahrend, Arnold and Murtin, 2009).

2.2 Normative Stakeholder Theory

CSR, in its broadest sense, is the subject of an abundant literature, and the concept of CSR is treated in numerous ways. Despite the polysemous character of CSR, approaches regarding the scope of corporate responsibilities can be categorized into two groups (Quazi and O'Brien, 2000): i) an approach characterized by a limited view of corporate responsibility, namely shareholder value maximization (Friedman, 1970), and ii) an approach that considers an expanded view of corporate responsibility (Freeman, 1984). The first approach is based on the traditional model of the firm that considers the firm as an individual agent likened to a black box in which inputs (capital, work, raw materials) are transformed into outputs (products and services) and sold on the market (Donaldson and Preston, 1995). The second approach considers the company as an open entity that interacts with its environment and towards which it has responsibilities, including value maximization, the integration of stakeholders' expectations, the promoting of common interests (Schwartz and Carroll, 2003) as well as the taking into account of negative externalities on stakeholders (Heal, 2005). This second approach currently represents the most popular CSR approach (Quazi and O'Brien, 2000).

Normative stakeholder theory advocates that the firm must meet the expectations of its stakeholders. According to the definition proposed by Freeman (1984) that defines a stakeholder as any group or individual that can affect or be affected by the activities of the firm, we can identify the following stakeholders for FIs in general: depositors, the government (which guarantees a portion of deposits), customers, investors, interbank market participants, shareholders, employees, regulators, the community and taxpayers[3] (Awotundun, Kehinde and Somoye, 2011). According to Schwartz and Carroll (2003), CSR encompasses the economic, legal and ethical expectations that society has towards organizations. Economic expectations include the activities that have a direct or indirect economic or financial impact on the firm. Legal expectations focus on compliance with the rules prescribed by society. Ethical expectations include the adoption and conformity by the firm to ethical rules, both local and international. Given the FI stakeholders listed above, we can therefore identify the following expectations (see figure 1): profitability (shareholders and investors), solvency (depositors, taxpayers, and interbank market participants), liquidity (depositors, interbank market participants, and regulators), compliance with rules and standards (regulators, community, government, employees and customers) and ethical compliance (community, government, employees and customers). Compliance with rules and standards includes, among others, compliance with common law rules regarding the operation of any

3. FIs can affect taxpayers, notably in periods of crises if they benefit from public funds (Bossone, 2001).

firm, compliance with provisions related to the products and services offered and compliance with prudential standards specific to FIs (discussed in section 2.3.1).[4]

2.3 Common Interest Theory

Common interest theory considers that the firm should positively contribute to the well-being of the community and should not be detrimental to the common good, whence the importance of an ethical behavior (Garriga and Melé, 2004). Thus, in addition to considering the expectations of stakeholders, CSR also involves the mitigation of negative externalities (Schwartz and Carroll, 2003). This ethical compliance is assessed in relation to conventions, deontology and teleology, as described below.

2.3.1 Conventional Ethics

Conventional ethics refer to the respect of principles or conventions relating to sustainable development and human rights. For FIs, these voluntary agreements can be categorized into two groups: standard conventions that apply to all sectors, and conventions specifically intended for FIs. The main conventions are presented in table 1. Standard conventions include, among others, the Global Compact, a United Nations initiative to support ten principles covering human rights, working conditions, the environment and the fight against corruption.[5] This standard, which includes principles related to the three main extra-financial factors (Environment, Social and Governance; ESG hereafter), forms the basis for most CSR indicators discussed in section 3.

4. Products and services offered by the FI can be subject to specific regulations. For example, following decisions by the United Nations Security Council, dispositions were made to regulate transactions with so-called at-risk countries or listed individuals. Similarly, FIs that operate internationally are also required to comply with the specific rules related to their activities and location, such as the *International Emergency Economic Powers Act* (IEEPA), the *Trading with the Enemy Act* (TWEA) and the *Foreign Account Tax Compliance Act* (FATCA). Failure to comply with these standards can lead to sanctions. For example, BNP Paribas has been convicted on May 1st, 2015 for violation of the IEEPA and the TWEA for transactions with Iranian, Sudanese and Cuban entities which are subject to economic sanctions. The bank was put on a 5-year probation period and paid $140 million, the largest financial penalty imposed on a FI for a criminal case.
5. See U.N. Global Compact website: <www.unglobalcompact.org>.

Table 1 – Description of the main standard and FI-specific conventions

This table presents a description of the main standard and FI-specific CSR-related conventions. *Dimensions* identifies the key extra-financial dimensions assessed in the convention, *Factors* identifies the main CSR factors (environmental, social or governance) included in the convention, *Evaluation of* indicates the type of organization targeted by the convention, *Number of signatories* indicates the number of organizations that signed the convention as of May 2017 and *Scope of the assessment* indicates whether only the FI is evaluated or whether the evaluation also includes its asset portfolios.

Type	Convention	Dimensions	Factors	Evaluation of	Number of signatories	FIs and/or portfolios
Standard conventions	*United Nations Global Impact*	Human rights; working conditions; environment; corruption	ESG	Firms	12,482	FIs
	Global Reporting Initiative (GRI)	ESG reporting	ESG	Firms	110,574	FIs
	ICC Business Charter for Sustainable Development	Fair and free competition; sustainable management	E	States	130	FIs
	United Nation Principles for Responsible Investment (UNPRI)	Issuer's ESG performance	ESG	Investors, investment managers and service providers	1,705	FIs + Portfolios
	Anti Money Laundering (AML)	Money laundering signalling policies and procedures	G	States	36 (including G20)	Portfolios
	Who Cares Wins	ESG reporting and integration in the investment process	ESG	FIs, firms, governments and multilateral institutions, regulators, financial markets, teaching and research establishments and NGOs	21	FI + Portfolios
FI-specific conventions	*United Nations Environment Programme Finance Initiative* (UNEP-FI)	Sustainable development; public information and awareness of ESG issues	ESG	FIs	200	FIs
	Equator Principles	Identification and evaluation of social and environmental risk for project financing ≥ $10 millions	ES	FIs	90	FIs
	Montreal Carbon Pledge (MCP)	Evaluation and reporting of assets' carbon footprint	E	Institutional investors	141	FIs + Portfolios
	Portfolio Decarbonization Coalition Initiative (PDCI)	Reducing the carbon footprint of investment portfolios	E	Institutional investors	27	FIs + Portfolios
	GRI Financial Services Sector Supplement (GRIFSSS)	Reporting on 49 environmental, social and economic indicators	ES + economics	FIs	110,574	FIs
	Sustainable Stock Exchanges Initiatives (SSEI)	Transparency and ESG performance; sustainable investment in financial markets	ESG	Financial markets	63	Portfolios

Among the conventions specifically designed for FIs, we find the Equator Principles that have been developed by a group of banks (ABN Amro, Barclays, Citigroup, Credit Lyonnais, Credit Suisse, Hypo, Rabobank, Royal Bank of Scotland, West LB and Westpac Banking Corp.), adopted in 2003 and later revised in 2006. They represent the commitment of the banking sector to promote responsible management and sustainable development.[6] The Global Reporting Initiative's (GRI) *Financial Services Sector Supplement (*GRIFSSS) includes 49 indicators grouped into three categories: i) economy, ii) environment and iii) society. The first category includes indicators of economic performance, the institution's presence on the market, indirect economic impacts and procurement practices. The second category includes materials, energy, water, biodiversity, emissions, effluents and waste, products and services, compliance, transportation, environmental assessment of suppliers and the environmental complaints mechanisms. The third category includes work practices, human rights, society and product liabilities.

2.3.2 Deontological Ethics

Deontological ethics, or deontology, refers to the obligations that individuals are required to comply with in their work.[7] It is related to sharing, in a comprehensive and objective matter, information on the nature or on the advantages and disadvantages of products and services offered. Deontology recommends that we refrain from giving information that is incomplete or truncated in order to derive a benefit, financial or not.[8] Deontological ethics can therefore include codes of conduct, the compensation structure, tax avoidance schemes, etc.

2.3.3 Teleological Ethics

Teleological ethics refer to the negative externalities generated by the FIs' activities. These activities include the products and services offered as well as the processes that have the potential to negatively affect the FI stakeholders, as illustrated in figure 1.

6. IFC (2012), *International Finance Corporation's Policy on Environmental and Social Sustainability*, online: <www.ifc.org>.
7. See website: <www.ethique.gouv.qc.ca>.
8. One such example would be the recent fictitious credit cards accounts scandal involving Wells Fargo that was unveiled in 2016. The Consumer Financial Protection Bureau has ordered the bank to pay $185 million, and an investigation has been opened by the Securities and Exchange Commission (SEC).

In terms of products and services, these externalities may come directly from the products and services (in this case, only the stakeholders are affected) or indirectly through the risks to which FIs are exposed. These risks include those that are related to the products and services such as credit risk, market risk and liquidity risk. In terms of processes, which are defined according to *ISO 9000:2005* standards as the set of correlated and interactive activities that transform inputs into outputs, externalities may come from infrastructures, human resources or procedures (i.e. a weakness in governance). They can also come from process-related risks such as operational risk, compliance risk, reputational risk and environmental risk. Thus, through failures or shortcomings such as computer breakdowns, frauds, errors or unauthorized transactions, processes can generate externalities that affect the various stakeholders of the FI. Human resources can also become a source of negative externalities through the compensation structure if managers and/or employees are incentivized to take on excessive risk. In the end, teleological ethics include the management of the sources of negative externalities that affect the FI's stakeholders, which implies that we can identify these sources and ways to mitigate them.

Overall, FISR encompasses stakeholders' expectations (profitability, solvency, liquidity, compliance with rules and standards, compliance with conventional and deontological ethics) and the management of negative externalities (teleological ethics). In this context, in order to fulfill their informative and predictive functions (Chatterji, Levine and Toffel, 2009), FISR indicators should cover all these components.

3. SOCIAL RESPONSIBILITY INDICATORS

CSR indicators are quantitative or qualitative data that have i) an informative function to communicate information regarding the firm's CSR level or progress in terms of social responsibility and ii) a predictive function to guide decision-making (Chatterji, Levine and Toffel, 2009). There are four main indicators of CSR: extra-financial reporting, extra-financial rating, CSR indices and CSR labels.

3.1 Extra-financial Reporting

Extra-financial (or CSR or sustainability) reporting is provided by the firm itself and covers the economic, environmental and social impacts of its activities. It also presents the corporation's value, its governance structure and the link between its strategy and its commitment to a sustainable economy. It may be presented either separately or integrated with standard financial information.[9] For FIs, extra-financial reporting is becoming more and more common. According to the GRI's sustainability disclosure database, 767 FIs around the world have disclosed some type of extra-financial report in 2016, compared with 6 in 2000 and 329 in 2010. In Canada, the largest banks and life insurers have all disclosed an extra-financial report in 2016. In fact, the Big5 banks have been doing so since 2010 (and some, like RBC of CIBC, since 2005). Because there are no formal guidelines to follow, the quality and coverage of these reports vary greatly from one institution to another.

3.2 Extra-financial Rating

Extra-financial rating or notation is provided by external agencies or organizations and represents an external, independent, opinion regarding the firm's socially responsible behavior. It is based on the extra-financial reporting made by the firm or its stakeholders as well as on standards suggested by international organizations (see section 2.3.1). Its objective is to provide information related to the firm's integration of stakeholders' interests and expectations as well as the managing of its negative externalities through internal policies or programs. The extra-financial rating sector includes local rating agencies, specialized agencies and international agencies. The three types of rating agencies are presented in table 2. Local agencies focus on a particular regional market. Specialized agencies are interested in specific areas or specific sectors. International rating is dominated by MSCI/KLD, EIRIS/VIGEO,[10] OEKOM, Sustainalytics,[11] INRATE, Thomson Reuters and Bloomberg.[12]

9. GRI (2013), *Sustainability Reporting Guidelines & Financial Services Sector Supplement*, online: <www.globalreporting.org>.
10. Vigeo and Eiris merged in 2015.
11. Sustainalytics and Jantzi Research Inc. merged in 2009.
12. Unlike other extra-financial rating agencies, Thomson Reuters (who provides *Asset4*) and Bloomberg, are considered to be *suppliers* of extra-financial information. For example, unlike agencies, suppliers do not provide, upon customer request, the rating of the securities in its portfolio. Asset4 offers raw ESG information collected from companies, NGOs and the press. Bloomberg now also offers ESG data collected from CSR reports, annual reports, corporate websites or other public sources.

Table 2 – Description of major extra-financial rating agencies

This table describes the three types of extra-financial rating agencies.

				Services offered										
Categories	**Agencies**	**Country of origin**	**Firms / States evaluated**	Corporate analysis	State analysis	Normative anaysis	SME analysis	Industrial/ ethical exclusion	Alerts/ Controversies	CSR indices	Vote counsel	Industrial analysis	Audit	Activism
Local agencies	Eco-Frontier	South Korea	2,200 firms	x		x		x		x				x
	Ecovalores	Mexico	n/a	x				x	x					
	Caer	Australia	360 firms	x				x	x				x	
	Grenneye	Israel	n/a	x				x	x					
	KO CSR	South Korea	n/a	x				x	x					
	OWW	Malaysia / Singapore	n/a	x		x		x		x				
	Reputex	Hong Kong	2,000 firms	x						x				
	Responsible Research	Singapore / Hong Kong	n/a	x		x		x	x					x
Specialized agencies	Ethifinance	France	450 firms / 100 States	x	x		x	x	x	x			x	
	Ethix	Sweden	7,000 firms	x		x	x	x	x					x
	Ges Insvestment Services	Sweden	18,500 firms	x				x	x	x			x	
	MAPLECROFT	U.K.	360 firms	x	x				x	x				
	Trucost	U.K.	4,500 firms	x		x								x
International agencies	MSCI/KLD	U.S.	5,000 securities / 90 States	x	x	x		x	x	x		x		x
	EIRIS/VIGEO	U.K.	15,800 firms /170 States	x	x	x	x	x	x	x	x	x	x	x
	OEKOM	Germany	3,500 firms / 56 States	x	x			x	x			x	x	x
	Sustainalytics	Netherlands	4,500 firms / 170 States	x	x	x	x	x	x	x		x		x
	Inrate	Switzerland	2,600 firms + 100 bond issuers	x	x	x		x	x			x		
Data suppliers	Thomson Reuters (Asset4)	U.S.	4,000 firms	ESG data vendor only										
	Bloomberg	U.S.	5,000 firms											

Extra-financial rating agencies identify a series of dimensions and a number of indicators that will be assessed for each firm. For example, MSCI/KLD evaluates the strengths and concerns for each firm on seven CSR-related dimensions (see Appendix A).[13]

3.3 CSR Indices

Social responsibility indices combine the best CSR-rated firms from a regular stock index. Their objective is to allow investors to follow the evolution of firms' extra-financial performance and compare the most socially responsible firms to the rest of the market. Table 3 presents the major CSR indices available. We see that most indices are developed and distributed directly by extra-financial rating agencies (see section 3.2). Their indices are based on their own extra-financial ratings and provide investors with the insurance that companies that are included in the index are selected, followed and evaluated according to their CSR. Private asset managers, such as Calvert Investment (U.S.) and Robecosam (Switzerland) for example, can also create indices based on their own criteria.

13. Each dimension is rated according to the strengths and concerns (or weaknesses) of the company on the indicators associated with this dimension. Thus, the strengths and concerns relating to each dimension are evaluated separately and binarily. For strengths, a value of 1 (0) represents the presence (absence) of a strength. For concerns, a value of 1 (0) represents the presence (absence) of a concern. The extra-financial agency also assesses the company's presence in one of six controversial activities: alcohol, gambling, tobacco, firearms, military activities and nuclear energy.

Table 3 – Description of the major CSR indices

This table presents the main CSR indices available.

CSR Index	Provider	Filter	Number of securities	Reference stock index	CSR index composition	Exclusions
Advanced Sustainable Performance Index (ASPI)	EIRIS/VIGEO	Positive	120	*DJ Euro Stoxx*	100 best in terms of CSR + 20 selected among those ranked 101st to 140th already included in ASPI	No
Calvert Social Index	Calvert Investments	Negative	680	*DJ Global Index*	Selected among the 1,000 biggest stocks in DJ Global Index based on Calvert social criteria	Gaming, tobacco, military
Dow Jones Sustainability Index (DJSI)	Robecosam	Positive	319	*DJ Global Index*	10% best in terms of CSR from the 2,500 largest in DJ Global Index	No
Dow Jones Sustainability Index (DJSI-Stoxx)	Robecosam	Positive	154	*DJ Euro Stoxx*	20% best in terms of CSR	No
Domini 400 Social Index	KLD/MSCI	Negative	400	*S&P 500*	Stocks with highest scores	Alcohol, gaming, tobacco, nuclear, arms and military
Ethibel Sustainability Index	EIRIS/VIGEO	Hybrid	200	*S&P Global*	Stocks with highest scores	Arms, energy, tobacco, jeux de hasard
FTSE4Good	EIRIS/VIGEO	Hybrid	270	*FTSE All Share Index*	Stocks with highest scores	Arms, tobacco and nuclear
Jantzi Social Index	Sustainalytics	Negative	50	*S&P/TSX*	50 Canadian stocks with highest scores	Tobacco, nuclear and military

Starting with a reference stock index, the CSR index provider selects stocks that will be included according to a number of predetermined criteria and filters. The filter or screen can be either negative (i.e. exclude specific securities), positive (i.e. include specific securities) or hybrid (i.e. sequential combination of positive and negative filters). The negative filter can be industrial (i.e. exclude stocks from specific sectors), normative (i.e. excluding stocks if non-compliance with a specific standard) or thematic (i.e. exclude stocks that are not related to a specific theme). The positive filter can be based on specific themes such as renewable energy or gender equality or be based on all three ESG factors. The positive filter can also be applied to a specific sector (*Best in class*), regardless of the business sector (*Best in universe*), or on the firm's progress regarding its socially responsible practices (*Best effort*). Periodic reviews are carried out to include newly eligible securities and exclude those that no longer fulfill the criteria. Exclusion from an index can result either from the deterioration of the firm's CSR performance or from the relative improvement of other firms.[14]

3.4 CSR Labels

Labels are seals of quality issued by non-profit organization or agencies that certify a specific quality or other CSR-related feature. They are usually backed by conventions, standards and requirements aimed at positively discriminating a firm by attributing it special CSR-related qualities that other firms in the same sector do not have. Table 4 provides some examples of CSR labels. There are two categories of CSR labels: industrial labels and international general labels. Industrial labels focus on specific areas or industries such as the Forest Stewardship Council that focuses on wood and its derivatives. International labels include B Corp, which assesses the performance of companies on the three ESG factors. In Canada, the Business Development Bank of Canada (BDC) is the only FI to have the B corporation certification (as of 2017).

14. For example, following the oil spill in the Gulf of Mexico in 2010, British Petroleum was excluded from the DJSI and FTSE4Good indices.

Table 4 – Description of the main CSR labels

This table presents some examples of CSR-related labels. *Provider* identifies the main provider of the label, *Country* identifies the country of origin of the label, *Content* identifies the factors or elements to be assessed by the label and *Target* identifies the entities who are targeted by the label.

Category	Label	Provider	Country	Content	Target
Industrial labels	FSC Certification	Forest Stewardship Council	Canada	Forest products	Firms
	Ecologo	UL	International	Product life cycle (e.g. furniture, cleaning products, electronics)	Firms
	Standards AFNOR	Association française de normalisation	France	ESG factors	Firms
	Transition Écologique et énergé-tique pour le Climat TECC)	French government	France	Environment	Firms
	ISR	FNG	Germany	ESG factors	Funds
	LuxFLAG Microfinance Label	Luxembourg Finance Labelling Agency	Luxembourg	Social	Funds
	LuxFLAG Environment Label	Luxembourg Finance Labelling Agency	Luxembourg	Environment	Funds
	LuxFLAG ESG Label	Luxembourg Finance Labelling Agency	Luxembourg	ESG factors	Funds
	Green Property	Credit Suisse Real Estate Fund Green Property	Switzerland	Green buildings	Funds
General labels	B Corp	B Lab	U.S.	ESG factors	Firms
	Climate Change and Etical Awards	Incisive Media	U.K.	ESG factors	Firms, funds and public institutions
	Your SRI Diamond Standard	CSSP, Center for Social ans Sustainable Products AG	Liechtenstein	ESG information and practices	Funds
	Ethibel EXCELLENCE	Ethibel	France	Responsible investment in stock and bond portfolios (A, B or C rating)	Funds
	Ethibel PIONEER	Ethibel	France	Responsible investment in stock and bond portfolios (A or B rating)	Funds
	European SRI Transparency Code	Eurosif	Belgium	ESG information and practices	Funds
	PRI	UNEPFI and UN Global Compact	U.S.	Sustainable portfolios	Funds
	ISO 26000	International Organization for Standardization	Switzerland	ESG factors	Firms
	ISO 14001	International Organization for Standardization	Switzerland	Environment	Firms
	Global Reporting Initiative (GRI	CERES and PNUE	U.S.	ESG reporting, impact and performance	Firms
	Responsible Invetsment Certified	RIAA	Australia	ESG reporting and education	Funds

3.5 Discussion

Despite their diversity, we see that the three types of CSR indicators are closely related. Specifically, extra-financial reporting by the firm or its stakeholders is instrumental to external extra-financial ratings, which are, in turn, fundamental to the construction of CSR indices and important for certifications or labels. However, despite the diversity of criteria assessed by extra-financial rating agencies, rating models are essentially based on the standards established by the Global Compact. Table 5 presents the different CSR dimensions assessed by major extra-financial rating agencies.[15] We see that, for all agencies, CSR ratings reflect elements from the three ESG factors. However, a more in-depth analysis of the specific indicators used to assess each factor (see, for e.g. Appendix A for MSCI/KLD) shows that they are effectively mainly based on the Global Compact principles and little or not at all related to other standards or conventions. For most non-financial companies (NFCs), Global Compact principles-based dimensions are sufficient to cover all their assets and operations. However, for FIs, whose assets are primarily financial, social responsibility should extend to investment portfolios such as loan or securities portfolios and include elements such as money laundering or other potential negative externalities, as suggested by the UNPRI standard or by FI-specific agreements such as PDCI (see table 1).

Table 5 – CSR dimensions evaluated by the major international extra-financial rating agencies

This table presents a summary of the dimensions assessed by the main international extra-financial rating agencies described in table 2.

ESG Factor	Dimension	MSCI / KLD	EIRIS / VIGEO	OEKOM	Sustainalytics	INRATE	Asset4
Environment (E)	Environment (ENV)	x	x	x	x	x	x
Social (S)	Community (COM)	x		x	x		x
	Diversity (DIV)	x			x		x
	Employees and suppliers (EMP)	x		x	x	x	x
	Human rights (HUM)	x	x				x
	Products and business practices (PROD)	x			x		x
	Business ethics (ETH)			x			
	International (INT)				x		
Governance (G)	Governance (GOV)	x	x	x	x	x	x

15. NOVETHIC (2016), *Notation extra-financière et empreinte carbone : acteurs et offres*, see website: <www.novethic.fr>.

For instance, in terms of the environmental (E) factor, FIs are evaluated according to their direct pollution or their recycling policy, among other things. However, the pollution or the recycling of the companies that make up the FI's portfolio of assets is not considered. Yet, because of their role as an intermediary, FIs can indirectly affect the environment via their portfolios of loans or securities. Financial assets are also increasingly sensitive to the risks related to climate change.[16] For example, stranded asset risk can strongly affect the value of FI assets (Caldecott and McDaniels, 2014) and thus affect the FI's stakeholders.[17] This is the case, for example, with investments in the shale gas sector, which represent a significant amount for a number of bank portfolios. With the falling of the oil barrel price and the enforcement or development of environmental policies, the value of reserves, which used to determine drilling companies' borrowing capacity, strongly depreciated and forced many bankruptcies.[18] This situation forced major banks to substantially increase their provisions to cover losses.[19] Therefore, because of the rapid development of climate-change-related regulations, of the removal of many subsidies related to fossil fuels, of technological development, of the increase in alternative solutions to fossil fuels, and because of declining energy prices, stranded asset risk is now a reality and a concern, not only for FIs but also for investors and authorities. In fact, according to a 2015 survey by Ernst & Young of pension funds, foundations and portfolio managers, 62.4% of respondents expressed their concern about asset risk.[20]

In terms of the social factor, only controversial investments are evaluated, with varying degrees of assessment.[21] However, even

16. Report from the University of Cambridge Institute for Sustainability Leadership (2015), *Unhedgeable risk: How climate change impacts investment sense.*
17. Stranded asset risk is the risk that an investment or an asset loses value or turns into a liability before the end of its economic life. This devaluation is mainly due to sudden and significant changes in legislation, environmental constraints or technological innovations, which makes assets obsolete before their full depreciation.
18. According to Haynes & Boones, LLP, 42 drilling companies filed for bankruptcy in 2015, see website: <www.haynesboone.com>.
19. For example, JP Morgan set aside $550 million in 2015 and another $750 million in 2016 because of the decline in the price of the barrel; Wells Fargo provisioned $1.2 billion in 2016 to cover potential losses in the oil and gas sector; Citigroup set aside $250 million in 2015 and added another $600 million in 2016; RBC provisioned $106 million in 2016; NBC provisioned $250 million in 2016.
20. ERNST & YOUNG (2015), *supra*, note 2.
21. For example, the Dutch NGO *PAX* issued a report in October 2015 showing the financial participation of 411 FIs in companies involved in the manufacture, storage

non-controversial products, services or processes can sometimes generate negative externalities for stakeholders or lead to irresponsible behaviors. For instance, in terms of products and services, predatory mortgage lending, such as ghost loans, balloon mortgages or repeated refinancing loans, have largely contributed to the high volume of subprime loans which are considered to be a determining factor in the 2007-2008 financial crisis in the U.S.[22] The $10 billion (nominal value) cross-currency swap proposed by Goldman Sachs to the Greek Government in 2001 to facilitate its entry into the Euro is another example. While the swap was legal under the various regulations in place at the time of its design, it nevertheless allowed Greece to conceal the real size of its debt, thereby circumventing Maastricht Treaty requirements regarding budget deficits.[23] In terms of processes, the dematerialization of financial activities to reduce transaction costs contributed to the emergence of alternative trading platforms such as dark pools or private securities trading systems. While the process is intended to improve market efficiency through better liquidity or the minimization of transaction costs and shocks on the market, some question its opacity or denounce the potential conflict of interest (Crudele, 2015).[24] Specifically, because they are considered as brokerage services and not formal exchanges (Matus, 2000), dark pools do not have to disclose information about their users or trading rules. High frequency trading is another example of a new process that some associate with high potential risks to stakeholders (Weber, 2011). Thus, while they offer advantages in terms of gains or reduced costs to FIs, processes sometimes generate negative externalities for stakeholders. In the end, products, services and processes must not only be analyzed in light of the different regulations to which they are subjected to, but also evaluated with respect to conventional, deontological and teleological ethics as discussed above.

and maintenance of nuclear weapons, report online: <www.dontbankonthebomb.com>. However, these investments are not considered by the main extra-financial rating agencies.

22. Predatory loans refer to a series of practices, including deception, fraud or manipulation, that a mortgage broker or lender may use to sign a loan that is disadvantageous to the borrower.
23. N. DUNBAR (2003), "Goldman Sachs' mega-deal for Greece", *RiskMagazine*, July 2003.
24. In fact, the Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA) in the U.S. have undertaken investigations on a few dark pools.

Finally, in terms of governance, vulnerabilities and failures of control systems, the compensation structure (such as bonuses) and compliance are little or not assessed (see, for example, Appendix A). We note, for example, the lack of assessment of compliance with the rules of common law or prudential rules. However, shortcomings related to these non-evaluated items can lead to sanctions or negative externalities that can affect firm returns or the value of the company.[25] Stock options offered to managers as a form of compensation can also become sources of negative externalities. Although intended to align the interests of managers and owners (shareholders), their amount can incentivize managers to excessive risk-taking or, in the worst cases, downright financial statement manipulation, which can jeopardize the institution.[26] Short-term performance objectives, which are also often associated with compensation, can also lead to excessive risk-taking, frauds or scandals.

4. THE SOCIAL PERFORMANCE OF FINANCIAL INSTITUTIONS

To examine the social performance of FIs, we conduct a descriptive and comparative analysis of extra-financial scores for FIs and NFCs during the period from 1991 to 2015. Scores are obtained from MSCI/KLD, one of the major extra-financial rating agencies, and represent the most commonly used data by researchers and investors (Waddock, 2003). Overall, our sample is composed of 50,163 extra-financial scores and covers 1,641 IFs and 7,103 NFCs during the period 1991-2015.

Table 6 shows descriptive statistics for the global aggregate scores.[27] We see that FIs obtained higher aggregate scores than NFCs

25. OXFORD METRICA (2012), *Reputation Review*, online: <www.aon.com>.
26. For example, between 2000 and 2007, just prior to the bankruptcy of Lehman Brothers, its chief operating officer, Richard Fuld, received approximately \$480 million in salaries and bonuses, of which approximately ¾ came from exercising his options.
27. The aggregate score for a given dimension is obtained in two steps. First, a standardized STRENGTH score and a standardized CONCERN score are obtained by dividing the number of strengths (or concerns) observed by the number of indicators evaluated. Second, the aggregate score on a given dimension corresponds to the STRENGTH score minus the CONCERN score for that dimension. Thus, an aggregate score of 0 means that there are as many strengths as there are concerns about this dimension. A positive (negative) score means that there are more (fewer) strengths than concerns observed on this dimension.

for 24 of the 25 years studied, although both types have a negative score on average over the years which indicates the presence of more concerns than strengths for the seven dimensions studied. Score volatility is systematically lower for FIs until the end of 2012. Figure 2 shows the evolution of annual average aggregate scores for FIs and NFCs between 1991 and 2015. We observe a relative stability of average scores over the years, both for FIs and NFCs, with a sudden increase in 2012 following the drop (notably for FIs) in 2011.

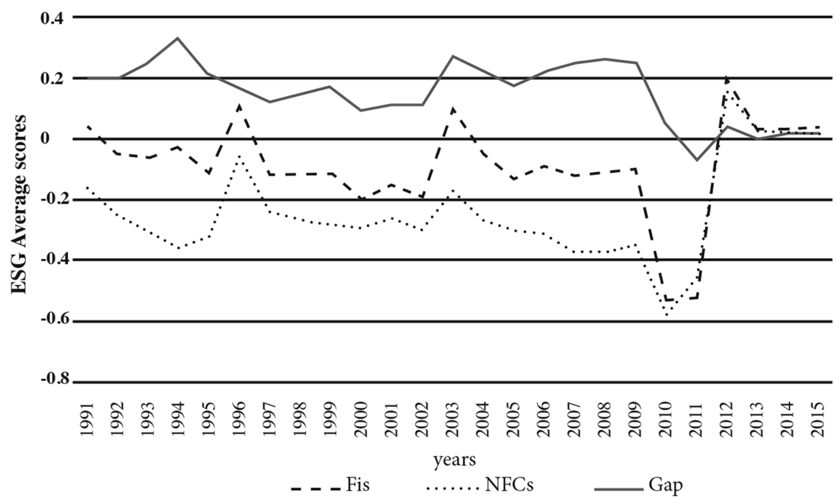
Table 6 – Descriptive statistics for the global aggregate scores for IFs and NFCs

This table presents the descriptive statistics for the global aggregate CSR scores for financial institutions (IF) and non-financial companies (NFC) in our sample. For each year, the number of firms examined is presented.

Year	N			Average		Std. Dev.		Minimum		Maximum	
	FI	NFC	Total	FI	NFC	FI	NFC	FI	NFC	FI	NFC
1991	71	576	647	0.04	-0.16	0.28	0.69	-0.67	-3.22	0.67	1.60
1992	65	587	652	-0.05	-0.25	0.49	0.81	-2.04	-3.55	0.93	1.75
1993	67	584	651	-0.06	-0.31	0.45	0.86	-1.48	-3.88	0.85	2.16
1994	68	575	643	-0.03	-0.36	0.47	0.84	-1.44	-3.77	1.33	2.47
1995	74	574	648	-0.11	-0.32	0.48	0.82	-1.33	-3.16	1.33	2.68
1996	79	573	652	0.11	-0.06	0.38	0.77	-1.17	-2.97	1.33	2.63
1997	84	569	653	-0.12	-0.24	0.56	0.90	-1.43	-4.01	1.57	2.63
1998	86	572	658	-0.12	-0.27	0.54	0.93	-1.11	-4.44	1.65	2.56
1999	88	574	662	-0.11	-0.28	0.57	0.87	-1.43	-4.42	1.65	2.56
2000	90	570	660	-0.20	-0.29	0.51	0.85	-1.44	-4.28	1.33	2.12
2001	183	924	1107	-0.15	-0.26	0.40	0.74	-1.92	-4.22	1.33	2.06
2002	226	882	1108	-0.19	-0.30	0.46	0.74	-1.92	-4.01	1.33	1.87
2003	664	2299	2963	0.10	-0.17	0.49	0.56	-3.68	-3.83	1.00	2.23
2004	635	2399	3034	-0.05	-0.27	0.56	0.62	-3.44	-4.02	1.08	1.78
2005	672	2343	3015	-0.13	-0.30	0.46	0.64	-2.42	-4.74	1.08	2.68
2006	643	2319	2962	-0.09	-0.31	0.43	0.59	-1.80	-4.47	0.92	3.05
2007	625	2312	2937	-0.12	-0.37	0.42	0.66	-1.88	-4.64	0.89	3.27
2008	617	2306	2923	-0.11	-0.37	0.43	0.68	-2.26	-4.80	0.89	2.87
2009	577	2335	2912	-0.10	-0.35	0.44	0.68	-2.26	-4.80	0.87	2.87
2010	619	2346	2965	-0.53	-0.58	0.47	0.61	-3.61	-3.27	0.49	1.94
2011	601	2247	2848	-0.52	-0.45	0.61	0.87	-2.56	-3.19	2.75	4.01
2012	633	2164	2797	0.20	0.16	0.46	0.58	-1.06	-2.69	2.75	3.95
2013	596	4094	4690	0.03	0.03	0.09	0.08	-0.17	-0.28	0.44	0.58
2014	615	4346	4961	0.04	0.02	0.09	0.07	-0.19	-0.26	0.35	0.39
2015	318	2097	2415	0.04	0.02	0.08	0.06	-0.11	-0.24	0.30	0.35
Total	**9,005**	**41,158**	**50,163**	**-0.10**	**-0.21**	**0.48**	**0.63**	**-3.68**	**-4.8**	**2.75**	**4.01**

The global aggregate score is determined by averaging the aggregate scores for the seven dimensions.

Figure 2 – Average global CSR scores for financial institutions and non-financial companies

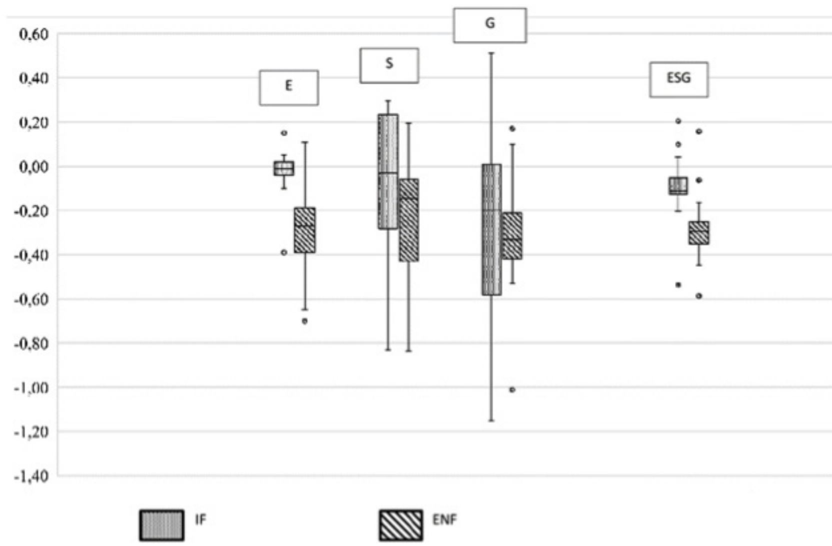


This figure shows the evolution of CSR average global scores for FIs and NFCs between 1991 and 2015 as well as the evolution of the gap between CSR scores for IFs and NFCs.

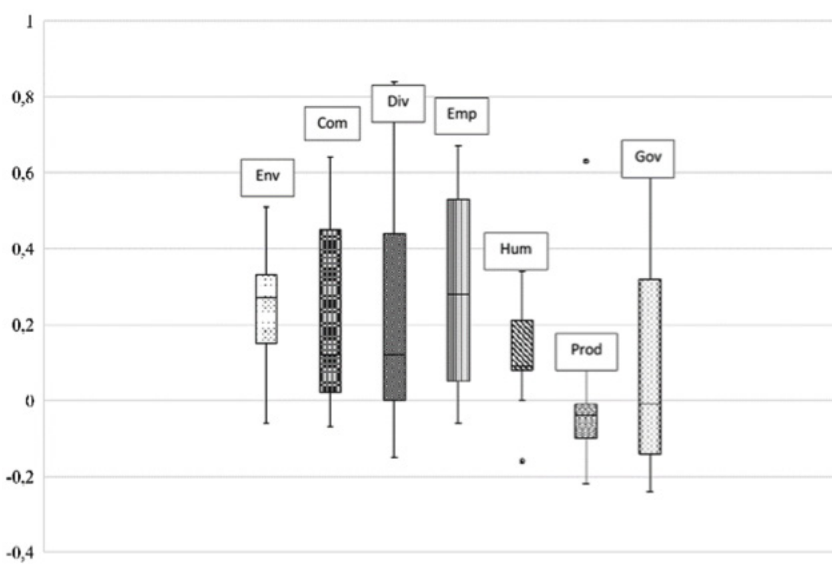
In order to better understand the gap between FIs and NFCs, Panel A of figure 3 presents the distribution of average scores, globally and for each ESG factor. For the environment (E) factor, the distribution of scores is denser for FIs than for NFCs, with 50% of FI scores between -0.04 and 0.02 (vs between -0.39 and -0.19 for NFCs). On the other hand, for the social (S) and governance (G) factors, the distribution of scores is denser for NFCs. Specifically, 50% of FI scores range between -0.28 and 0.23 (vs between -0.43 and -0.06 for NFCs) for the social factor and 50% of FI scores lie between -0.58 and 0.01 (vs between -0.42 and -0.21 for NFCs) for the governance factor. In terms of the global aggregate ESG score, the distribution is denser for FIs than NFCs where 50% of the scores range between -0.13 and -0.05 for FIs (against -0.35 and -0.25 for NFCs). Aggregate scores therefore differ mainly for the environmental and social factors.

Figure 3 – Score distribution

Panel A – Distribution of the average aggregate and global scores for IFs and NFCs



Panel B – Distribution of the score gap between IFs and NFCs



Panel B of figure 3 illustrates the gap between average aggregate scores for IFs and NFCs for the seven dimensions. For the environmental dimension, more than 75% of the annual differences are positive, indicating that FIs generally have superior scores than NFCs. For the social factor, composed of the community (COM), diversity (DIV), employees (EMP), human rights (HUM) and products (PROD) dimensions, the gaps are mainly positive for the first four dimensions. However, for the product dimension, we see that 75% of the differences are negative, which indicates that FIs have generally lower scores than NFCs. Finally, for the governance dimension, a little more than 50% of the differences are positive.

Details about the scores for each of the seven dimensions are presented in table 7. In general, we observe that FIs score higher than NFCs for the environmental factor as well as for most of the dimensions associated with the social factor. Specifically, for the environmental dimension, FIs have scores that are either statistically significantly higher than NFCs (16 of the 25 years studied) or statistically similar to NFCs (9/25 years). Further, for four of the five dimensions related to the social factor, statistically significant differences between scores for FIs and NFCs are almost always in favour of FIs. Specifically, IFs obtain significantly higher scores for Community (13/25 years), Diversity (9/25 years), Employees (13/25 years) and Human Rights (11/25 years). Further, for the latter three dimensions, FIs' scores are never significantly lower than NFCs. The only dimension within the social factor for which IFs and NFCs have statistically similar scores (with the exception of 2012) is Products (PROD) dimension. Finally, for the governance dimension, the differences between FIs and NFCs vary according to the years. Nevertheless, FIs obtain significantly higher (lower) scores than NFCs for 7 (3) of the 25 years studied. For all the dimensions, we observe a decrease in the gaps between scores for FIs and NFCs for the last three years of our sample, namely 2013-2015.

Table 7 – Average annual scores for seven CSR-related dimensions

This table presents the average aggregate scores for seven CSR-related dimensions: environment (ENV), community (COM), diversity (DIV), employees (EMP), human rights (HUM), products (PROD) and governance (GOV). Panel A presents aggregate scores for financial institutions (IF), while Panel B presents aggregate scores for non-financial companies (NFC). Panel C presents the differences between FI and NFC scores, as well as the results of a t-test for independent samples for the significance of the differences. ***, ** and * refer to statistical significance at a threshold of 1%, 5% and 10% respectively. The dimensions and the associated indicators are presented in Appendix A.

	Panel A - FI							Panel B - NFC							Panel C - Difference (FI - NFC)						
	E	S					G	E	S					G	E	S					G
Year	ENV	COM	DIV	EMP	HUM	PROD	GOV	ENV	COM	DIV	EMP	HUM	PROD	GOV	ENV	COM	DIV	EMP	HUM	PROD	GOV
1991	-0.01	0.91	0.31	0.14	-0.56	-0.18	0.01	-0.39	0.35	0.20	0.08	-0.79	-0.13	-0.04	0,38**	0,57***	0.11	0.06	0.23	-0.04	0.05
1992	-0.10	0.97	0.40	-0.04	-0.46	-0.15	-0.20	-0.54	0.37	0.29	-0.01	-0.80	-0.11	-0.16	0,44*	0,61***	0.11	-0.03	0.34	-0.04	-0.04
1993	-0.07	0.82	0.21	0.04	-0.25	-0.26	-0.22	-0.58	0.43	-0.42	-0.01	-0.55	-0.07	-0.21	0,51**	0,39**	0,62**	0.05	0,30*	-0.19	-0.01
1994	-0.03	1.01	0.31	0.13	-0.10	-0.07	-0.31	-0.65	0.37	-0.54	-0.11	-0.31	-0.13	-0.27	0,62**	0,64***	0,84***	0.24	0.21	0.06	-0.04
1995	0.00	0.98	0.47	0.10	-0.14	-0.24	-0.58	-0.47	0.42	-0.28	-0.08	-0.21	-0.20	-0.40	0,47**	0,56***	0,75***	0.18	0.08	-0.04	-0.17
1996	0.03	0.87	0.55	-0.10	-0.13	-0.28	0.13	-0.26	0.41	-0.13	-0.04	-0.14	-0.24	0.10	0.29	0,46***	0,68***	-0.06	0.01	-0.04	0.03
1997	0.05	0.80	0.65	0.30	-0.12	-0.39	-0.66	-0.27	0.35	0.03	0.04	-0.27	-0.28	-0.42	0.32	0,45***	0,62**	0.26	0.15	-0.11	-0,24*
1998	0.05	0.58	0.53	0.50	-0.04	-0.29	-0.66	-0.27	0.19	0.15	0.16	-0.23	-0.38	-0.53	0.32	0,39***	0,38*	0,34**	0.19	0.09	-0.13
1999	0.02	0.54	0.52	0.68	-0.04	-0.45	-0.60	-0.32	0.10	0.18	0.10	-0.27	-0.44	-0.46	0,33*	0,44***	0.33	0,58***	0,23*	-0.01	-0.14
2000	-0.04	0.21	0.60	0.73	-0.17	-0.64	-0.72	-0.27	0.13	0.17	0.16	-0.26	-0.50	-0.53	0.23	0.08	0,44*	0,56***	0.09	-0.14	-0.19
2001	-0.04	0.12	0.30	0.24	-0.08	-0.74	-0.37	-0.30	0.00	0.24	-0.07	-0.24	-0.52	-0.37	0,26**	0,12*	0.06	0,31***	0,16**	-0.22	-0.01
2002	-0.06	0.03	-0.07	0.15	-0.06	-0.76	-0.36	-0.23	-0.02	0.08	-0.13	-0.24	-0.66	-0.48	0,17*	0.05	-0.15	0,28***	0,18***	-0.1	0.12
2003	-0.03	0.01	-0.37	-0.21	-0.01	-0.33	0.51	-0.15	-0.01	-0.27	-0.55	-0.20	-0.37	-0.09	0,12***	0.02	-0.10	0,34***	0,19***	0.04	0,59***
2004	-0.05	0.02	-0.66	-0.31	-0.04	-0.42	0.17	-0.19	0.00	-0.65	-0.72	-0.28	-0.34	-0.22	0,14***	0.02	-0.01	0,40***	0,23***	-0.08	0,39***
2005	-0.03	0.01	-0.67	-0.34	-0.03	-0.45	-0.05	-0.19	-0.06	-0.73	-0.81	-0.12	-0.41	-0.27	0,16***	0,07*	0.07	0,47***	0,09***	-0.04	0,22***
2006	-0.01	-0.02	-0.50	-0.32	-0.03	-0.48	0.01	-0.16	-0.05	-0.70	-0.84	-0.12	-0.44	-0.34	0,15***	0.02	0,20*	0,53***	0,09***	-0.04	0,36***
2007	-0.02	-0.08	-0.66	-0.26	-0.03	-0.50	-0.04	-0.29	-0.12	-0.79	-0.82	-0.12	-0.46	-0.35	0,27***	0.03	0.13	0,57***	0,09***	-0.04	0,32***
2008	0.00	-0.02	-0.60	-0.20	-0.03	-0.53	-0.04	-0.27	-0.15	-0.82	-0.84	-0.12	-0.47	-0.36	0,27***	0,13***	0,22**	0,65***	0,09***	-0.07	0,32***
2009	0.00	-0.01	-0.67	-0.20	-0.03	-0.54	-0.01	-0.26	-0.14	-0.79	-0.86	-0.11	-0.45	-0.33	0,26***	0,13***	0.12	0,67***	0,09***	-0.09	0,32***
2010	-0.39	0.10	-3.77	-0.09	0.00	-0.39	-0.39	-0.70	0.12	-3.64	-0.31	-0.01	-0.34	-0.22	0,31***	-0.03	-0.13	0,22***	0.01	-0.05	-0,17***
2011	0.30	0.11	-3.53	0.01	0.02	-0.16	-1.15	0.36	0.17	-3.49	0.00	-0.06	-0.06	-1.01	-0.06	-0,07**	-0.04	0.01	0.08	-0,10*	-0,14***
2012	0.15	0.14	-0.35	0.01	1.09	0.58	0.17	0.11	0.19	-0.43	0.01	1.25	-0.05	0.17	0.04	-0,05**	0.08	0.00	-0.16	0,63***	-0.01
2013	0.02	0.04	-0.14	0.11	0.00	0.00	0.06	0.03	0.09	-0.07	0.11	0.06	-0.01	0.01	-0.01	-0.05	-0.07	0.00	-0.06	0.01	0.05
2014	0.02	0.00	-0.08	0.04	0.00	0.01	0.10	0.03	0.02	-0.06	0.04	0.06	-0.01	0.02	-0.01	-0.02	-0.02	0.00	-0.06	0.02	0.07
2015	0.01	0.00	-0.03	0.06	0.00	0.00	0.10	0.02	0.00	-0.01	0.05	0.03	-0.01	0.03	-0.01	0	-0.01	0.00	-0.02	0.01	0.07
Total	**-0.01**	**0.09**	**-0.78**	**-0.09**	**0.04**	**-0.29**	**-0.09**	**-0.16**	**0.05**	**-0.70**	**-0.31**	**-0.05**	**-0.25**	**-0.22**	**0.15**	**0.03****	**-0.08**	**0.22*****	**0.10**	**-0.03**	**0.13**

Overall, FIs appear to perform well in terms of CSR, at least related to NFCs. With the exception of one dimension within the social factor, namely the product dimension, FIs often have higher scores than NFCs. However, this difference disappears in the last three years of our sample.

5. CONCLUSION

The purpose of this chapter is to better understand FISR. To do so, CSR indicators are analyzed against stakeholders' expectations and sources of negative externalities of the FIs. Based on financial intermediation theory, stakeholder theory and common interest theory, the expectations of stakeholders are identified and sources of externalities are circumscribed. Extra-financial ratings, CSR indices and labels are discussed. Extra-financial ratings incorporate company and stakeholder reporting while labels are CSR indices, in turn, based mainly on extra-financial ratings. Extra-financial ratings are therefore a representative of social responsibility.

In order to provide an empirical picture of the social performance of FIs, we conducted a descriptive and comparative analysis of extra-financial scores for IFs and NFCs. Our analysis of 50,163 extra-financial scores produced by MSCI/KLD, which involve 1,641 IFs and 7,103 NFCs for the period 1991-2015, reveals a good social performance by IFs compared to NFCs. Specifically, IFs get average scores above those by NFCs for the three ESG factors as well as for the global score. The gaps between IF and NFC scores are particularly important for the environmental factor as well as for some dimensions of the social factor.

The fact that many scores are negative would certainly deserve some additional examination, although this can very well be attributed to the way scores are estimated. Further, despite the empirical social performance of FIs, it is important to question the adequacy of extra-financial ratings to measure social responsibility. The discussion in section 3.5 concludes with the importance of integrating the specificities of the financial sector to assess FISR. In light of this discussion and our empirical results in section 4, it would be interesting to see if FIs still over-perform relative to NFCs when these specificities are also considered. We leave this for future research.

APPENDIX A – AN EXAMPLE OF EXTRA-FINANCIAL RATING INDICATORS

This table presents the indicators of strengths and concerns for each of the seven dimensions evaluated by MSCI/KLD, a major extra-financial rating agency.

Dimensions	Strengths	Concerns
Community	– Charitable donations – Innovative donations – Non-US charitable donations – Support for housing – Support for education – Indigenous peoples relations – Volunteer programs – Other strengths	– Investment controversies – Negative economic impact – Indigenous peoples relations – Tax disputes – Other concerns
Corporate Governance	– Limited compensation – Ownership strength – Transparency strength – Political accountability strength – Other strengths	– High compensation – Ownership concern – Accounting concern – Transparency concern – Political accountability concern – Other concerns
Diversity	– Diversity in the CEO – Gender and minority promotion – Board of Directors – Work/Life benefits – Women & minority contracting. – Employment of the disabled – Gay & Lesbian policies – Other strengths	– Controversies – Non-Representation – Other concerns
Employee Relations	– Union relations – No-Layoff policy – Cash profit sharing – Employee involvement – Retirement benefits strength – Health and Safety strength – Other strengths	– Union relations – Health and Safety concern – Cash profit sharing – Workforce reductions – Retirement benefits concern – Other concerns

Dimensions	Strengths	Concerns
Environment	– Beneficial products and services – Pollution prevention – Recycling – Clean energy – Communications – Property, plant, and equipment – Management systems – Other strengths	– Hazardous waste – Regulatory problems – Ozone depleting chemicals – Substantial emissions – Agricultural chemicals – Climate change – Other concerns
Human Rights	– Positive record in South Africa – Indigenous peoples relations strength – Labor rights strength – Other strengths	– South Africa – Northern Ireland – Burma concern – Mexico – Labor rights concern – Indigenous peoples relations concern – Other concern
Product	– Quality – R&D/Innovation – Benefits to economically disadvantaged – Other strengths	– Product safety – Marketing/Contracting concern – Antitrust – Other concerns

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