

The Difference That Catholic Institutional Investors Can Make

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Introduction

The initial decision by institutional investors in the Catholic community to invest some of their assets in equities emerged from a number of considerations. Increased return for the mission of their institutions and organizations; diversification of investment portfolios and the fulfilment of their fiduciary responsibilities informed this transition. Most of these decisions were taken following the advice of financial consultants and advisors from the financial community, who were retained by investors.

At the time that this was taking place most corporations were singularly focused on their respective business models which included manufacturing products, delivering services, growing market share, enhancing the value of their stock and satisfying the board and their major shareholders. This perspective fit conveniently into the overall expansion of corporate capitalism and into the commonly accepted business practice of the day.

In recent decades the social and environmental responsibility of the corporation has elbowed its way on to many corporate agendas. It continues to be a hotly debated topic in general terms, but it also raises very specific issues and different challenges depending on the business sector and the business model which a corporation is following. Corporate social responsibility movement has both spawned many debates and opened a whole new area of research.

Frank Dixon in his article on “Total Corporate Responsibility” characterizes the challenge as follows;

“While business obviously provides great benefits to society, it also has large negative impacts, both directly through manufacturing and indirectly through consumption of its products and services. Negative impacts are tangible (pollution, inefficient use of resources, destruction of natural habitat and biodiversity, unsafe products, layoffs etc) and intangible (disruption of indigenous cultures, degradation of cultural values and public spirit by overemphasizing materialism, etc)” *Total Corporate Responsibility Funds; Maximizing Financial and Sustainability Performance Frank Dixon (Published in GreenBiz.com, January 2005)*

The effort to capture and respond to these negative impacts has resulted in the development of new industries, new tools, new partnerships and new debates and I will highlight some of these developments throughout this paper.

In the Catholic and faith communities, since Vatican II, when the doors and windows were thrown open to promote a new consideration of the church’s engagement with the world, catholic institutional investors have been confronted with a series of new questions and challenges. Many of these challenges have been centered on a critical and evolving consideration of mission and have surfaced from different directions. Often, a growing awareness of the increased influence of multinational corporations, which was brought to their attention by colleagues in the far flung missionary corners of the world, raised significant ethical questions about some of their equity positions. At other times questions arose from considerations that were

more internal to the integrity of the work or mission of their own institutions and its position within the Catholic tradition.

This paper suggests that the contribution of catholic and other faith based institutional investors to the growth/evolution of a business model, that includes all the costs of doing business, has and continues to be significant. Though reluctant to include social and environmental considerations in their operations at the outset, an increasing number of corporations and their leaders have demonstrated not only an openness to this development but have embraced it as a growth strategy. While the mainstream catholic community and the official hierarchy have been slow to appreciate how active shareholder ownership opens up another dimension of the church's evangelizing presence in the world, the opportunities in this arena are numerous.

Faith Consistent Investing

Members of faith traditions have been at the forefront of the effort to bring social and environmental questions into corporate boardrooms and corporate operations. They have been steadfast in crafting principles and screens that are both positive and negative to guide their investment and active in all manners of engagement with corporate boards, managers and other shareholders and stakeholders.

Many of today's well recognized SRI mutual funds were created by people who wanted to integrate their beliefs and their values into their investment decisions. E.g. Calvert; Pax Funds; Domini come immediately to mind.

In this evolving process, institutional faith based investors have been busy researching and mining both the core belief statements of their traditions, the various social principles that are part of those traditions and the body of research which has emerged to guide them in this initiative. The journey from a principled commitment to practical implementation has been and remains a challenging and evolving process.

In the Catholic tradition many investors started their work by looking at the scriptures and the tradition of the church for guidance. They also searched Catholic Social Teaching (CST) and the lived experience of their own mission and charism for insights. They were also challenged by both the growing internationalization of their own institutions and the questions which a more diverse membership brought to their investment committees and general chapters.

Translating principles into actionable measurable steps that money managers and the investment community could implement proved a bigger hurdle than developing the principles. The effort to integrate faith principles into the investment policies and strategies that had primarily emerged from a traditional investment philosophy was a learning process for both sides but one that has made significant progress over the past 35 years.

Among the initial steps in this process was direct action and engagement with the management of corporations through the exercise of shareholder rights. The objectives were clear, particularly about the corporation's presence and activities in specific countries, like

apartheid South Africa. Representatives of catholic institutional investors made use of the legal and regulatory tools that were available to them as shareholders to access the proxy and the annual meetings of corporations to present specific resolutions for consideration by shareholders.

The intervening 35 years have witnessed the emergence of a number of different steps along the process of shareholder engagement with corporations. In the beginning the filing of resolutions for inclusion in the proxy and for presentation at the annual meeting could most accurately be described as hostile and confrontational. At some point along the way, with a few corporations, the tone changed and there was a breakthrough in the modes of engagement. In many instances this has grown into a constructive process of engagement. This may have come from something as simple as better dynamics between the proponents or the personal experience or beliefs of the CEO or the levels of support which were emerging from the vote count on resolutions.

The Interfaith Center for Corporate Responsibility has been a leader at the heart of this process for the past 35 years. ICCR's membership is an association of 275 faith-based institutional investors, including national denominations, religious communities, pension funds, endowments, hospital corporations, economic development funds, asset management companies, colleges, unions, and publishing companies. ICCR and its members press companies to be socially and environmentally responsible. Each year ICCR-member religious institutional investors sponsor over 200 shareholder resolutions on major social and environmental issues. The combined portfolio value of ICCR's member organizations is estimated to be \$110 billion.

In its early years the work of ICCR members was focused primarily on US corporations and their multinational presence. In recent decades that effort has grown to a network that has viable presence in Australia, Canada, South Korea, Hong Kong and a number of European countries. This growing network of SRI institutional investors from the faith communities along with their colleagues in the SRI community has been successful in including a larger number of global corporations in their SRI process. Catholic religious orders and societies of men and women from many different religious families have been an important part of this effort.

Corporate Codes

One of the first things that shareholders started to ask during the process of engagement with management was for criteria, principles or codes that the company used in making any number of decisions about their business. These ranged from criteria for lending to developing countries, policies about equal opportunity, worker safety and protection. Corporations always understood the need for a number of internal policies particularly around intellectual property, product safety and testing, government engagement, antitrust compliance etc. These were carefully articulated, approved and presented to employees.

The development of an external code of conduct that was publicly available in the annual report and on the company's website is a much more recent phenomenon. A number of different forces have combined to influence this process and indeed contribute to the elements that define many of these codes. It was one thing to state very clearly that the company seeks to be in compliance with all local laws and regulations especially when it comes to worker safety, wages

and benefits and pollution. It is quite another when a companies code is measured against the core labour standards of the International Labour Organization or CST principles on human dignity and human rights and compliance was independently verifiable.

Corporations in this process were also challenged to translate their culture into policies and principles that both their employees understood and that offered assurance to the general public that there was a consistent message between their public persona and their internal practices. On the one hand it was easy to assume that those who were there at the company's founding and those who worked alongside the principal founders understood the culture and the driving force which they sought to instil into their business. As companies grew, diversified their businesses and spread out to achieve a global presence and as the early pioneers moved on or retired, it became more and more important to be able to articulate and communicate core principles and values which formed the culture of the corporation.

It was not unusual at all to hear corporate representatives, for instance, assure shareholders and others that their way of doing business was unique and founded on a set of standards that had withstood the test of time. Developing a process to communicate and to train new employees effectively about these policies and standards became an important goal. In many instances representatives of catholic institutional investors, many of whom were formed in a charism that valued deeply education and formation, brought to the table many years of active experience in education at all levels. They became insightful critics and a wellspring of creative ideas and suggestions for corporations who were challenged by the need to hand on their corporate culture, traditions and values to new employees and provide appropriate opportunities for continuing formation for all their employees.

It was one thing to be able to bring this level of formation and training to their own employees but an additional challenge emerged when many corporate business models began to operate out of a supply chain, vendor process which saw a proliferation of different entities that were, in some way, contributing to the products and services of an individual corporation. Additionally many of these contributors were from different regions of the world; their employees spoke a different language and came from different ethnic and cultural backgrounds.

Commitment to Stakeholder Engagement

A core commitment of any company that is committed to being a good company must include a process for stakeholder engagement. The following groups of stakeholders have emerged through this engagement process; shareholders, suppliers, competitors, employees, local communities, consumers and the environment. Each category of stakeholder brings a specific perspective and interest to the table but the focus of my concern is the unique contribution which faith based shareholders are playing in this arena.

From the beginning of most enterprises one could safely assume that the founders wanted to make money and make a positive contribution to the communities in which they operated. Now, however, when we consider the complex nature of modern global corporations we realize that most corporations are engaged in numerous local communities. Thus the commitment to stakeholder engagement, which may have been assumed at the founding of many corporations, has been stretched and deepened in many directions. www.socialfunds.com

In many instances, as we mentioned above, if the original core commitment established a pattern of stakeholder engagement then that commitment has served as a guiding paradigm for the corporation. Clearly, however, the circle of stakeholders and our understanding of their relationship and investment in and with corporations have evolved significantly. The core commitment of any company that is committed to being a good company must include a process that embraces a broad range of stakeholder.

Acknowledging the benefits that are achieved through this engagement has increased in recent years though it has often been a difficult and slow learning process for many in the corporate world who have been primarily schooled in the “core curriculum” of the traditional business school. A combined process whereby stakeholders can identify and raise their concerns along with the enlightened outreach of some corporate leaders has led to some important new developments in this arena.

Catholic Institutional Investors

The Catholic tradition through its moral teaching and the treasure of CST has provided catholic institutional investors with a great resource for the development of faith consistent investment principles. This process has benefited from the research of scholars in the theology, ethics, business and legal disciplines. It has also included a lively discussion between investors and the professionals from the financial community who manage their investments and advise them in the management of their resources.

Catholic institutional faith based investors who strive to be faithful to the insights of their tradition can bring the benefits of that tradition to any company that is open to serious engagement around the social and environmental challenges that they face. In addition the rich teaching on human dignity, human rights and responsibilities provides a helpful framework for companies interested in developing and implementing codes of conduct.

Finally the tremendous global network of relationships and communication which these same institutional investors bring to the table can be helpful to those who are interested in proactively addressing issues through a process of multi stakeholder engagement.

Case Studies

Freeport: For over ten years catholic institutional investors and other faith based institutional investors have been engaging Freeport McMoran Copper and Gold Inc about their operations in Indonesia. Concerns and questions about this operation were raised by missionaries of different traditions in the field and by the environmental community. The issue of concern primarily cantered around the impact of the Freeport operations on the communities living in the area, including health and safety, land rights, values and culture, employment opportunities etc.

Through this ongoing process of engagement with the corporation the company in 1996 created the Freeport Partnership Fund, which was to provide one percent of the revenues from the operations in Papua managed by PT Freeport Indonesia (PT-FI) for the benefit of the local communities. By the end of 2004, total contributions from this “One Percent Fund” since

inception were \$152 million. They furthermore committed in 1996 to quadruple total Papuan employment at the Grasberg mine and to double the number of Papuans in staff positions. These commitments have been exceeded.

In 1999, the Board of Directors of Freeport-McMoRan Copper & Gold Inc. (FCX) and the Board of Commissioners of PT-FI adopted a wide-ranging Social, Employment, and Human Rights Policy for all operations, with particular emphasis on its Indonesian operations. In 2004, these Boards adopted an enhanced version of the policy. The policy recognizes that protection of human rights begins with the cessation of violence against individuals and groups, but also extends to economic and social development and the opportunity for people to lead healthy and productive lives.

Fulfilling these commitments relating to social employment and human rights matters involves significant challenges. For that reason, FCX and PT-FI have established a number of initiatives to enable achievement of its commitments and to ensure that the results of these initiatives are measurable. In 1999, FCX named Judge Gabrielle Kirk McDonald, former President of the International Criminal Tribunal for the former Yugoslavia and former U.S. federal judge and civil rights attorney, as Special Counsel for Human Rights to the Office of the Chairman. Judge McDonald has had a strong influence on the implementation of the FCX and PT-FI human rights programs, and she has championed the social and developmental rights of women in the PT-FI operations area.

Also in 2000, FCX agreed to be a participant in the U.S. State Department/British Foreign Office Voluntary Principles for Security and Human Rights. The Voluntary Principles establish standards for extractive companies working in developing countries with regard to providing for necessary security within an operating framework that ensures respect for human rights.

The company has contracted with the International Center for Corporate Accountability www.ICCA-corporateaccountability.org to complete an audit of how they have followed through on their existing commitments and to make recommendations on ways that they can improve compliance.

Project K: Supply chain code of conduct compliance in a global economy continues to present significant challenges to corporations. In a global economy, with a business model that sources products and services from all parts of the world and with suppliers and vendor relationships numbering in the tens of thousands for many corporations this can be enormous challenge.

For the past four years a group of faith based and SRI institutional investors have been engaged in a project with McDonald's and Disney to explore the viability of a new model of sustained compliance. The overall goal of the project is to develop a replicable approach to promoting sustained compliance with supplier codes of conduct. The hoped for outcomes of this project are to improve the quality of life for the workers; diminish the need for multiple, ongoing monitoring and compliance at the factory level by each corporation that is supplying from the factory and diminish the risk exposure for the parent corporations who have pledged specific commitments through their codes of conduct.

The final results of this project are not yet available but will hopefully be ready by the end of the year. Through a process which has included the creation of a common code by the brands involved; participation by suppliers, factory owners and workers; extensive training and auditing as well as on site visits by the project team and a broad range of stakeholder engagement, this project shows great promise. It has so far involved ten factories in the Pearl River Delta area of China. This region as you probably know is home to thousands of factories and suppliers for global corporations.

At this stage the working group has ventured the following observations about what it has learned from experience and participant feedback:

- Participating suppliers and factory managers prefer DSC (Dynamic Social Compliance) to the traditional compliance approach. They embrace the idea of taking charge of the compliance process and perceive advantages to their business. They especially like knowing exactly what compliance means and how to measure it.
- Active participation by a wide range of stakeholders adds critical values to compliance efforts.
- Voluntary factory participation requires concerted efforts to build trust. One needs to be purposeful and direct. Factories, understandably, are initially concerned that transparency will lead to negative consequences.
- Learning a new way of thinking about compliance and translating it into functioning internal systems takes considerable time. One must be patient.
- All participants in the system need training to be able to effectively participate.

Conclusions

Faith based and especially catholic institutional investors have and continue to bring unique contributions to the building of “The Good Company”. Among those are:

- ✓ the insights and principles of CST,
- ✓ belief that shareholder value is maximized in the long term through a sustained commitment to stakeholder engagement,
- ✓ their extensive network that extends though their experience and relationships throughout the world,
- ✓ the grounding of their principles in the core beliefs of Catholic social teachings and their respective traditions,
- ✓ their extensive experience in pastoral work including education and health care, with people from diverse ethnic, religious and cultural groups,
- ✓ their long term commitment to building institutions and investing in corporations that strive to make a positive contribution to the common good without seriously damaging the environment.

