ST JOHN'S COLLEGE

ETHICAL INVESTMENT WORKING GROUP

Report to Governing Body

I. OVERVIEW

Governing Body set up a Working Group in Michaelmas Term 2019 to consider the ethical issues facing the College, specifically on investments but also on wider issues, taking into account the legal obligations incumbent on the College's Trustees.

The Terms of Reference and Membership of the Group, to be chaired by the President, were as follows:

- To consider the principles of College investment in relation to its stated charitable objectives.
- To consider the legal context and the fiduciary responsibilities of Trustees, seeking advice when appropriate.
- To consider the principles of ESG and review the range of approaches adopted by comparator institutions.
- To recommend a framework for the College to be reviewed and subsequently adopted in relation to ESG investing.

Membership of the Working Group was to be open to any member of Governing Body who presented themselves and the JCR and MCR were each invited to nominate a student representative.

The Group was asked to report to Governing Body in Trinity Term 2020.

The Group met five times (two meetings were virtual). In its deliberations, the Working Group considered a wide range of issues and heard from guest speakers on a variety of topics. These included an overview of the College's endowment and financial activities, criteria and approaches for considering ethical investment decisions, comparison of endowments and ESG investment policies of other Oxford colleges and the University, the Oxford Martin Principles for climate-conscious investment, and fiduciary responsibilities of trustees under UK charity law. The Working Group used tobacco as an example to work through the arguments for and against divestment from a particular sector by applying an ethical framework in which to consider the financial implications of divestment while keeping in mind the College's charitable objectives. A discussion with representatives from Shell was postponed at the firm's request.

The Group took note of a number of representations received from students, alumni, outside faculties and members of the public, supporting or arguing against divestment from fossil fuel companies, including an open letter from the SJC Fossil Free Campaign.

II. CONSIDERATIONS

a) <u>College endowment</u>

The Group received a summary of the College's financial activities, the portfolio split between property and equity investments, its investment approach working on a total returns basis, and the extent to which the College relies on its endowment to support ongoing operating activities. Only about a quarter of core activities are covered by public funding; the draw on the endowment was £18m in the financial year 2018/19.

The environmental, social and governance (ESG) policies and principles of the College's main financial advisers were noted:

- Cazenove, part of Schroders, manages the College main equity portfolio. It is a diversified portfolio in terms of sectors and regions, including some allocation in fossil fuel and tobacco companies. It was noted that Schroder/Cazenove scores consistently high in ESG rankings and is a member of the UN's PRI (Principles of Responsible Investment), Climate Action 100+ and signatory to the Global Investor Statements to governments on climate change.
- Edgewood advises the College on its US investments. While they do not formally apply ESG principles, their investment process filters out certain companies, e.g. tobacco, alcohol, gambling, weapons manufacturers.
- LGT is a global equity manager based in Switzerland that focuses on emerging markets in Asia/Pacific. LGT have taken an early lead on ESG in their sector and one of their managing partners is on the board of PRI.

The Working Group considered that in managing its investments, the College was operating under three imperatives that may not necessarily always pull in the same direction:

(i) UK charity law and the responsibility of trustees to maximise returns for the charity, and the extent to which investment decisions have to be justifiable in terms of the College's charitable objectives.
(ii) Requirement to fund the College's core activities in the present and also in perpetuity by prudently managing its assets to benefit future generations.
(iii) Increasing expectations from internal and external stakeholders within a societal framework to include ethical and moral considerations in investment decision-making.

While the Group believed ongoing funding needs and ESG considerations were the main tensions, all three forces will need to be considered.

b) <u>Ethics</u>

A Professor of Philosophy and a Professor Political Theory were invited to discuss with the Group the concept of an ethical framework for investing. From an ethical perspective, the guiding principle is that actions should not lead to severe harm, and the avoidance of foreseeable and severe harm should operate as a constraint on investment decisions.

Rightness and wrongness of actions are therefore determined by the goodness and badness of their consequences and whether our actions make or do not make a difference. This implies that our thinking should apply moral reasoning and principles to balance the rightness and wrongness of a decision when determining what counts as severe harm. Various arguments were considered in the College's context. These included consideration of a 'snowballing effect' such that other institutions are likely to follow any ethical stance set by a leading college. In contrast, engagement with certain companies was unlikely to lead to a positive, indirect, snowballing effect. Thus, the severe harm principle would not support engagement from an ethical point of view. Opinions on engagement were split within the Group, but there was a consensus that engagement was a viable option in some asset classes.

c) Research on industry bodies, especially in other higher education institutions

A comparison including 26 Oxford colleges and OUEM showed that actual practices and policies adopted to date varied significantly: 13 colleges followed OUEM policy; 7 colleges focused on engagement and their policies described how they or their managers engaged with companies about ESG issues; and 2 colleges held at least modest investments in 'positive change' funds. Where a college followed the OUEM approach, this would exclude tobacco, manufacturers of weapons illegal under UK law and companies whose main business is the extraction of thermal coal and oil sands. Two colleges intended to reduce or eliminate holdings in fossil fuels. Five colleges did not have explicit policies on ESG investments but most were considering the issue at the time of writing this report.

d) Oxford Martin School Principles for climate-conscious investment

The Group heard from a representative of the Oxford Martin School about their principles for climate-conscious investment, which were designed to provide a framework for engagement between investors and companies:

(i) Commitment to net-zero emissions, including all emissions associated with a business; companies should be required to develop and publish a net-zero transition plan. Companies' public statements and support for other organisations should be consistent with advancing public, political and corporate action towards net zero emissions.
(ii) Profitable net-zero business model: what is a company's strategy to achieve a net-zero business model that limits risks once emissions reach net-zero while still being profitable? For companies that provide a carbon-intensive service or fuel for which there is no currently available substitute, a clear plan is required.
(iii) What are a company's quantitative medium-term targets and how will they monitor that they are on track to achieve net-zero?

These principles were discussed in view of the upcoming Congregation motion[1] to divest from the fossil fuel industry (which has since been passed). The view was shared that while the motion provides a commitment to engage better with firms and the principles on which to

[1] http://www.ox.ac.uk/news-and-events/fossil-fuel-divestment

engage, it lacks a mechanism and resources to evaluate a company's net-zero plans and track progress against those plans. Therefore, a coordinated effort by Oxford colleges to fund a research post would be welcomed, ensuring that Oxford University owns the process of developing metrics and methodologies for evaluation, monitoring and reporting on companies' progress, thus informing long-term investment decisions. If a company made clear progress along the way, a decision to invest or stay invested would become clearer. However, if a company still did not have a credible transition plan to net-zero in a few years' time, disinvestment may be a justifiable option.

The Working Group commended the Oxford Martin Principles for climate-conscious investment as a framework to consider engagement, including the option to disinvest, and expressed its support for the creation of a dedicated research post.

The Group further recommended signing the Global Investor Statement on Climate Change[2]. While acknowledging that doing so was, in part, a political statement and would not prevent the College from supporting other initiatives that may go further, the Working Group felt that adding the College's name to the statement would give a clear indication of how seriously the College took these issues to a wide audience.

e) <u>Charity Law</u>

The Working Group heard from a partner at Winckworth Sherwood LLP about UK charity law on investments, fiduciary responsibilities of trustees when taking investment decisions, and to what degree trustees can and cannot take investment decisions based on moral or ethical considerations. The detailed guidance on when ethical investment is allowed is set out in *Charity and investment matters: a guide for trustees*[3]. In terms of case law, the core principles of the Bishop of Oxford case from 1992 still apply. This case recognised three situations in which trustees can allow their investment strategy to be governed by considerations other than the level of investment return. First, there are cases where investment in a particular type of business would conflict with the aims of the charity. Secondly, a charity can avoid investments that might hamper its work, for example by alienating supporters. Thirdly, trustees can accommodate the views of those who consider an investment to be inappropriate on moral grounds, provided they are satisfied that this would not involve '*a risk of significant financial detriment*'.

The Charity Commission is currently consulting on responsible investment and how charities approach investing in line with their aims; further guidance from the Commission is expected next year. It was noted that the consultation does not seem to address how to deal with tensions arising from investment activities the public might find unethical but that are not in direct contradiction to a charity's objectives. The lawyer explained that a charity would not

[2] https://globalinvestorcoalition.org/global-investor-statement-climate-change/
"Full support for the Paris Agreement and urge all governments to implement the actions that are needed to achieve the goals of the Agreement."

[3] https://www.gov.uk/government/publications/charities-and-investment-matters-a-guide-for-trustees-cc14

be expected to adopt public opinion *per se* in its investment decision but may consider consulting with stakeholders. This could help to understand whether certain investment policies would lead to serious reputational risk causing, for example, donors to withdraw their financial support to the College. However, even in such a case the College would still need to evaluate the overall financial impact of an investment decision rather than relying on the reputational risk argument.

Trustees have specific investment duties, namely to achieve the best financial returns and to select investments that are right for the charity by considering their suitability and diversification. Suitability includes considerations of asset allocation, stock selection, risk and, for charities with permanent endowments such as St John's, a balance between the interests of present and future beneficiaries. In all of their investment decisions or changes to policies, trustees are expected to take professional advice on the financial impact.

The College's Statutes provide relatively wide investment powers and few restrictions. However, this does not give Governing Body, as the collective decision-making body, completely free rein. Investments have to reflect the charity's aims and objectives, in the College's case being a *perpetual College of learning sciences, sacred theology, philosophy and good arts*.

The lawyer suggested that the perpetuity requirement in the College's charitable aims of being a *perpetual College of learning …* may justify longer-term sustainability and environmental matters as an investment objective. In addition, a more explicit statement on investment policies, in particular in relation to ESG investing, could be included in the College's annual report. The Group believed that the College's aims of fostering excellence in research need to be taken into account as well.

f) <u>Divestment case study</u>

Having considered the role of the College's charitable objectives in its decision-making as a reflection of our values, the Finance Bursar prepared a framework for applying ethical criteria to guide investment decisions from a legal perspective (see Appendix 1).

Having regard to these principles and taking account what these criteria might look like in the College's context, operating under UK charity law, the Group agreed to consider the College's investments in tobacco as a worked example to consider whether particular investments were in tension with the charitable goals of the College or pose unjustifiable reputational risk.

The case study included a survey to test whether the example covered the type of questions trustees should be considering when making ESG investments and could therefore serve as a template to discuss other asset classes in future. It was also designed to trial ways of soliciting views on particular investment classes, whilst recognising that the Working Group has no decision-making powers.

III. CONCLUSIONS

Having reviewed ESG principles and approaches adopted by comparator institutions, it is clear that many organisations are actively reviewing their investment policies or have amended them recently to explicitly address environmental, social and governance matters. Those which have made changes to their investment policies have chosen different options, including policies focusing on engagement, investing in positive change funds, or applying exclusions and restrictions to certain asset classes.

In line with this, Governing Body, on the recommendation of the Working Group has agreed to:

(i) Sign the Global Investor Statement on Climate Change.
(ii) Commend the Oxford Martin Principles for climate-conscious investment as a framework to consider engagement
(iii) Support the creation of a dedicated research post at Oxford to develop methodology and metrics to track and measure companies' net-zero plans.

The Working Group recognises that trustees must exercise their fiduciary duties in the best interests of the charity and that investment decisions have to be justifiable in terms of the College's charitable objectives. The College's charitable aim as a perpetual institution of learning and research sets the parameters for investment activities. Trustees are required to assess the financial impact of investment decisions and take financial advice before deciding on policy changes.

Discussions on ethical investments might usefully continue into the new academic year. It is hoped that a direct discussion with Shell can be arranged, in particular to test the Oxford Martin Principles for climate-conscious investment with Shell. There is also interest in further case studies following the tobacco example to test the approach in other asset classes, in particular arms and fossil fuels.

The newly constituted Investment Advisory Group should also be consulted and participate in those discussions. It could be considered to consult alumni that have offered support.

The Working Group further suggests establishing a process by which trustees can raise ESG investments matters to Governing Body and propose a review of a particular asset class. Such requests should be considered at defined points in the academic year and, once a particular asset class has been considered and decided upon, there would not be a repeat review within an agreed period of time.

IV. RECOMMENDATIONS

The Working Group recommends to Governing Body:

1. Use the framework in Appendix 1 as a way of considering the ethical aspects of investment decision-making and to illustrate how and why the College is making certain decisions.

2. Consider the survey questions used in the case study as a tool to scope views on particular asset classes.

3. Consider adapting a governance process to raise ESG investment issues at Governing Body.

The Group further proposes that Governing Body, through its Finance and Investment Committees:

(a) Consider if any investment classes currently held are in tension with the charitable objectives of the College or pose unjustifiable reputational risks in addition to assessing their financial return.
(b) Review investment policy statements in the College's annual accounts and consider providing more details on specific ESG aims and objectives.

Ethical Investment Working Group
16 June 2020

Appendix 1

A framework for conclusions on ethical issues in investment

1) Some activities will be so clearly at odds with our direct charitable purposes that it is not felt possible to hold investments in these areas regardless of financial impact or the potential for engagement with the relevant companies.

2) Some activities will have more complicated ethical arguments for and against or will present genuine ethical concerns despite the activity not being directly opposed to our specific charitable purposes. In considering these areas we may find that:
   a) some activities cause genuine and clear-cut ethical concerns despite not being directly opposed to our specific charitable purposes;
   b) some activities raise serious ethical issues but there are genuine and reasonably held ethical views both for and against them and a single ethical stance does not arise as a consequence of the College's charitable purposes;
   c) some activities raise ethical issues but there is no consensus about whether the activity is a problem or about how serious those issues are. A single ethical stance does not arise as a consequence of the College's charitable purposes;
   d) the nature of some types of business is such that activities causing ethical concerns sit alongside activities in which the College would want to invest and it would not be practical to detangle them for purposes of investment;
   e) some activities cause ethical concerns but these concerns are felt to be minor in the scale of other issues under consideration;
   f) some activities raise ethical issues but these issues are pervasive throughout the market generally and not restricted to a particular sector.

3) When considering a response to those activities which fall under 2 we may decide:
   a) the reputational damage or negative views of our stakeholders about particular activities are so great that we should choose not to hold particular investments;
   b) the general moral case is so clear-cut and the potential financial impact so slight that we should choose not to hold particular investments;
   c) the particular issue is such that more can be achieved through engagement of our managers with the companies they hold and we should instruct that such engagement take place;
   d) the particular issue is too widespread or an activity forms too great a part of the market for the college not to hold investments in the area, although managers may still be instructed to engage with companies we hold in the sector;
   e) no stance should be adopted by the College because no single ethical stance arises as a consequence of the College's charitable purposes and reasonable people hold differing views;
   f) no stance should be adopted by the College because the particular issue is not major enough to form a core part of the College's investment strategy.