SUSTAINABLE IMPACT INVESTING

The next step in the evolution of Socially Responsible Investing (SRI)

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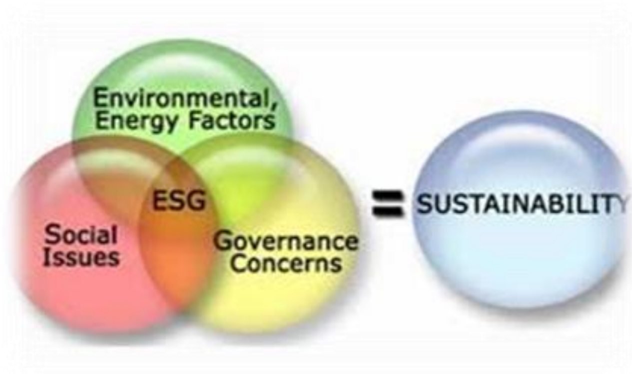
At SmartTrust®, we look to provide for diversified income and total return opportunities through innovative investment strategies. The majority of SmartTrust® Unit Investment Trusts (UITs) offer diversified income opportunities (*as well as the potential for total return*) and have incorporated such underlying investment strategies as individual taxable and tax-free bonds, individual stocks, preferred stocks, business development companies (BDCs), closed-end funds (CEFs) and exchange traded funds (ETFs). This particular report will focus on a growing trend amongst financial advisors, and their clients, across the country to invest in companies that provide for a sustainable global impact and include an overview of the innovative equities-based solution from SmartTrust® in this regard.

Sustainable impact investing is not necessarily something new to Wall Street but rather actually just the next step in the evolution of socially responsible investing (SRI) strategies. For those who may not be aware, socially responsible investing is an investment style that uses both positive and negative screens to include or exclude companies in a portfolio based on social, moral, ethical and religious criteria. For the majority of the existing SRI strategies in the marketplace, this equates to an exclusionary process that excludes companies who may have a certain percentage of their revenue derived from areas such as weapons, tobacco, alcohol or gambling. Other strategies may look to exclude the stocks of companies in certain industries, or sub-industries, which are associated with these socially taboo areas. One of the oldest, and most recognized SRI indexes, is the Domini 400 Index. This index, which is now the MSCI KLD 400 Social Index, was launched back in 1990 and currently uses the MSCI USA IMI ESG Index as its selection universe. According to its stated index methodology, companies involved in the following activities are excluded from the index:

- Alcohol
- Gambling
- Tobacco
- Military Weapons
- Civilian Firearms
- Nuclear Power
- Adult Entertainment
- Genetically Modified Organisms

Some critiques of traditional socially responsible investing strategies are that they often do not consider the investment merits of a given company's stock and that the excluded companies that were perhaps “sinful” in certain areas were providing positive, sustainable characteristics in other areas and yet are excluded anyway. Limiting the sectors or industries that are included in a given investment portfolio can also hinder potential diversification and/or growth of capital opportunities.

Sustainable, responsible and impact investing, on the other hand, offers what I believe to be a more dynamic approach to investing in this rapidly growing area. This type of investing involves more of a positive, proactive and comprehensive review of a company to provide for a more robust picture of the company’s operations and social, as well as economic, impact. Factors considered for this type of investing generally fall into the categories of environmental, social and governance (ESG).



Picture Source: *www.dealmarketblog.com*

Investopedia defines the application of these factors as, a set of standards for a company’s operations that socially conscious investors use to screen investments.

- **E**nvironmental criteria looks at how a company performs as a steward of the natural environment
- **S**ocial criteria examines how a company manages relationships with its employees, suppliers, customers and the communities where they operate
- **G**overnance deals with a company’s leadership, executive pay, audits, internal controls and shareholder rights

Through impact investing, investors will look to invest in businesses or investment strategies that combine both social and financial returns. Investment funds (*i.e. mutual funds, variable annuity funds, closed-end funds, exchange-traded funds, alternative investment funds and other pooled products*) incorporating ESG factors have grown considerably since 1995. The number of funds incorporating ESG factors has grown by nearly 1,600% from just 55 in 1995 to 925 in 2014. Additionally, total assets invested in funds that incorporate ESG factors have also increased by nearly 36,000% from $12 billion in 1995 to $4,306 billion in 2014.

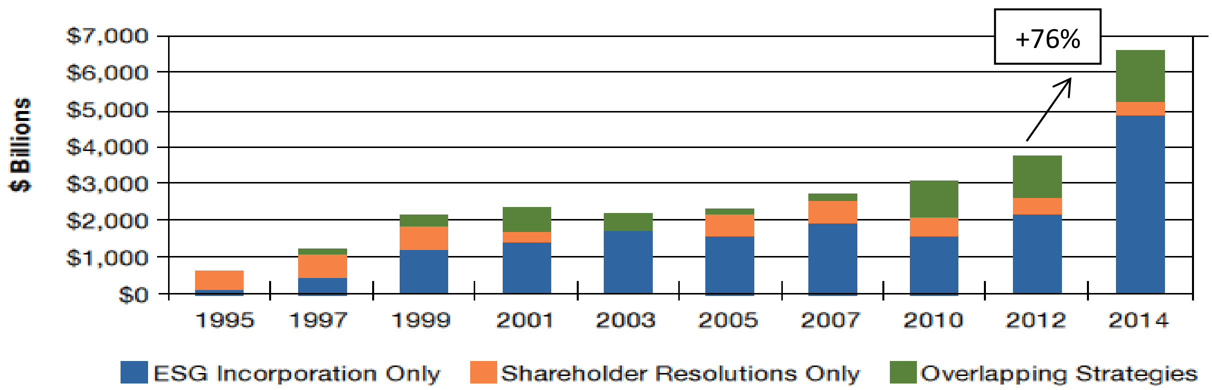
Investment Funds Incorporating ESG Factors (1995 – 2014)

	1995	1997	1999	2001	2003	2005	2007	2010	2012	2014
Number of Funds	55	144	168	181	200	201	260	493	720	925
Total Net Assets (In Billions)	$12	$96	$154	$136	$151	$179	$202	$569	$1,013	$4,306

SOURCE: US SIF Foundation.
NOTE: ESG funds include mutual funds, variable annuity funds, closed-end funds, exchange-traded funds, alternative investment funds and other pooled products, but exclude separate account vehicles and community investing institutions.

Overall, a growing number of investors are considering sustainable, impact, environmental and socially responsible factors in the asset allocation decision making process. To this end, the total U.S.-domiciled assets under management using Sustainable, Responsible and Impact (the "new SRI") strategies expanded from $3.74 trillion at the start of 2012 to $6.57 trillion at the start of 2014 according to the U.S. Sustainable, Responsible and Impact Investing Trends 2014 report.

Total Assets using "new SRI" Strategies



SOURCE: US SIF Foundation.

Some Wall Street investment firms are promoting the benefits that sustainable impact investing has in their investment platforms. For example, according to Morgan Stanley's website, they will, "…*expand the Investing with Impact Platform through new products and innovative thematic portfolios to meet rapidly rising client demand for new opportunities. The Firm has set a five-year goal of $10 billion in total client assets through the Investing with Impact Platform.*" As another example, Goldman Sachs Asset Management stated in a January 2013 article entitled, "GSAM Statement on Responsible and Sustainable Investing" that, "*We believe responsible and sustainable investing extends beyond the evaluation of quantitative factors and traditional fundamental analysis. Where material, it should include the analysis of an entity's impact on its stakeholders, the environment and society. We recognize that these environmental, social, and governance (ESG) factors can affect investment performance, expose potential investment risks, and provide an indication of management excellence and leadership*."

The rising trend toward the "new SRI" is not limited to the United States. Assets under management incorporating sustainability investment strategies reached $21.1 trillion globally as of the beginning of 2014, up 61% from the onset of 2012, said the "*Global Sustainable Investment Review 2014*," released recently by the Global Sustainable Investment Alliance. As a result of the growth, assets that use a sustainability approach accounted for 30.2% of all assets under management across the regions covered by the review, up from 21.5%. Interestingly, negative screening (i.e. "old SRI") is the largest strategy in Europe, while ESG integration (i.e. "new SRI") now dominates in the United States, Australia/New Zealand and Asia in asset-weighted terms according to the report.

Additionally, according to a Merrill Lynch article entitled, "Socially responsible investing: Aligning your principles with your investing goals", managers representing 15% of the world's investable assets committed to socially responsible investing in 2013 and managers/strategies representing more than $45 trillion in assets committed to investing through the United Nations Principles for Responsible Investment (UNPRI) in 2014.

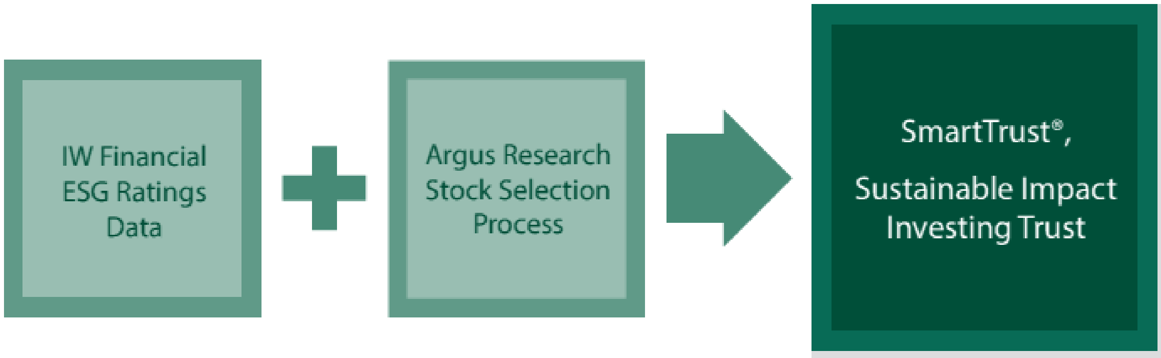
The UNPRI is at the core of the global sustainable and responsible investment movement. The Principles for Responsible Investment were developed by an international group of institutional investors reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The process was convened by the United Nations Secretary-General. These are the six stated principles:

- **Principle 1**: We will incorporate ESG issues into investment analysis and decision-making processes.
- **Principle 2**: We will be active owners and incorporate ESG issues into our ownership policies and practices.
- **Principle 3**: We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- **Principle 4**: We will promote acceptance and implementation of the Principles within the investment industry.
- **Principle 5**: We will work together to enhance our effectiveness in implementing the Principles.
- **Principle 6**: We will each report on our activities and progress towards implementing the Principles.

Companies are invited to apply to become a signatory of the UNPRI if they can demonstrate their commitment to responsible investment and desire to be at the heart of the global community seeking to build a more sustainable, overall financial system. There are three categories of signatories to the UNPRI which include asset owners (288), investment managers (884) and professional service partners (187).

<u>The SmartTrust® Approach</u>

The innovative approach to sustainable, responsible impact investing at SmartTrust® combines the research and technology solutions, provided by IW Financial, that help financial professionals evaluate the environmental, social, and governance performance of companies with the equity management and research expertise of Argus Research Company.



IW Financial, led by CEO Sam Pierce, is a leading provider of objective research and technology solutions that help financial professionals evaluate the environmental, social, and governance performance of companies. Established in 2001, the company is headquartered in Portland, Maine. IW Financial is a current signatory of the United Nations Principles of Responsible Investing (UNPRI) within the category of professional service partners. IW Financial was named by World Finance magazine's ESG Awards as the best U.S. research house in 2009.

Argus Research Company, on the other hand, produces independent research for investors. Since 1934, their business has been to produce, distribute and market high-quality investment and economic research. Their recommendations reflect the judgment of an analyst about a company's prospects as an investment in terms of value, expected growth and risks. Their research system involves rigorous quantitative analysis into a company's growth prospects, financial strength and valuation. The framework also requires detailed qualitative analysis into the company's industry, the risks it faces and, most importantly, the quality and integrity of its management team.

Utilizing IW Financial research and "Best in Class" (BIC) ratings methodology that looks at 60 points of distinct criteria, the **SmartTrust® Sustainable Impact Investing Trust** strategy digs deeper to incorporate a more comprehensive SRI/ESG portfolio while introducing a performance element using Argus Research. The 60 points of ESG data are broken into 14 issue areas as follows:

Issue Area 1: *Auditing & Accounting*

1. Financial expert on audit committee
2. Disclosed percentage of audit fees
3. Restatement of financials

Issue Area 2: *Board Accountability*

4. Board responsibility for the company's human rights policy
5. Board responsibility for the environmental policy
6. Board responsibility for the climate change policy

Issue Area 3: *Board Composition*

7. Tenured directors
8. Directors over age 70
9. Directors that are active CEOs
10. Absentee Directors (*attended less than 75% of meetings*)
11. Directors on more than 4 boards

Issue Area 4: *Board Independence*

12. Percentage independent board members
13. Independent audit committee
14. Independent compensation committee
15. Independent governance committee
16. Independent nominating committee

Issue Area 5: *CEO Compensation*

17. Incentive pay as a percentage of total

Issue Area 6: *Climate Change*

18. Climate change disclosure
19. Climate change policy
20. Direct GHG emissions
21. Direct GHG emissions per revenue
22. Indirect GHG emissions
23. Indirect GHG emissions per revenue

Issue Area 7: *Community & Politics*

24. Community involvement policies and programs
25. Political policies and disclosure
26. Predatory lending
27. Community Reinvestment Act rating

Issue Area 8: *Diversity*

28. Senior management percentage of woman
29. Senior management percentage of minorities
30. Diversity disclosure
31. Percentage of females on the Board of Directors

Issue Area 9: *Environmental Management*

32. Environmental disclosure
33. Environmental policy
34. ISO 14001 environmental management systems

Issue Area 10: *Environmental Performance*

35. Toxic emissions
36. Toxic emissions per revenue
37. Toxic emissions trend
38. Toxic production waste
39. Toxic production waste per revenue
40. Toxic production waste trend
41. Chemical or oil spills
42. Chemical or oil spills per revenue
43. Chemical or oil spills trend
44. Environmental fines
45. Environmental fines per revenue
46. Environmental fines trend
47. Energy use
48. Energy use per revenue
49. Water use

50. Water use per revenue

Issue Area 11: *Human Rights*

51. Oppressive regime (weighted exposure)
52. Human rights disclosure
53. Human rights policy

Issue Area 12: *Recognition*

54. Diversity recognition
55. Workplace recognition

Issue Area 13: *Sexual Orientation*

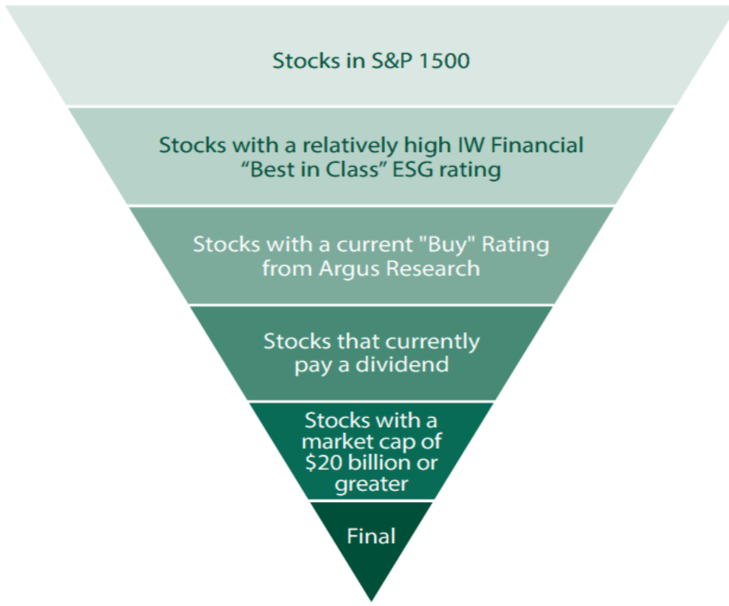
56. Non-discrimination policy

Issue Area 14: *Workforce*

57. Strikes or labor actions
58. Workforce disclosure/policy
59. Employee benefits
60. EEOC disciplinary action

Each company within the S&P 1500 is applied with an overall BIC rating on a scale of 0 – 100. Some may be surprised to see some of the names that receive a high relative BIC rating after applying this comprehensive listing of ESG screens. As a result, it is important for investors to not make assumptions about the sustainability of a given company based upon the industry they operate within or past difficulties that they may have experienced as it relates to environmental, social or governance factors. Such previous difficulties may have resulted in the company changing their policies, or even implementing new policies, to address such sustainability matters. In addition, the BIC ratings from IW Financial represent a current ESG assessment of each company, which we would argue is more relevant than a historical assessment that may no longer prove to be accurate.

Argus Research then seeks to find those companies with a relatively high BIC Rating from IW Financial and a "Buy" rating from Argus Research. A "Buy" rating means that Argus Research Company estimates the security to deliver a risk-adjusted return that beats the S&P 500 Index over the next 12 months. Argus only considers dividend paying large-cap companies (*which it defines as companies with market capitalizations greater than $20 billion*) for inclusion in the Trust's portfolio in an effort to find sustainable companies that are at least in the large-cap category and signal they value their shareholders by paying a dividend.



While there is nothing inherently wrong with traditional socially responsible investing strategies, and incorporating exclusionary screening factors such as tobacco, weapons and gambling certainly have their merits and appreciative audience of investors, we feel that our approach to sustainable impact investing represents the next step in the evolution of socially responsible investing and can be consistent with investors' attutides towards promoting a sustainable, responsible world and desires for competitive investment return. In other words, these two objectives no longer need to be mutually exclusive.

Picture Source: *Market and Sell to Women, "Impact Investing – Can you Make a Difference and Make Money?" October 28, 2014.*

According to IW Financial's website, "*Historically, values-based investor requirements were mostly exclusionary: avoiding ownership of stocks with exposure to certain industries such as tobacco or nuclear power. Today, however, investor demands have grown to incorporate a broader range of issues and ideas, and a wider range of perspectives.*" In our view, the SmartTrust®, Sustainable Impact Investing Trust is worthy of consideration for investors with these new demands.

This paper is provided for informational purposes only. The discussion of specific stocks or UITs is not a solicitation to buy or sell any of the referenced securities. Investors should consider the Trust's investment objective, risks, charges and expenses carefully before investing. The prospectus contains this and other information relevant to an investment in the Trust. Please advise your clients to read the prospectus carefully before they invest. If a prospectus did not accompany this literature, please contact SmartTrust at (888) 505-2872 or visit www.smarttrustuit.com to obtain a free prospectus.