INTRODUCTION

Abstract

The modern privately endowed university participates in two worlds simultaneously: academia and social/institutional reality. We examine one of the areas of their overlap by considering the investment of university endowments in terms of social and environmental responsibility. An ethical review demonstrates the need for universities to maintain a buffer between the two worlds; while it necessarily does act politically in the outside world and thus has ethical responsibilities to itself and the community, the university must also protect its academic sphere from the undue influence of a biased institutional structure. There are three general modes of internally consistent action a university can take in the ethical treatment of its investments: maximizing fiscal return only, participating to change corporate behavior or using ethics as a criterion for purchase and sale decisions. We study these modes ethically, fiscally and institutionally, developing from them a series of principles for responsible, academically neutral investment for universities as a whole. We conclude with a set of recommendations for Williams College: a revised investment responsibility committee with a new mission and greater activity.

Statement of Need

Apartheid is over. For this reason, there has been some quieting of the shareholder voice in the last five years. Indeed, one member of the Williams College Advisory Committee for Shareholder Responsibility (ACSR)[1] asked at a 1994 meeting, "What do we take on now?" With the issue that overwhelmingly dominated, and in most cases defined, shareholder activism in the 1980s and early 1990s gone, what role should shareholders now play in influencing the behavior of firms?

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[1]The authors were the two student members of the ACSR from September, 1994-June 1996. We were elected directly by the student body.

Introduction

Private colleges and universities, endowed institutions dedicated to higher education and research, have many concerns arguably more central to their missions than the social and environmental implications of their investing. Indeed, the fiscal performance of these moneys in the market place is fundamentally important to the operation of the school; yet even this performance is not the central purpose or usually even a theme of the school as an educational institution. Why should the school be interested in the effects of its money when it is simply trying to maximize this money to do its best job educating? Further, why should we be interested in examining this very narrow overlap of higher education and socially responsible investment?

The answers to these questions and the reasons that the authors have taken on the research and analysis of this narrow issue are complex and ultimately answerable only in the analysis itself. We have been driven to perform this analysis by our perceptions that the ACSR, functionally just a proxy-voting committee at this time, is not living up to the potential and responsibilities of its members and the Williams Community at large. Members of the Committee frequently note the defeat we feels when turning down resolutions that have good intent but are poorly structured or worded. This frustration is indicative of the need that the authors perceive for re-enlivening and re-authenticating the responsible investment movement so institutions are capable of investing ethically. Further, the authors value, in general, the type of concerns pressed by investment activists and hope that we can develop a mechanism that Williams, an institution which we also highly value, can use to engage these concerns. There are a number of historical and thematic issues that are identifiable and useful in understanding the goals and approach of the research.

Incorporation serves as a means to consolidate capital and limit liability so as to produce goods that the public wants. The resultant distancing of ownership from management is not complete functionally (shareholders elect the managers of the firm) and certainly not ethically. While a shareholder cannot be held responsible for his or her company’s every action, the shareholder's purposeful profits[2] from corporate action do to some extent make him or her ethically accountable. The investor freely chooses to invest in or divest from a firm with the potential for knowledge of that firm's behavior; the buying of and profiting from a stock implicitly condones the actions of a firm.

With this in mind, over the last 25 years investors have insisted on taking a larger and larger role in corporate management, especially when the corporation makes choices with significant social impact.[3] While this has been most evident in the push to force firms to divest from South Africa, its roots can be found in domestic issues such as equal opportunity and corporate-government relations. The first shareholder-initiated social resolutions that were forced onto a firm's annual proxy (that is, the first successful use of the now standard technique) were concerned with corporate "public policy," requesting an internal review committee and public disclosure.[4]

Universities[5], typically progressive institutions and major investors, have played a large role in the introduction and ongoing development of responsible investment. Campaign GM targeted universities specifically in the first shareholder initiated resolutions[6]; since, universities have been active voters and the subjects for research on how proxy votes are determined.[7] Further, universities tend to have strong ties to their communities (local town, peer institutions, etc.) and are highly respected members within them. As such, universities are expected to play

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[2]A non-profitable or money losing company and its owners are not excused from behaving ethically. However, for ease of argument, we will not discuss this case here.

[3]In this paper, we use "social" very broadly (as the word suggests), to include issues such as community structure, income distribution, environmental quality, etc. We use it to indicate where corporate behavior has reasonably direct effects outside of the market which may benefit or harm individuals with or without direct connection to the firm.

[4]The Project on Corporate Responsibility's Campaign GM forced General Motors (by the Securities and Exchange Commission and judicial rulings) to include resolutions in both 1970 and 1971. David Vogel, *Lobbying the Corporation*, 1978, pp. 71, 81.

[5]To avoid bulky language, we use "universities" to refer to colleges and universities in general and "the College" to refer to Williams College specifically.

[6]Vogel, p. 78.

[7]For example, Edward H. Bowman, *University Investing and Corporate Responsibility*, MIT, 1971 and John G. Simon, Charles W. Powers and Jon P. Gunnemann, *The Ethical Investor; universities and corporate responsibility*, Yale University Press, 1972.

an active role in community improvement and to behave ethically. Because of their place in their communities, universities are in fact a very interesting and important subject for responsible investment analysis.

As students and thus the primary benefactors of university investments, the authors feel there are several additional needs for analyzing university investments. Since at a school such as Williams a significant portion of operating costs is drawn from investments, the students have a vested interest in the endowment. Further, as the greatest beneficiaries, they are ethically bound to their universities' investments: while students do not own the stocks, they do bear the ethical burden associated with the profit. While it might be suggested that students, consumers of education, are separated from the investments by the university institution and Trustees, this is not so. This point is especially so in a case such as Williams, where the Residential College system attempts to educate the student through all interactions with the institution and not just those that take place in the classroom. Thus, students have a double interest in understanding the responsibility of university investments.

We stated above that there had already been significant research on responsible investing in universities; why another study? The previous studies were performed before or during the South Africa- and apartheid-domination of corporate responsibility. Now that apartheid, and the homogeneous condemnation it generated, is a relic of history, we have both a broader perspective and more challenging questions to ask. Further, as corporations grow in individual and total size, becoming transnational entities sometimes much more powerful than governments, they have greater and greater social influence. As evidenced by the massive media and entertainment conglomerates, the market is inseparable from the social and cultural lives of modern Americans. The relationships of corporations to society must thus be under constant scrutiny and question, and this exploration of responsible investment is one small part of a necessary massive endeavor.

Statement of Purpose

We seek to explore the ethical implications of socially responsible investment in private, endowed universities[8] and develop ethically motivated strategies for approaching responsible investment that are also financially sound. Our primary criteria are acceptance of ethical burdens *as each institution interprets them* and actions consistent with such acceptance. This necessitates a tri-level ethical analysis: identifying the issues that are important to the intersection of education and investment, explore the problems created by this intersection, and isolating internally consistent paths that could be taken. From these analyses we propose a set of general mechanistic modes schools can enter and move among to invest responsibly. We consider real world examples of these modes and then make recommendations for universities at large and Williams in particular. Our goal is to provide background and an approach, and perhaps even a framework, for schools to use to identify a means for bringing their investments within their ethical standards. A university's responsibility policies must grow from their own ethical standards or they will be ineffective and ultimately unethical. We share our opinions about what path Williams should take, based on our interpretations of the Williams ethics, so as to initiate an active discussion on this and other campuses.

[8]The ethics of funding for public schools, with its more obvious social and political implications, is an equally interesting question. Regrettably, we do not have space to address them here.

ETHICAL ANALYSIS

University Neutrality

Carl Cohen, Professor of Philosophy at the University of Michigan, argues that universities must remain neutral in most issues of concern to the public because

> Learning and teaching is our mission, the advancement of understanding and the accumulation of new knowledge our principal goals. We are not above our country, or our community, but we serve them best by providing that very precious setting in which every rational opinion, every argument, theory, or proposal may be advocated and criticized, defended or debunked without fear by scholars whose primary obligation is to the truth as they understand it.[9]

He is describing the need for university neutrality as the moral and practical obligation of universities as institutions to remain politically neutral in their academic pursuits. Neutrality is indeed of utmost importance: the university exists as a home for and facilitator of free thought, mental risk taking and criticism by peers. The individual institution (e.g., Williams College) must strive to distance its academics from the political reality of the outside world and the institution itself so to grant the thinkers within the institution's academic sphere the freedoms and safeguards needed to explore all ideas fully. Yet, absolute university neutrality is, of course, unattainable; the creation of an institution to protect academia (a university) necessarily establishes a political player--since the university exists in the real world, it cannot escape real world interactions. The challenge is for the university to balance the separation of the academic from the rest of its actions (institutional development and interactions with the outside world) with the participatory role the institution must take in creating the academic sphere.[10]

Cohen goes on to promote a specific and problematic vision of *University Neutrality* (from here on Cohen's specific recommendations for trying to attain university neutrality are

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[9]Carl Cohen, "Political Controversy and the University," in Ellen Berek, ed., *Williams Reports*, pp. 33, 29.
[10]The university institution is not simply the moat between the "real world" and the Ivory Tower. Rather, the university is the girders supporting and framing the Tower, giving it structure but (attempting) to only minimally interfere with the movement of ideas within.

referred to as *University Neutrality*) characterized by having the university take no political stand on any public issue that does not have an immediate connection to the educational role of the university itself. Cohen and many other academics, including such notables as Derek Bok, then President of Harvard, promoted *University Neutrality* as reason for not assuming responsible investment policies during the early 1980s. In all cases, these academics emphasized that universities must avoid making unnecessary political choices; only in cases where the university would be directly influenced should the institution itself take a public position.

Proponents of policies of *University Neutrality* use exceptions and limitations to try to avoid these failures noted above. Among these exceptions is for political activity when it is central to the mission of the university, presumably allowing the university to participate in and take public positions in discussions of academic freedom and other issues of public concern. One must then ask what defines an activity as central to the university's mission? It is unclear what exceptions would be allowed under the above policy. While guidelines could be established, the restricting of any academic discipline is inflexible, at least somewhat arbitrary and necessarily problematic.

What none of these authors completely accounted for, however, is the inevitable political impact, in one way or another, of all decisions. Even in cases where no overt political position is claimed, political action can and is made. Ignoring the political consequences of a decision by either not discussing it or by failing to be aware of them[11] does not eliminate them. Further, and more importantly now than ever before, institutional decisions are becoming more and more transparent. Students and university neighbors insist on explanations for actions, thus forcing the university to expose the processes for making decisions and the decisions themselves as part of the public record.[12] If positions are public, and each of these positions has political

[11]This suggests that protecting neutrality must be an active process; a static institutional mechanism will not be able to defend the academic sphere. The risks to neutrality must be defused, not simply shielded against or ignored. The academic can be separated from the political only if through recognition of the political: you cannot dodge something that you cannot see.

[12]The causes of this increased transparency are multiple and complex. Most directly, the constituents of universities, their faculties and student bodies, along with other stakeholders (such as neighbors, funding agencies, government agencies, etc.) are demanding transparency from the schools. These demands not

implications, there is risk of damage to university neutrality, if the school is not structured in such a way as to separate "outside" institutional actions from "inside" academic actions. The accountability (institutional and personal) demanded by students and other critics narrows the possibilities of maintaining public neutrality -- all the decisions that a school makes will eventually be seen to be, in fact, informed by values. Even if a university were to be successful in avoiding taking a public stand on issues, the school's actions would still have influenced the internal structure of the university, meaning that a successful *University Neutrality* policy is not necessarily a move towards university neutrality. Consider the schools at which there is research supported by the Department of Defense or the CIA which is deemed to be secret by national security policy. By agreeing to not submit scientific research to open peer review (because it is secret), the university circumvents the open discourse which is part of mainstream academics. While the university may not publicly announce that it thinks that the research has been successful, by submitting to the restrictions on discussion, it is limiting the review process which operates to select high quality research over poor research. Thus, the academic sphere is compromised because there is no academically recognized means for judging the quality of the research.

If fact, not only is *University Neutrality* ineffective in approximating neutrality, but the highly analytical, communicative and skeptical world of the modern university, <u>absolute neutrality is unattainable</u>. While it may be held as a goal, it cannot be reached in any absolute terms as long as the university is to remain functional and responsive to a rapidly changing world. As long as there are students and faculty criticizing ideas, including ideas to which the

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only indicate a renewed public and stakeholder interest in how society spends so much of its resources in educating itself but also suggest that the public realizes the tremendous power of its schools. Universities collect from public and private coffers billions of dollars and then spend them, generating the vital but intangible product education. The public is right to be concerned with how these moneys are raised and spent, and certainly should question any claim that universities (which survive through donations) behave neutrally.

This transparency movement is not limited to universities; there is also a public call for greater accountability for corporate behavior. This call is not unrelated to the need the authors feel for universities to invest responsibly: as beneficiaries of Corporate America, universities should play an active role in determining its behavior.

university adheres, the institution in which ideas are criticized will be under the constant scrutiny of that very criticism. This criticism will force the institution to explain its decisions, and these explanations will thus be public. Pretending to maintain neutrality by a policy of *University Neutrality* is deceptive and will become more and more difficult as transparency is increasingly demanded.

Specifically because of the risks to academic integrity associated with the failure to maintain a reasonable level of neutrality, universities must continue to strive towards it. Universities must not invite political polarization within the academic sphere of the institution or of the institution as a whole; to do so puts the school's academic capabilities and public standing at risk. It also invites political action from without, making the university not only a political actor but also a target.

These risks are real for investment, the particular case we are studying. Consider the example of a university which decides to divest from firms which are associated with performing abortions (e.g., insurance companies which pay for them, companies that make the equipment). Depending on the way in which the choice was made[13], to some extent faculty will feel restricted in their ability to fully discuss the abortion debate with their students as part of the academic process (i.e., while operating within the academic sphere). Importantly, the decision to divest would probably not be independent of other choices by the institution: a public statement against abortion, a refusal to offer insurance which pays for abortions, etc. In reality, these other factors would likely have more of a direct effect upon faculty's willingness to touch the abortion debate in class because they are closer to daily behavior and real-life concerns. However, the investment decision is an important marker (which may precede these other actions): and this is why it may stifle discussion. If a faculty member fears that discussion of abortion is disliked by the university institution, s/he may avoid it (an entirely non-neutral action) in fear of future reprisals such as during tenure a decision.

[13] This dependency is a complicated issue which is taken up at length later.

In addition to the internal effects on the academic process, a divestment from abortion-promoting firms (or other public action) could invite external actions against the university. Academically, scholars at other institutions might, because of the risk of internal effects, hesitate to consider the analyses of abortion by faculty at the said university. The divestment from abortion-associated firms would mark the institution as biased and preclude it from being funded to perform studies on the effects of abortion. Further, the university's actions could make it the target of political actions from the outside (e.g., abortion-associated firms may cut research projects they had funded at the school).

The common image of the university as an Ivory Tower, a place separated from society and its ills, has its merits. The university as an institution is somewhat separated from the rest of society for good reason: to allow the unimpeded flow of ideas without the encumbrances of political and economic risk to the intellectuals among whom the ideas flow. Without separation from these risks, there is no telling how functional the university will be; certainly creative, risk-taking processes would be impeded. There are any number of specific reasons that a tendency towards neutrality must be defended on internal institutional and external creditability grounds.

Internal neutrality is necessary for the very reason it was delineated: to allow an environment which fosters the free flow and criticism of ideas, without the hindrances of political pressures promoting some ideas over others. The university is the only environment in the modern world that strives to hold knowledge and understanding above all else; it is only without the prejudice of political intent that "truths" (whatever they may be) can emerge accurately. Specifically, academic decisions, about everything from the requirements for a major to the hiring of new faculty, must turn primarily on academic grounds, and minimally on the non-academic values of the institution.[14]

There also exist significant risks for the university's relationship to the others, both other parts of academia and the greater world as a whole, if it fails to defend neutrality. Universities

[14] Defining an institution's values is a challenging problem, certainly without a discrete solution. While we do address it to some extent in our section on mechanisms, we cannot do it full justice in this paper.

and their members rely on the opinion of their peer institutions and their members for their validation as academic institutions and experts; without this validation (e.g., accreditation, publication of articles in peer-reviewed journals), universities cannot claim to educate and professors cannot claim to be expert. The politicization of a university potentially puts this validation at risk: who would trust an article on evolutionary biology written by a researcher at a school that claimed Creationism was the only truth? Derek Bok recognized that the public, politicized move of "[divestment] tends to undermine the willingness of outside groups to respect the academic independence of the University."[15] Further, the special privileges universities receive from society at large are not small; with the collapse of neutrality, a university will lose its status as an academic institution and thus will lose its special privileges. Most notable among these is, in the United States at least, the tax-exemption universities are granted (others include discounts for the purchase of scientific and other equipment). While there are certain politicized institutions which are also tax-exempt, universities are granted their exemption on academic grounds. When a university is no longer be respected as an institution of higher learning, but rather a politically motivated actor, it loses its previously granted privileges. The perception of the academic community and general public (rather than the reality of the political activity of a university) is fundamental to the ability of that university to fulfill its educational goals.

In all, a university's internal ability to function as an academically rigorous institution searching out knowledge and understanding depends on the institution maintaining a politically neutral framework. The university's public identity and functionality as an institution of higher learning are largely dependent on the perception of the university as neutral. Thus, it appears that as the academic sphere of a university loses its university neutrality, the university cannot function as such, it will not be successful in unbiased, high quality research and teaching.

This dependence on university neutrality is made challenging when considering that

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[15]Derek Bok, "Reflections on Divestment of Stock: An Open Letter to the Harvard Community," in Ellen Berek, ed., *Williams Reports*, p. 26.

> ...the doctrine of [university] neutrality suffers from the worst disability which can afflict a norm: what it prescribes is not wrong; it is impossible. A large university in contemporary America simply cannot adopt a value-neutral stance, either externally or internally, no matter how hard it tries.[16]

University Neutrality supposes that by not publicly addressing contentious issues, the institution can remain value neutral. Wolff demonstrates, however, that institutional structure itself, not just the public acknowledgment of values, is political and polarizing. The institutional commitment to free debate, a core value for universities, is in itself a political act: a university Chaplain's office which gives equal voice to Catholicism and Hinduism is implicitly denying the doctrine of single truth of Catholicism.[17] More to the central theme of this paper, consider that a university's simple maintenance of an endowment is a political act, implicitly promoting capitalism and the firms in which the university is a partial owner. Might this not be stifling to a Marxist economist? Do students of economic theory receive their academic due if the entire institution through which they learn is supported by a single economic system?[18]

Thus, approaching university neutrality is vitally important to the academic pursuits of universities, but also very difficult because the institution of a university which protects the (neutral) academic sphere is in itself inevitably a political body. There is a fundamental need for universities to design institutions or policies to actively defend academic neutrality.

The proponents of *University Neutrality* suggest one primary means for balancing the need for an unbiased environment for academic pursuits and the participation of universities in

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[16]Robert P. Wolff, *The Ideal of the University*, p. 70. Wolff's use of "neutrality" can be taken in either sense that it is used here. Because of the demand for transparency, universities cannot speak in value-neutral (*University Neutrality*) terms. Further, the institutional body of a university likewise cannot be apolitical; so it cannot have university neutrality.

[17]Wolff, p. 73.

[18]Harvey Carter (Visiting Part-Time Lecturer, Center for Environmental Studies, Williams College), personal communication, 4 Oct., 1995. As was pointed out by Kai Lee (Professor of Environmental Studies, Williams College), Marxists do have a long history at universities. We believe that the presence of Marxists at universities is a function of the careful structuring of universities so as to preserve neutrality; schools have been successful in the past in separating this obvious aspect of academics from institutional structure.

the real world. They suggest that universities not take public stands on potentially contentious issues. We have pointed out that 1) all "real world" issues are potentially contentious in the academic world, and 2) the lack of public statement does not effectively result in an unbiased academic environment. Further, we showed that not only is neutrality itself but also the perception of a university as apolitical is necessary for it to be able to serve its primary purposes of education and research. Therefore, *University Neutrality* cannot produce university neutrality. Thus, in the following section on Mechanisms we present a variety of techniques which suggest institutional means for protecting and defending academic neutrality while recognizing and working within the political reality of being a public institution with goals (to research and educate), needs (financing said goals) and a politically charged membership (students, professors and alumni) and set of donors, including taxpayer-supported agencies. Instead of having universities attempt to do the impossible of avoiding political positions and actions, we propose techniques for distancing the political acts of responsible investment from the academic sphere within the university institution. We recognize that absolute separation is impossible (indeed, that is why this paper is necessary!); instead we present options for minimizing the coerciveness of their interaction. We find that these steps are especially necessary in the realm of investments because of the pervasive (but incorrect) inference that profit maximization is a neutral policy.

The challenge is to develop mechanisms which allow the university to make politically weighty decisions while defining and defending the neutral space for the scholarly activities of the institution. The university must strive to protect the internal flow of ideas while not ignoring the fact that, as a prominent member of several communities, it has significant political influence, whether or not it wants it.

Investment as Necessarily Political

While colleges and universities must strive to remain politically neutral in order to preserve their academic integrity, we hold that the pursuit of neutrality must not prevent institutions of higher education from grappling with the ethical questions that accompany investment. The failure to address ethical questions is fails to achieve neutrality because endowment management is an inherently political activity. When undertaken by institutions that have, and exercise, political will, political activity has ethical ramifications. We begin the following section with an examination of the political nature of investing. We go on to show that this sort of political activity is not foreign to institutions of higher education; rather, we argue that politically charged goals and assumptions are inherent in the very nature of a college. We conclude that both the necessity and the precedent exist for colleges and universities to seriously engage the ethical questions that arise from their investments.

Investing is an inherently political act

Shareholders in corporations are to some degree responsible for the activities of the firms in which they invest. Simple logic underpins this statement. Firms are political creatures, and shareholders can affect the behavior of firms. If firms exert power in the political arena, and if shareholders have some power over the behavior of firms, then it follows that shareholders are political actors.

Our analysis begins with the notion that corporations play a central role in the workings of society. This is implicit in the prominence of the firm in capitalist economies. Firms supply nearly all the goods and services we consume. Their decision making generates the supply side of the supply and demand equilibrium that market economies rely on to set prices and allocate scarce resources. Corporations also hold the reins to many of the political, cultural, and economic forces that determine the outcome of major social problems.

The exact nature of the interface between corporations and the rest of society is complex and very difficult to fully document, but for the sake of our analysis we can divide it into four categories. Our purpose here is not to catalogue every interaction between the firm and society, but rather to establish that firms wield substantial power in the social and political arenas. While most of the examples we present illustrate how firms have the potential to harm society, we certainly acknowledge that the vast majority of corporate activity promotes social welfare.

The most direct links between firms and social welfare are the goods and services provided by firms. Corporations make available and in some cases aggressively market socially harmful products. These harmful products are often created for particularly vulnerable groups of consumers. The anecdotal evidence for this is compelling. Ammunition manufacturers develop and market low cost hollow tipped “cop killer” bullets. Beer distillers target poor urban neighborhoods in advertising campaigns for high alcohol malt liquor. Tobacco companies come up with advertisements geared to encourage junior highschoolers to smoke.[19]

A less direct but related set of interactions between firms and society stem from the externalities generated by commercial activity. An externality is any cost or benefit of commerce that accrues to someone other than those directly involved in the transaction.[20] In the case of negative externalities, firms shift some of the costs of an activity or transaction from themselves to society. Negative externalities take the form of pollution, extinction of species, and the perpetuation of violence -- particularly against women-- by certain types of media.

Hiring and employee relations policies of corporations profoundly affects the welfare of entire segments of society. Well documented glass ceilings keep women and minorities from achieving top management positions. Banks refuse to hire janitors that belong to unions. Corporations possess tremendous amounts of power over the lives of their employees, and they often exercise this power in ways that harm employees and those who might otherwise be employees .

Finally, firms lobby, contribute to political campaigns, fund political action committees, and directly participate in the political process. They bring with them clear vested interests which form strong incentives to seek policy outcomes which may be in conflict with the social good. An extensive literature documents the impacts of corporate participation in the democratic process. One recent book articulates it thus: “to discover who rules, follow the gold (i.e. trace

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[19]P.L. Moses and J. Krausz, *Corporate Responsibility and Financial Performance*, p. ?.
[20]R.H. Frank, *Microeconomics and Behavior*, p.?.

the origins and the financing of the campaign)." [21] It is no wonder that Supreme Court Justice Louis Brandeis characterized the corporation as the "master instrument of civilized life."[22]

An important question for the discussion at hand is what parameters constrict the ability of firms to exercise what we categorize as political power? Do managers choose what effects firms will have on society? On one hand, firms can be seen as rational decision makers seeking only to maximize profit. In the rational choice model the freedom of the firm is constrained by a prime directive; only that course of action which promises to maximize profits will be selected. Even a cursory look how firms behave reveals, however, that other factors come into play. Tradition, altruism, error, and egotism can all affect what firms do. Furthermore, firms rarely encounter a situation where a clear and predictable course of action will maximize profits. Instead, the behavior of firms is determined by an interaction of forces that include the preferences of managers, the imperfections of the market, and, central to our analysis, the actions of investors.

Stockholders, as part owners of corporations, have the power to affect what corporations do in the political arena. The details and evidence supporting this assertion will be fully analyzed when we investigate the various strategies endowment managers can take to achieve socially responsible investing. Here we will offer only a brief sketch of the power investors exert over corporations. We emphasize that, as one of many factors influencing the behavior of firms, the power of shareholders is limited. The limits of shareholder power are implied by the fact that shareholders cannot be held liable for corporate wrongdoing under the laws of this and other states.[23]

Shareholders can impact how firms act in two ways. First, they can limit the amount of capital companies have at their disposal by declining to invest in socially harmful firms. Second, investors assert their will by communicating with management, either directly

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[21]T. Ferguson, *Golden Rule: The Investment Theory of Party Competition and the Logic of Money Driven Political Systems* , p. ?.
[22]Quoted in J.G. Simon, C.W. Powers and J.P. Gunnemann, *The Ethical Investor*, New Haven, Yale University Press, 1972.
[23]Stan Parese (member of Williams College ACSR), personal communication, 30 October, 1995.

(management will often listen out of fear of a more drastic strategy), or by proposing and voting shareholder resolutions. The effects of proxy voting may be greater than they initially appear. Managers are legally required to conform to the will of the majority of shareholders. In addition, some corporate officers contend that whenever a shareholder proposal gets more than 2 per cent of the vote it receives serious consideration.[24] No matter which approach the investor chooses, the outcome will be the same: shareholders are on some level morally accountable for the behavior of the firms in which they invest.

This relationship places an ethical burden on the investor. If one accepts the preceding argument, the stockholder is on some level responsible for the actions of any firms in which s/he has an ownership interest. Failure to acknowledge and act on this responsibility constitutes a strong moral vote in favor of the notion that the only acceptable investment criteria is income maximization. Seeking only to maximize returns therefore amounts to an ethical choice and does not absolve the shareholder from moral responsibility for the actions of the firm. Instead, ignoring firm's behavior amounts to an endorsement of the activities of that firm.

The fact that stockholders receive a portion of the income earned by a firm (the dividend paid by a stock) increases the burden of responsibility borne by the investor. The dividend paid by a stock is a partial share of the benefits earned in the course of corporate activity. The fact that an investor gives his/her money in exchange for the right to share in the benefits of the activity implies an implicit if not always acknowledged approval of that activity. If I own shares in a tobacco company, then some of my income is coming directly from the sale of tobacco. Ownership of the investment is tantamount to approving of the sale of tobacco. Through their investments, colleges and universities have a financial stake in perpetuating the consumption of tobacco, and in the success of anti-environmental legislation currently before congress. It is this sort of reasoning that likely moved John Chandler, writing as president of Williams College, to

[24] Simon, *et al*., p.?.

assert that "As an investor Williams is in some measure responsible for the behavior of the companies in which it invests."[25]

Similar ethical considerations arise from holding bonds and participating in venture capital and leveraged buy out investments. Purchasing a bond is one way of lending capital to a corporation. The implications of this are twofold. First, the college is acquiring a financial interest in the success of the borrower. Second, by providing them with access to capital, the college is helping corporations achieve their business goals. The same two points are implied by investments in venture capital, with the added twist of ownership; when the college participates in the venture capital market, it acquire partial ownership of firms. The fact that no established channels of communication exist between investors in bonds and venture capital funds and the firms they support weakens the explicit link between the college and its holdings. But that does not absolve the college of responsibility implied by the fact that it has a direct financial stake in the success of the firm, regardless of whether they have positive or negative social impacts.

Investing is an inherently political act, and investors are political actors. How then are we to reconcile the profound need of colleges to avoid the political with their status as investors? To fully understand the nature of this question, we need to delve into the political nature of higher education.

Institutions have political will

In this section we strive to show that institutions of higher learning are, on some level, inherently political, and therefore cannot use neutrality as an excuse to ignore the ethical problems created by investing. The political nature of the academy is implicit in its very mission. Why does a college exist? To educate is the obvious response. Why educate? To improve the minds of young men and women, and thereby improve society, or, in the words of

[25] John Chandler, "Williams as a Responsible Investor: The Fundamental Questions," in *Williams Reports.* Ellen Berek, ed., 1983.

former Williams president John Chandler, to "promote the unambiguous social good of education."[26] The improvement of society through education is no less political than the improvement of society through socially responsible investing.

An uncritical application of the notion of neutrality might preclude entire academic programs, departments, and schools on the grounds that they represent views which could only be considered normative.[27] The Center for Environmental Studies at Williams College is predicated on the idea that the relationship between the environment and society is of enduring importance; law schools across the nation rest on strong assumptions about the value of the rule of the law. Thus we see that the idea of university neutrality begins to break down as soon as it is removed from the context of the community of scholars and placed into the vastly complex context of the real world.

Universities exercise political action

The notion of a college making decisions based on values is nothing new; it is a tacit confirmation of the idea of neutrality has problematically fuzzy edges. This logic is articulated by Derek Bok, the former president of Harvard University, who writes in an open letter to the Harvard community regarding socially responsible investment that

> "In carrying on its academic activities, Harvard is constantly responding to ethical considerations and social concerns. We devote thousands of hours to encouraging student recruitment and employment practices that will provide opportunities for people who have traditionally been overlooked or disadvantaged. We expend enormous effort in raising and distributing funds to give every deserving student a chance to acquire a Harvard education regardless of financial means."

Investments are simply a nominally more distant part of the college which deserves the same political consideration afforded to financial aide, hiring, or procurement.

Conclusions

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[26] *ibid*.
[27] Simon, *et al*., p.?.

University neutrality, while a valid and necessary goal, is unattainable for universities because of they way they define themselves. Approximating neutrality is vital to the fulfillment of the educational mission of the college, yet that very mission is charged with political and moral values and judgments. This appears paradoxical only if we think of neutrality as an axiom that cannot be violated. If instead we understand neutrality to be an ideal that guides and shapes, we can escape the paradox by devising mechanisms to approach neutrality. The college exists in a political world. In the course of the college's affairs, it is inevitable that it will interact with morally charged situations. In these situations, the college must not hide behind a veil of inappropriate idealism. Instead, the college must strive to deal with the situation in a manner consistent with the values it espouses. The application of ethical criteria to the endowment does not necessarily undermine the free discourse within the community of scholars that neutrality strives to protect.

A university's endowment is as central to the fulfillment of its educational goals as the physical infrastructure or the faculty. It is different only in that it extends beyond the borders of the campus and into a politically volatile world that has Wall Street and Washington DC as its foci. Irving Kristol emphasizes this distinction: "No University is merely a 'community of scholars.' In order for such a community to exist and survive, it needs to be buttressed by an organizational component, by an administration which manages money and real estate and employees and relations with the world outside."[28] In order for universities to fulfill in good faith its contract with society, it must conduct these affairs in an ethical manner.

Responsible to Whom?

We have shown that universities have political will and that they exercise this will every time they purchase a share of stock. Further, just because they are universities and the home of free thought, they cannot ignore their political will; they are morally obliged to consider and act on the ethical implications of their investments. However, having and exercising political will

[28] Quoted in Simon, *et al.*, p. ?.

does not begin to describe what type of responsible investment policy is appropriate for a university. Indeed, a number of other questions must be asked before the structure of such a policy can be set out. Primary among these questions (in that it is of great moral import) is: to whom is the university responsible in its responsible investment policy? While one could list any number of potential stakeholders (its Trustees, its students, society, etc.), we find that these fall into two basic categories of ethical intent. A university can invest responsibly for its own sake or it can do so to affect social good. We recognize two very different sets of ethical influences and implications and potentially two very different investment policies.

<u>Investing to satisfy institutional values</u>

It can be shown through example that universities have and act on values other than doing educational good. Some of these institutional values are frequently (if not usually) difficult to define and certainly subject to change. These aspects are likely a function of recent institutional membership, a significant portion comprised of opinionated and impressionable students with high turnover. Yet, the institution's values are not all, or even mostly, transient and a function of recent membership, for the institution's very structure is an acting out of its values. An institution makes a decision in a certain way because it has determined (through its evolving membership) that decisions should be made that way. It values the decision-making process (this can be for any number of reasons: because the process if efficient, it gives the "right" answer, it was valued by past members, etc.).

We turn to Williams for examples of these university-held values. Our challenge is to point to policies or procedures that are both beyond the primary educational goals of the school (such that the College's affirmative action program *in the name of creating a capable faculty* does not demonstrate a non-educational value of improving the economic condition of historically repressed peoples) and beyond legal requirements (such that the College's insistence that students in laboratories wear safety goggles is not a demonstration of valuing student health, since federal law mandates goggles). This is not an easy task, because the College, as an institution, finds it easiest to justify decisions not by its values but rather on the grounds of the educational mission or legal requirements. These justifications are irrefutable from within and without since they speak to the primary purpose of the institution and the social framework within which it operates (although, one could argue that obeying the law is in itself a value-laden decision). We present two examples here, one relating the College to the larger world through its affirmative action policy and one bringing the discussion back to responsible investment.

Williams' affirmative action programs are justified in terms other than just legal requirements. In a 1972 report from the Williams College Committee on Equal Opportunity on the position of women in the Williams faculty, the authors concluded:

> Williams College -- as a liberal institution committed to the standards of social justice -- should associate itself with the broad developing movement in behalf of women's rights, by demonstrating its full respect for the ability and achievement of academic women.[29]

This statement is heavily value-laden ("liberal institution committed to the standards of social justice") and indicates action based on those values ("should associate itself with the broad developing movement in behalf of women's rights"). The statement is not limited to the promotion of women for the sake of creating a better faculty, but rather states that the College should take action because it values social justice. Further, the statement is unambiguous and in a document available to the public, so that the College has precedent for identifying, enunciating and acting upon its values in its relationship to the world at large.

Likewise, the College has demonstrated, through a series of public statements starting in the late 1970s and continuing through the 1980s and 1990s, that it is dedicated to a very restricted, but nonetheless definitive, policy of responsible investment. Specifically, the Trustees state the College's values as they relate to the behavior of firms in which the College invests as follows:

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[29]Paul G. Clark and Stephen W. Botein, *Women on the Williams Faculty: Report for the Committee on Equal Opportunity*, p. 2.

> . . . the College through its Trustees has a right to expect companies in which it owns shares to follow business policies and practices in their foreign and domestic operations that are *broadly consistent with the moral and social ideals of American society*.[30]

In 1986 the Trustees go further and indicate clear actions which the College is to take based on these values:

> . . . Williams must now extend further the logic of the shareholder activism it has pursued for the past eight years and shift its stance to one of disinvestment advocacy. That is to say, it will now begin to use its prerogatives as a shareholder to urge the companies whose stock it holds to withdraw from South Africa.[31]

We have now shown that the College does have values and that it has, in the past, acted upon them. We suspect that this is the case for all universities and will assume so for ease of analysis. The next step then is determining if and how a university should apply these values to its investments. Deontological morality[32] suggests that an ethical university has the duty to follow a policy of responsible investment, “responsible” being defined solely by the university’s own values. That is, the ultimate effect of the school’s behavior on the social good does not matter; rather, it is the fulfillment of the institution’s self-defined values that matters. The ethics of value-fulfillment are attractively self-contained; that is, decisions depend solely on the institution and its members, not on the potential impact of those decisions on the rest of the world. There is no broader purposefulness in this act (other than fulfilling values), so the real-world effects of potential options do not alter decisions.

To act morally, the school must consider its non-financial values when investing, no matter what those values are. That the investments are removed from the campus and university

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[30]“Trustee’s Statement on Divestment,” January 24, 1981. In Ellen Berek, ed., *Williams Reports*, 1983, p. 6. Emphasis added.
[31]“Memorandum to ACSR instituting disinvestment advocacy (From the Finance Committee [of the Board of Trustees]),” September 18, 1986. In Ellen Berek, ed., *Williams Reports: South Africa*, 1986, p. 8.
[32]Whereby each individual has a duty to his or her own code of ethics. Reinterpretation of personal communication with Steve Gerrard (Assistant Professor of Philosophy, Williams College), 26 October 1995.

community does not excuse them from the morals of the university. The school's duty is to apply its own values to all of its doings, not just those within its immediate educational environment.

Before leaving the discussion of investing within the institution's values, it is necessary to consider the difficulty of defining an institution's values. The ease of self-containment in deontological thought is counterbalanced by the difficulty of defining what the values of an institution are. An institution does not have a conscious, ethical mind of its own and thus cannot make its own decisions, ethical or otherwise. Acting through its members, the institution makes choices according to its structure and the interpretations of the members-of-the-moment. The question is then, can an institution use the same mechanisms for defining its values and making acknowledgedly ethical decisions as it does for choosing what color to paint dorm rooms?

Above we concluded that institutions have values and that some of them are incorporated into their very structures and decision-making processes. Necessarily then, an institution's values are as mutable as its decision-making processes. These processes do change, usually through periodic, long-term internal reviews; by extension, the low mutability of decision-making processes indicates that institutional values are also relatively slow to change and are subject to their own internal review. To develop an explicit list of values for a university would be a challenging task; while some would come easily (e.g., academic freedom) others would surely be disputed by the bulk of institutional members. Since universities include among their members diverse students, faculty and alumni (from potentially contrary ethical camps and eras), consensus would be unreachable. While consensus can be difficult to reach for daily decisions also, the case of ethics is more extreme because it is taken more to heart by the membership and because it has a greater long term effect upon the institution itself.

Ultimately, a decision to take on a value-fulfillment responsible investment policy (an ethical, and thus challenging, decision itself) has the potential to stall the university's investments in the ethics stage. In addition to the fact that widely divergent personal values of members will spill into the process of defining institutional values, the final output itself could be limiting of action. If the university defines its values significantly differently from those of popular American business culture, then fulfillment of those values through the investment process will be next to impossible. While the market is beginning to provide a larger variety of choice in business ethics, the vast bulk of the investment marketplace is dominated by the simple profit motive. The need for a diversified portfolio with a stable core will make the fulfillment of non-traditional values a challenge.

<u>Investing to have social/environmental impact</u>

A university may take on a more utilitarian view in reasoning the need for a responsible investment policy. An argument that a university should follow a responsible investment policy so to affect social good (or at least avoid social harm) is, in some sense at least, a somewhat simple case. In the previous instance it was necessary to establish that universities have values to be able to apply the deontological logic that they should act upon those values in their investment decisions. In this case we suggest that universities should establish responsible investment policies not for the satisfaction of internal qualms, but rather to better society. If we assume away or otherwise resolve the nebulous nature of "social good," the dilemma is relatively straight forward: what is more valuable (to the university, to society), the social good of education or the social good responsible investment? By focusing on (external) social good, rather than (internal) university values, the university is free of the internal debate for establishing what is responsible internally. Below we address the doing of social good and that, especially for an institution like a university, social good is ultimately indefinable. We resolve this dilemma by stepping back from "doing good" to "avoiding harm."

Whether individuals and institutions should be concerned with doing good has been the subject of millennia of philosophical debate, the bulk of which is well beyond the scope of this analysis. For us, the most important theme of these years of discussion is that of social utilitarianism, that is, the assertion that an individual's or institution's acts should be good for society as a whole. Limiting ourselves to Rule Utilitarianism[33] for functionality's sake, we can consider that a university may seek to improve society not only through its primary educational activities but also as rule utilitarianism in its general behavior. Thus, as a participant in society, the university may choose to conduct its affairs with the general good in mind, so that its actions as a whole are beneficial. Several potential problems are apparent in this very broad picture: Who decides what is good for society? (That is, relieve the assumption we stated before.) Does the good that the university does through its educational mission outweigh its other interactions with society?

Institutions with a membership as large and diverse as universities will have a difficult enough time establishing values (such as for deontological investment); it is fairly safe to assume that such an institution would be entirely incapable of finding consensus on what is good for society at large. Further, as will be discussed later *[where will we discuss the legal issues of investment?]* in our section on the legal implications of responsible investment, it is debatable whether the institution should consider itself in the light of anything other than education. While it is disappointing to think that it is necessary to refrain from doing good, the authors realize that without moral absolutes, there is no reasonable way to define good. Without definition, one day's good could be the next's bad and thus neither creates ultimate social benefit. We thus seek to step back from our current topic of doing social good and settle for a realistic absolute, even if it is not within (an admittedly self-defined and thus non-absolute) our own definition of maximum good.

A useful and potentially common-ground point that resolves some of the above discordance by relaxing from "doing good" (impossible for a heterogeneous institution) was delineated in the 1972 Yale study *The Ethical Investor*. Simply put, an institution seeking to behave ethically must do so through negative injunctions rather than affirmative duties, primarily

[33]Such that an institution's behaviors are subject to rules that, when followed by the members of a group, lead to behavior which is socially good overall. The benefit of this is that, contrary to Act Utilitarianism, not all decisions are subject to the qualification of creating the maximum social good, so that individuals have more freedom to pursue goals tangent to social good. Reinterpretation of personal communication with Michael McPherson (Professor of Economics, Williams College), 25 October 1995.

because affirmative pro-action requires an unattainable consensus *and* potentially leads to the diversion of resources away from the primary goals of the institution.[34]

> . . . ought universities to use their financial resources to attack some of society's more difficult problems? Thus posed, the question forces one to choose between devoting resources and energy to education and devoting energy and resources to doing good in non educational ways. Faced with such a choice, the argument in favor of concentrating on education and letting others do good in other ways would be strong indeed. But this choice we are asked to make is a contrived necessity. It suggests that the only moral investment decision a university has to make concerns the amount of good it can achieve through investment action, thereby ignoring any duty it might have to avoid social harm in the pursuit of financial return.[35]

An institution that decides to invest ethically through negative injunction must still decide what harm is and thus what to avoid in investments, but it need not identify what is good or how the world should be. The negative injunction is not unlike Pareto safety in economics, the rule of allowing any choice which harms none of the parties involved. Like Pareto safety, it gives no guidance as to what is the *best* action, but it assures that the decision will make neither the university institution nor the social whole worse off.[36] One last ethical relaxation which is reasonable in this framework is to insist not on doing *no* harm, but rather on *minimizing* harm. A university would have to determine which of these is appropriate for it, considering its goals and values.

We now return to the balance between the interaction of ethical decisions with the rest of the world and the identification of institutional ethics. While in the value-fulfillment analysis performed above we found that a university's values are self-contained (having no purposeful impact) but difficult to define. In the current analysis of avoiding social harm, the converse is true. Identifying social harm to avoid is, compared to defining institutional values, relatively

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[34]John G. Simon, Charles W. Powers and Jon P. Gunnemann, *The Ethical Investor*, p. 16.
[35]Simon, *et al.*, p. 17.
[36]A change is Pareto safe if it harms no participants; there exists a set of positions (termed Pareto optimal) for which no more Pareto safe moves are possible. It is not surprising that designing Pareto safe moves is challenging if not impossible in our society (although this does not necessarily suggest that the economy exists at a Pareto optimum).

easy because the goal is to have no effect. However, measuring the fulfillment of that goal is difficult, and ultimately dependent on further refinement of investment responsibility objectives. If taking the most stringent case, to properly measure the harm caused by one's investments, one must perform empirical socioeconomic analysis on the university's portfolio and then compare this to the rest of the market (assuming the university wishes to minimize the harm that its portfolio does relative to all other firms). This is an essentially impossible task for a financially-limited school, of course (below, in the section on Mechanisms, we suggest some alternative investment objectives that present some more realistic goals for responsibility and its metering). While a reasonable substitute for this analysis could probably be made by using resources such as the Investment Responsibility Resource Center (IRRC, a non-profit research firm that compiles social and environmental performance data on publicly traded firms), a fundamental question still remains: does a university's responsible investment policy itself (as opposed to the performance of the firms in which it is partial owner) prevent any harm? The economic power of any one university is relatively small (although the social power of its public comments are arguably much more significant). Many responsible investment activities, such as proxy voting, have no directly tangible effect (social proxies, as a rule, do not pass--but there is significant evidence that they may influence corporate behavior nonetheless); without changing market structure or laws, it is arguable that any change a university forces upon firms will be met with an equal and opposite change by other firms (if the damaging behavior is still profitable, the market share will be taken up). In all, a minimum-harm policy is of questionable real-world effectiveness.

<u>Conclusions</u>

Ultimately, a university will choose under what system(s) of ethics it will make its investment decisions (as discussed above, the non-choice of ignoring the social and environmental impact of investment choices can be considered a choice for valuing educational purpose above all else within the value-fulfilling framework). There are good arguments for both of the analyses presented above and universities may choose to use some fusion of the two. Reasonable possibilities include the options of fulfilling a minimum standard under each; fulfilling this standard and then following one more carefully; following just one standard, etc. This choice will, of course, greatly effect what mechanisms will be established and the subsequent actions taken.[37] While each case will be different, some probable outcomes can be associated with the two ethic systems. Satisfying institutional values would likely lead to a policy of withdrawal, of avoiding "bad" investments. A precursor to the risk of the stalling of investment because of the unavailability of ethically acceptable firms, the fulfillment of university values indicates that the school may only buy stock in firms that meet (potentially strict) standards. Of course, an entire range of options is available to universities (only voting proxies may fulfill a schools standards); but, because standards are to be met, the easiest means to fulfill goals is to own firms which perform and not own firms that fail to meet standards.

The utilitarian ethic of doing good or minimizing harm suggests a more broadly proactive, participatory mechanism. Again, a university could choose to do no harm by simply not owning firms that are considered socially damaging. Yet, a seemingly more effective method would be to try to affect change within the corporations in which the university owns shares, so that the school would bring its economic and ethical voice to bear and push for changes that minimize harm. This is potentially more effective because the sale of such a stock would, in nearly all cases, simply mean a change in ownership, not policy (a school's economic power is not great enough so that the threat of sale of its shares would lead to a change in corporate policy). However, by submitting and voting proxies, the school could leverage its power and, speaking as a partial owner, potentially change corporate policy.

For the ultimate route that universities take in identifying an ethical framework, institutional values and actual investment policies and decisions will be as much a function of the university structure as the ethical considerations. While the above trends linking ethical

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[37]Before these actions are taken, however, the school must perform the secondary level of ethical analysis: for the value-fulfillment ethic, this means identifying institutional values. For the minimum-harm ethic, harms must be identified and possibly ranked relative to each other.

framework to investment policies will probably be visible in the aggregate level, no doubt individual universities will have policies that are complicated and personalized enough that no direct correlation can be found. Ultimately this is not necessarily important unless one is studying the causality of ethical decision making. What is important, to these authors at least, is that universities take the action and make the ethical decisions. Whether there is real social and environmental consequence (and what that consequence will be) from the increased ethical deliberation cannot be known from the ethics alone; only the educational and moral good of conscientious decision making is for sure.

Summary

We have presented two alternative but not mutually exclusive ethical frameworks in which universities may find themselves while deliberating and designing responsible investment policies. Institutional value-fulfillment allows an institution to become ethically consistent by bringing investment decisions into the same value system as the rest of the university's decision making. It burdens the school with identifying an ethic that is satisfactory to community as a whole. Alternatively, the university may find itself trying to do good with its investments as well as with its educational actions. While the school can avoid the problem of identifying common values by aiming only to do no harm, it is then stuck defining what harm is and deciding how to measure harm. Responsible investment is a complicated task, even at the most theoretical and impractical level of ethical motivation; ultimately the ethical deliberations will have profound effects on the investment decisions a university makes.

Responsible Investment Can Be Fiscally Responsible

Opponents of responsible investing by institutions of higher education argue that the financial cost of being a responsible investor will divert resources away from education. Of course, the costs of responsible investing vary with the approach taken, but in general they fall into three categories. First, any policy that limits the range of choices available to investment bankers may interfere with their ability to generate high returns.   Second, there may be substantial transaction costs associated with socially responsible endowment management. We will return to these issue when we evaluate the various options available to universities seeking to invest responsibly.

The final financial argument against socially responsible investing, and the one we seek to disprove at this point in our analysis, is that socially responsible firms will be outperformed by competitors that remain unencumbered by strict social and environmental standards. Stock in socially responsible firms may pay lower dividends and experience less appreciation.   If this is true, investors have a strong incentive to avoid risking money in such firms, and to halt any efforts to encourage social responsibility in currently owned firms. We conclude that this supposed cost is unlikely to be incurred by colleges and universities.   A university exists and invests in the extreme long run and is therefore interested in the long run performance of the corporations in which it is a shareholder.   Assuming that consumers will steer away from harmful products in the long run, it is safe to say that negative environmental and social impacts of corporations constitute a substantial risk to the long term performance of stocks.

This reasoning is at least partially confirmed by empirical evidence. Pava and Krausz, two business school professors who examined studies of the performance of socially responsible firms, write that "nearly all empirical studies to date have concluded that firms that are perceived as having met social responsibility criteria have either outperformed or performed as well as other firms that are not necessarily socially responsible."[38]   Of the 21 studies they analyze, only one demonstrated a negative correlation between performance and social responsibility. Over half of the studies, including ones conducted by Forbes Magazine and the Council on Economic Priorities, found direct positive correlation between financial performance and social responsibility.

It is important to note that Krausz and Pava attribute only part of is relationship to positive feedback for corporate responsibility. It is also due, they argue, to the fact that in

[38]Moses and Krausz, p. ?.

general only successful corporations can afford to spend money on pollution cleanups, aggressive affirmative action programs and the like. If this is the case, then social responsibility can serve as a flag alerting investors that a particular corporation is financially sound. Social responsibility in corporations may in fact be a positive criterion for endowment advisors.

RESPONSIBILITY MECHANISMS

Introduction

When a university comes to the decision that it wishes to invest responsibly, it must identify those values by which it frames responsibility and it must develop a responsible investment mechanism, a process by which it can make its investments meet the value criteria established. These two acts may not and probably will not be separate; indeed there are values embedded in the choice of mechanism. In this section we explore the ethical and financial implications of the three general modes of mechanisms that we identify as potentially internally consistent. We feel that a school's chosen mechanism will fall into one or among these three modes: Minimal methods by which a school chooses to ignore responsibility or address it only tangentially; Participatory ACSR methods by which a school seeks to change the behavior of corporations in which they own shares; and Screening methods by which a school only buys shares in firms that meet responsibility criteria. By generalizing an infinite number of possible investment mechanisms into three modes, we can look at each type in enough depth to consider its general character, benefits and problems.

We have identified ten criteria, not all of which are universally applicable, to analyze and compare these modes. The ten break down (although not entirely clearly) into three main categories: costs, university institutional matters and ethical matters. *Transaction Costs* measure the cost of implementation and operation of the program: the costs of information, increased brokerage fees, time of staff, faculty and students. *Opportunity Costs* measure the income forgone by having a limited set of options for purchases. We also include here any costs from decreased financial performance caused by programs implemented in response to shareholder activism.

Turnover Time is the amount of time it will take to implement changes in the portfolio, espoused by the responsibility policy. *Market Time-Frame* measures the time frame for firms to their behavior. *Application to Portfolio* measures what part(s) of the endowment (stocks, venture capital, leveraged buy-outs, etc.) will be affected by the policy. *Information Availability* is a measure of what information will be necessary for implementation of a policy (and how accessible it is). *Institutional Decision Making* questions what sort of choices the school will need to make (and who will make them) and what type of processes will be needed to accomplish a particular mechanism. The *Legal Implications* of each mechanism must be considered: will the Trustees be able to maintain fiduciary responsibility and will the non-profit and tax-exempt status of a university be put at risk?

Ethical Implications measure what degree of responsibility is the university implicitly acknowledging by using a specific policy. *Effect on Neutrality* questions if and how this policy will alter the academic environment and if there are means by which any stifling of academic freedom can be minimized. *Behavioral Impact* asks how effective this mechanism will be in influencing the behavior of firms and the market in general.

Minimal Ethical Risk Methods

Fiscal Maximization Mode

The least costly way to deal with the ethical issues raised by investing is to ignore them, and to seek only to maximize profits. This implies buying and selling securities without regard to ethical concerns, and voting proxies with management.[39] In the Ethics Section we argued that this approach (a form of *University Neutrality*) is just as active an ethical position as any other, and therefore raises the same issues within the academy.

Transaction costs and opportunity costs. By definition, pure financial maximization would cost nothing. This mechanism is unique among the four we analyze in that there is no chance that it could lead to any reduction in earnings, assuming that the portfolio managers were completely rational decision makers seeking to maximize profits in the long term. In addition,

[39]The second part is true in almost all cases, but it is possible that a shareholder resolution could make a firm more profitable. An example of this could be shareholder resolution to limit the salaries paid management.

unlike the other three approaches we examine, financial maximization does not require costly information and analysis on the part of the ACSR.

Turnover Time, Market Time-Frame, Application to Portfolio, Information Availability. The issues of time, applicability and information are not relevant, since there are no changes being made to the portfolio or within firms for reasons other than financial advantage.[40]

Institutional Decision Making. In light of the ethical implications of the decision maximize profit without regard corporate responsibility, we hold that a policy of ignoring issues of corporate responsibility should be adopted only after the same sort of process appropriate for any of our ensuing mechanisms. However, up until the late 1960's, this model of investing was the default approach taken by most, if not all, universities.

Legal Implications. This mechanism does not risk violating the fiduciary duties of the Trustees.

Ethical Implications. Once the issue of ethical investing has been raised, as it has been at most privately endowed schools, the decision to completely omit any ethical considerations from the management of the portfolio amounts to an ethically charged act. Specifically, failure to act is a reflection of one or more of three ethical positions; we see three possible lines of reasoning that would lead a college or university to adopt this mechanism.

The first position follows from the notion that institutions of higher education are in no way accountable for the behavior of the firms they partially own. This is the default position, taken by investors that have not grappled with the ethical dimensions of investing. The second position is generated by a cost benefit analysis that concludes that the (financial or academic) cost of acting in accord with ethical principles exceeds the (moral) cost of inaction. Finally, a college or university may come to the decision that the behavior of the companies in its portfolio is ethically acceptable, and that there is no need for closer scrutiny, much less any sort

[40]Decisions made solely on financial grounds (e.g., those made by the investment advisors) are not being considered here.

of action. Any one of these stances is just as much a manifestation of value-based decision making as is deciding to divest from a firm or industry on ethical grounds.

Effect on Neutrality. To the extent that financial maximization is informed by an ethical position, it has the same effect of distancing the college from the ideal of neutrality as any of the four mechanisms we identify. Financial maximization does, however, differ from the ensuing mechanisms in two important respects, both of which tend to suggest that it is the least threatening to university neutrality.

First, after the initial decision to avoid socially responsible investing is made, it is not necessary to continue making politically charged choices. This contrasts with the other approaches, which require the university to continually make judgments about the ethics of individual companies. Second, the policy of financial maximization has historically been chosen not through a careful process, but rather by default, or the very lack of any process at all. Under these circumstances, it poses no explicit threat to the ideal of neutrality because no active ethical decisions are being made. However, the purchase of securities is still an act with ethical consequences, even if they are not recognized.

impacts on the behavior of firms

Impact on the Behavior of Firms. This mechanism will have no effect on the behavior of firms, other than to perpetuate pre-existing behaviors and policies.

<u>Proxy Only Mode</u>

All publicly owned companies are on some level subject to shareholder control. Shareholders vote to decide a wide array of questions about the management of a firm, ranging from how managers will be chosen and compensated to the company policy towards the environment. Voting occurs at annual shareholder meetings; shareholders that cannot attend can vote by proxy. Many issues on the ballot have no explicit social or environmental weight, but some, particularly resolutions proposed by the shareholders themselves, target specific practices and policies of the firm that the framers of the resolution consider morally problematic. Colleges and universities have established committees similar to Williams' ACSR to advise Trustees on how to vote shareholder resolutions that have ethical dimensions.

Transaction Cots. There are minor costs associated with maintaining the structure necessary to vote proxies. At Williams, these costs amount to less than $6,000 per annum which pay for a subscription to the Social Issues Service offered by the IRRC and incidentals.[41] No shares are traded, so there are no commissions.

Opportunity Costs. If a university were to vote for a successful shareholder resolution that either depressed the value of the stock or decreased the amount of dividend paid by the stock, it is possible that some cost would be borne by the university. In light of the fact that shareholder resolutions almost never pass, the chances of this happening are minimal.

Turnover Time. The portfolio does not change under this mechanism, so the issue of turnover time is not relevant.

Market Time Frame. Shareholder resolutions are voted annually during the annual meeting of a firm. Proxies are mailed out several weeks or months before this meeting so that votes can be tabulated beforehand. Because resolutions do not pass, there is no fixed time frame for changes; in the past, positive responses to resolutions have occurred nearly immediately after the annual meeting or years later.[42] There is not means to judge the time for firm to respond to a resolution (or if the will respond at all).

Application to Portfolio. A major shortcoming of this approach to ethical investing is that it offer investors the ability to influence only the companies in which voting stock is owned. At Williams, this accounts for less than 60% of the portfolio; the rest is in venture capital and bonds, which remain out of the reach of this mechanism.

Information Availability. To wisely exercise its power as a shareholder, educational investors should have access to information about the practices of the firm in question, and information about the feasibility and appropriateness of the shareholder proposal. The

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[41]Douglas Phillips (Associate Treasurer, Williams College), personal communication, 9 November 1995.
[42]Vogel, p.71.

information provided to Williams' ACSR by the IRRC is of high quality, but addresses broad issues (e.g. the labor and environmental practices of US businesses in Mexico). It is not specific enough to guide the ACSR on individual proxies. The ACSR bases most of their decisions on information provided in the text of the resolution itself.

Institutional Decision Making. Colleges and universities that seek to vote proxies can either set a policy that will determine how all proxies will be voted ahead of time, or they can set up a committee charged with evaluating each proxies and voting according to their best judgment. The latter approach is taken by Williams and other private schools. Members are elected from the student body, and appointed by the president of the college from among the faculty, alumni, and administration. The ACSR does not actually vote the shares, but rather advises the Board of Trustees on how to vote.

Legal Implications. Voting proxies on ethical grounds presents no legal risk, for three reasons. First, voting on issues surrounding the operation of a company is an expected and necessary part of being a stockholder. Furthermore, voting proxies is unlikely to violate the Trustee's Prudent Man Rule because shareholder resolutions do not threaten the value of stock nor the flow of dividends. Finally, a long precedent exists for this sort of activity, both at Williams and at other schools.

Ethical Implications. The decision to exercise the power to vote social proxies signals the acceptance of a degree of responsibility by colleges and universities. Proxies allow investors to have a small influence on the behavior of firms, and then only after another shareholder has begun the process. Investors that only vote proxies are, therefore, able only to react, and make no proactive moves. As a result, the chances that they will have any direct effect on the behavior of firms is very small. Thus, voting proxies is a small, but meaningful, step in the direction of socially responsible investing.

Effect on Neutrality. Voting proxies is clearly political and therefore challenges university neutrality. Because of the normal absence of direct ramifications of voting (e.g., shareholder resolutions never pass), and the fact that voting proxies is considered standard action for stockholders, these effects are likely to be small. In addition, effects can be mitigated by separating the decision makers from the academic sphere of the college. We will detail how this can be done at Williams in the recommendations section of this paper.

Behavioral Impact. To legally force a firm to change policy, a shareholder resolution must receive a majority vote. This rarely occurs, and almost never happens in cases where shareholder resolutions are trying to change firms for ethical reasons. Shareholder resolutions that receive more than a 2% positive vote tend to receive serious consideration from managers, however. For example, three months after a resolution urging General Motors to form a "Committee for Corporate Responsibility" received a 3% yes vote, GM voluntarily formed a "Public Policy" subcommittee, and appointed Leon Sullivan, an advocate of racial equality, to its board of directors.[43] While it is clear that voting proxies is unlikely to force a change in corporate policy, even a small yes vote can and has inspired corporate action on a specific issue.

Participatory Mode

A university may choose to take a proactive, participatory role in determining the social effects of its investments. We call this the Participatory mode, inspired by the Williams College ACSR's broad mandate from the Trustees and past events. The ACSR's history begins to open up the possibility of a Committee that has significant communication with the management of firms, one that could propose shareholder resolutions, one that could involve the campus as a whole in its decision-making process. Thus, the participatory quality is both of the Committee (the mediator of the Participatory mode) with firms and the university community with the Committee. This Participatory mode, like the other modes, is very broad in scope and includes a wide variety of mechanisms that individual schools could undertake. Here we enumerate some of these in the process of exploring the mode in general. The Committee could write letters to firms requesting information on practices that have been questioned in the media. If the letters raised important issues, members of the Committee could conference call with management to

[43]Vogel, p.?.

discuss the firm's related policies. If these policies were deemed to be insufficient, the Committee and management could meet in person to discuss alternatives. If management is not responsive, then the Committee could draft and submit a resolution to have the firm initiate a more responsible policy. These actions would obviously take place over a significant time span and would be subject to debate among the general university community. The procedural operations of the Committee would vary from school to school; we make specific recommendations speaking to this below.

The Participatory mode is administered by a committee drawn from the university community. Because it is charged with both advising the Trustees on social responsibility matters and also taking an active role in directly communicating with and making proposals to firms, its membership would likely include Trustees themselves. This would allow the Trustees to maintain the necessary control over Committee actions while not burdening the entire Board with each matter before the Committee. Membership would presumably also include alumni, students, faculty and staff; the actual membership at a specific university should reflect the level of autonomy given the Committee. That is, if a university decides that the committee needs the authority to propose shareholder resolutions with firms' managers, then the Trustees will probably insist that there be Trustee membership on the committee. However, if the Committee is authorized only to write letters requesting information, the Committee may have a membership of only students, faculty and staff.

Transaction Costs. There are potentially high costs associated with the Participatory Mode. First, although this mode does not involve the purchase or sale of shares, and there are therefore no additional brokerage fees, the costs of operating an active Committee could be significant (the scale of these costs would be a function of how active the Committee is). Research on the issues themselves would necessitate work beyond the data provided by the IRRC (see description of this organization in the Mechanisms section): legal counsel for advising in the writing of resolutions ; phone calls and travel for interacting with the management of firms; coordination with other shareholders to make resolutions effective;

meeting regularly and at length to develop strategies and written materials. The issue of time commitment is not a small one. Depending on how active the Committee is (a function of the size and diversity of the portfolio, the ethical systems the school operates under, the willingness of the Trustees to subject the endowment to ethical analysis, etc.), it could meet anywhere from less than once a month to every week. Subcommittees investigating individual firms might have periods of extreme time commitment (especially if conferences with management are needed). This time commitment will influence the membership of the committee; not all members of the university community would be able give the time necessary to participate. The Committee will be limited in the projects that it can take on; we address this in the Recommendations section below.

Overall, the Committee could cost on the order of $10,000 to $20,000 per year[44]. Operating costs would vary greatly depending on the variables listed for time commitment and whether the university were to hire an analyst to gather and consider the vast amounts of data available.[45]

Opportunity Costs. Because there are no shares traded within this mode, there is no restriction of choice and thus there is no direct market-based cost. However, it is conceivable that there would be indirect market-based costs if the university's interactions with a firm were to cause negative publicity to the firm and lead to a drop in share price. While this risk is small, there are a few additional issues with effectively zero cost (or minimal risk of cost) that deserve mention. The costs to a firm for publishing and otherwise handling a resolution brought by a university are real but, once distributed among shareholders, probably not significant. This may not be so if for some reason the school were to bring legal action against the firm to force it to

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[44]Currently, the Assistant to the Vice President's Office currently spends under $6,000 per year operating the ACSR, primarily for subscriptions to IRRC publications (Doug Phillips, personal communication, 9 November 1995). We estimated the values given based on the judgment that the current ACSR is relatively inactive and that the Williams endowment, while large per capita, is significantly smaller than some large universities'.

[45]There is, unfortunately, no easy way to compare these figures to spending on other administrative committees at Williams. Like the current ACSR, most committees do not have their own budgets; those that do are allocated no more than $2000 per year. Stuart Crampton (Provost, Williams College), personal communication, 14 December 1995.

distribute the resolution on proxies. Here, however, the major cost to the school would be its own legal fees, not the lost profit from the firm in which it is partial owner. Lastly, the costs of policies implemented as a function of the school's efforts (direct communication with a firm may lead it to change policy so to avoid a proxy battle) again exist but are most likely to be insignificant to the school. Assuming that the school does not push for fiscally unsound policies, the costs of activities traditionally requested by shareholder-initiated resolutions (e.g., yearly reports on hiring) should again not be significant once distributed to all shareholders.

Turnover Time. Because no shares are sold, there is no turnover in the portfolio.

Market Time-Frame. The turnover of concern here is the turnover in firm behavior. The effects of direct communication could actually be significantly faster than those of simple proxy voting: if a firm responds to a direct request or makes changes so that a resolution is withdrawn before the proxies are mailed, it can do so without waiting for the annual proxy season. Further, the firm has the incentive to move quickly to avoid the submission or promote the withdrawal of a resolution.

Application to Portfolio. The activities of the Participatory mode Committee are limited primarily to the stock portions of the portfolio; the firms indebted and funded through the bond and venture capital portions of the portfolio do not have the incentives that the publicly-traded firms do for responding to direct communication from funders. That is, as a shareholder the College is partial owner in a firm and thus has a voice (small, but nonetheless legally enforced) in the operation of the company. However, lending through bond holding and the investment of venture capital gives no such official voice to the College.

While much of the Committee's influence on firms in which a university is a shareholder will be felt outside of the official lines of communication (sponsorship of resolutions, etc.), there is reason to believe that the presence of these official lines is one of the major reasons that a university's non-official voice would be heard at all. That is, a firm may listen to and act on a shareholder's unofficial request specifically to avoid an official request and the resultant publicity and potential cost.

Without the threat of official action, it is unclear whether firms in which a university holds bonds or invests venture capital would have any reason to respond to any requests from the school. There is respect accorded to universities that, along with the threat of the university going public, may induce some response by firms to a school's comments. However, it is doubtful that a firm would change its behavior any more than necessary for public relations reasons.

Information Availability. As suggested above in the Transactions Costs section, good decision making by a Participatory Committee will require significant information that is not necessarily readily available to a university committee. Since the intent of this mode is to induce change in firm behavior, the Committee must have specific information about the behavior of each of the firms in which the university is a stockholder. The Committee must chose the firm(s) with which it would be valuable to communicate and the very specific nature of the issue(s) that it will address. That is, the Committee must keep tabs on all of the firms in the university's portfolio and then, in order to be effective in bringing about the change that it desires, must fully research any particular firm's structure and behavior on the issue of concern.[46] While the Committee could do a less thorough job and simply advise a firm that it was "concerned" with a practice, it is hard to imagine that such discussion would generate significant change (especially change which that satisfy the Committee).

The research needed would be much more than that needed for simply voting proxies because the Committee would actually be initiating a discussion or authoring a resolution. Further, while there is quality, compiled information available from the IRRC about resolutions which have been submitted, there would be no such information available for a new resolution. Some of the information desired or needed by the Committee may in fact be available only from the firm in question, which may or may not choose to share it.

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[46]Consider an example. If a Participatory ACSR were to find General Electric's minority hiring practices to be unacceptable, the Committee would have to research GE's hiring practices, the history of such and alternative models before it could address GE with an alternative plan. An unresearched or poorly researched plan could easily be dismissed by GE, potentially with great embarrassment to the university.

Institutional Decision Making. There are two sets of decisions concerning the implementation of the Participatory Mode that need to be made: the university institution needs to decide the nature of the Committee, and the Committee itself needs to decide on specific actions. While the university must make choices about the nature of all its committees, there are some issues that stand out in this case. As mentioned in the beginning of this section, membership of this committee is interrelated to its independence and ability to act autonomously. The Trustees, on the part of the university, will have to decide how much leeway to give the Committee and its membership. Further, because the actions of such a Committee are pro-active, the university will have to determine how publicly it wishes to pursue its responsible investment goals. If it wishes to avoid the public eye, it will have to limit its communication to letters and conversations, avoiding the submission of resolutions. Lastly, since the Committee speaks on behalf of the university, it should attempt to incorporate the opinions of the university community into its deliberations. While this is so for all of the modes described in this analysis, it is especially true here because the Committee works pro-actively to effect change. The Committee is not simply performing the shareholder duty to vote proxies, but is actually working to redesign firms' behavior. With this greater involvement comes a greater stake for university community members and thus a greater need to involve the larger community in the decision making process. (With wider involvement comes greater transaction and coordination costs to the Committee. However, wider involvement could lower some costs, assuming that the various special interests within the community are willing to present research to the Committee on issues of import to them. Greater involvement also authenticates Committee actions.) Lastly, the Trustees may wish to empower the Committee to work jointly with other institutions, educational or not, to increase the effectiveness of each communication with a firm's management. That is, the university could cosign letters requesting change or cosponsor shareholder resolutions. This would necessitate public action and could lead to even greater transaction costs as time and resources were spent on coordinating between institutions.

When the Committee itself makes decisions on specific actions, it must consider a number of items. Of course, it must consider what social issues to address at what firms (unlike in the Proxy-Voting Only mechanism where these are chosen by the authors of proxies). In the Participatory mode, this means considering what firms will be receptive to shareholder input and about what issues. Since the goal of this mode is to change behavior, it would be useless to continually challenge a non-receptive firm with resolutions, which will never pass, since there will be no real change. A related item to decide is the means with which to address issues: assuming that the Trustees give the Committee the authority to submit resolutions and communicate directly with firms, the Committee must decide what would be the most effective means for affecting change. The Committee may be able to develop a standard operating procedure that sets out an ordered series of actions to take (e.g., letters followed by a conference followed by a resolution).

Legal Implications. The SEC has, since first allowing Campaign GM in 1970 to force GM to include two resolutions, defined and loosened the requirements for institutions to meet to force a firm to include a resolution on its annual proxy, and universities have successfully submitted resolutions for inclusion on proxies.[47] Thus, universities are legally entitled to submit proxies and presumably entitled to otherwise communicate with and try to alter the behavior of firms in which they are shareholders. Further, these actions (as free of opportunity cost in the market) are all acceptable under the "Prudent Man Rule"[48] used by the states and the Federal government to monitor the fiduciary responsibility of Trustees' actions, so that the Trustees should not be legally limited in their support of such communication.

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[47]Vogel, pp. 79, 115-119, 98.

[48]Whereby each Trustee must act on the part of the College as a "Prudent Man" would when dealing with his own finances. The rule, common to nearly all state and federal codes, is intentionally vague to give investors as much leeway as is reasonable. Operationally, the rule is the standard evoked (by the government in the case of a non-profit such as a university) if the controllers of a portfolio (the Trustees) are felt not to be investing responsibly. The regulatory body will find against the Trustees if it feels that they did not invest in a way that a reasonable, rational individual would if investing his own money. The Trustees can be held accountable for losses incurred by acts that violate the Prudent Man Rule. Personal communication with Stanley Parese, 30 October 1995 and Douglas Phillips, 9 November 1995.

Ethical Implications. The Committee is primarily in a utilitarian mode (i.e., investing to do social good); it attempts to shift the behavior of firms towards some university-defined responsibility. This separates it from both of the other modes. As opposed to the Minimalist mode which involves simply fulfilling minimum standards, the Participatory mode pro-actively seeks change toward some goal. Compared to the Screen mode, the Participatory mode seeks effectiveness, a final social outcome. This leaves the Participatory Committee, acting on the university's behalf, ethically obliged to both identify the university community's definition of responsibility *and* to choose methods of participation that are effective in bringing about change.

By taking on a Participatory mode of responsible investment, a university is acknowledging that it seeks to have an extra-educational impact on its community. This suggests that as an institution it feels capable and authorized to try to influence society: it promotes what it identifies as good. These are no small steps for an institution dedicated specifically to learning, not the broader social good, and have been and will be taken hesitantly. This is shown historically by the fact that it took seven years after Campaign GM (the first shareholder resolution that the SEC forced a firm to include on proxies; see Ethics section for background) for the first university to author and submit a resolution.[49] At Williams, this is evident in the tight control the Trustees have held over the ACSR: they refused in 1980 to allow Williams students to read a statement on behalf of the College at the annual stockholders' meeting of IBM, restricting the action to a letter to be approved by the Financial Committee of the Board of Trustees.[50]

Effect on Neutrality. This step that the university takes puts it at real risk of violating the internal institutional neutrality that allows free academic discourse. Is there a means for maintaining neutrality while allowing the institution as a whole to take the step towards responsibility (see section on University Neutrality)? Because this Participatory mode is

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[49]Vogel, pp. 75, 98. In the 1977/78 proxy season, the University of Minnesota offered the first resolution from a university.

[50]"Over the Years: The Members and Actions of the ACSR," in Ellen Berek, ed., *Williams Reports*, pp. 12, 1983. The statement was co-authored by student members of the ACSR and the Williams Anti-Apartheid Coalition.

necessarily close to the Trustees, there is the possibility that they, as external members of the university, can direct the institution towards a responsibility without biasing the academic sphere of the institution. It is also possible (by a converse logic) that by having the entire community participate in the framing and acting out of responsibility, neutrality is maintained through diversity--that the presence of a wide variety of opinions makes all safe. Lastly, there may be an institutional structure for the Committee, through careful, balanced representation and separation of duties, that would allow the functional separation of the responsibility decisions from academic decisions.

The Participatory mode itself, through its focus on action rather than definition of ethics, is somewhat amenable to this separation of social responsibility from academics. While certainly not clear cut, there is a slight advantage here for the Participatory mode over the Screen mode. Consider that because such a large portion of the Committee's actions would be dedicated to designing functional methods for inducing change, the responsibility issues that it addresses would have to be simpler and more agreeable (among the university community) than those addressed by the self-satisfying Screen mode.[51] This suggests that this Participatory mode is best used for simpler matters on which consensus can be gathered within the university community, allowing the Committee members to focus on effecting the responsibility that the community aspires to rather than debating the nature of this responsibility.[52]

Behavioral Impacts on Firms. Because the Participatory mode is an utilitarian approach, if successful, it should have significant impact on the behavior of firms. Indeed, the direct communication of shareholders with firms can induce changes in corporate behavior. Firms will

[51]Neither mode is entirely dedicated to either the utilitarian affecting of change or the deontological satisfaction of institutional values. However, as suggested in the section above on ethics, there are links between the Participatory mode and utilitarianism and the Screen mode and deontological thought. Here we have simplified to a binary relationship for argument's sake; it is more complicated than this.

[52]This argument is somewhat problematic: one could certainly counter it with the assertion that the Participatory mode is in fact much less workable than the others because it requires operation on this second, utilitarian variable. That is, the need for utilitarian debate does not excuse the need for value-identification debate. Yet, there are cases (as evidenced in the extreme by the movement to divest from South Africa) where values are relatively homogeneous and the choice of how to affect change is the truly challenging part of responsible investment.

frequently make changes in response to direct communication or even failed resolutions in an attempt to maintain high public opinion of the firm and thus maintain the ability to access capital in the market.[53] Again, as mentioned in the section on the applicability through the endowment, the Participatory mode will be most useful for addressing firms in which the university is a shareholder, not a creditor.

Conclusions

Ultimately, the Participatory mode allows a university to invest some human and financial resources, drawn from the entire institution, into responsibility research and decision making. This can produce effective, low market-cost options for promoting relatively simple and non-controversial policies at firms in which it is a shareholder. The financial tie between the university and the corporation, along with the Trustees' requirement to behave prudently, suggests that the university will only promote policies that it believes will be fiscally responsible. These actions are taken with the intent of not only making the university's endowment more socially responsible, but actually making the firms in the market more responsible. How effective the Participatory mode is in affecting corporate change will depend not only the university's fiscal might, but also on the Committee members' negotiating skills.

Screen Mode

Under certain circumstances, colleges and universities may choose to extend their ethical norms to the actual purchase and sale of securities. We call any systematic attempt to factor ethical concerns into the decision making process of the portfolio manager a screen. A wide array of approaches fall into this category. A screen may be as simple as a decision to sell a specific stock or bond for ethical reasons, or it may be as involved and complex as a strategy that requires a close scrutiny of all the securities earmarked for possible purchase. While different approaches to screening endowments give rise to distinct costs and benefits, the approaches all

[53]Vogel, p. 99.

have basic distinguishing characteristics in common. We begin this section by generalizing about what separates screens from the other mechanisms we have considered. We then analyze screens in terms of the ten variables described above.

Screens are fundamentally different from the proxy voting and direct communication models described above in three key ways. First, screens are the only practical way investors can apply their ethical norms to bonds and venture capital. Second, screens are distinguished by the fact that they may have some impact on earnings. The size of this impact (and according to some, even its direction) is debatable, but the fact that it exists raises a host of ethical and legal questions absent in the first two mechanisms. Finally, screens tend to be quite effective at achieving ethical consistency within a college or university, but they are less likely to catalyze changes in the behavior of firms. In terms of the ethical models developed above, screens emphasize the deontological over the utilitarian.

Transaction costs. The transaction costs associated with screens fall into two categories: the cost of the transactions necessitated by the screen, and the cost of the information necessary to effectively implement the screen. Trading securities costs Williams College $.04-.05 per share for each transaction, which usually amounts to less than one third of one percent of the share's value.[54] Screens that increase the number of shares trading hands in a given time period will therefore create only negligible transaction costs. The cost of information will vary with the type of screen. Comprehensive screens that require a careful analysis of every company earmarked for possible purchase are likely to be very expensive to implement. The information services described below all cost approximately $10,000 per year. In addition, schools will have to create some sort of structure to analyze this and other information and make specific recommendations. This would likely take the form of a paid position because the time and expertise it would require.

Opportunity costs. Commonly agreed upon financial theory suggests that any time a portfolio manager has his or her field of potential investments limited, income may suffer. The

[54]Douglas Phillips, personal communication, 9 November 1995.

magnitude of the loss is very difficult to pinpoint, as it varies with the skill of the manager and the behavior of the markets.[55] The best indicator of the costs of screens is the performance of socially responsible mutual funds and pension funds that manage in accord with a wide variety of screens. While these funds use the same basic type of screens that might be implemented by colleges and universities, their screens tend to be much more political and much more comprehensive than those appropriate for the academic context.

The financial literature has surprisingly little to say about the track record of funds managed in this way. This may be due to the fact that socially screened mutual funds have only been on the market for 15 years. Those that have been in existence long enough to be analyzed show only that screened mutual funds, like their non-screened counterparts, are highly variable. Some do well, and some do poorly. The examples I give highlight their successes. Between May 1990 and December 1994 the Domini Social Index outperformed the S&P 500 by over 10%.[56] The Parnassus fund, one of only 5 screened funds having at least a ten year track record, ranks number ten out of 481 growth funds. US Trust Company, which manages both screened and non-screened funds, found that their screened fund consistently performed better.

Finally, a study examining the differences between the returns to single employer and multiple employer pension funds found that screens had no long term effect on performance. The authors report that "little evidence is found that 'social investing,' most likely to occur in multi-employer funds, has increased the risk or consistently reduced the returns of union pension funds."[57] The successes of these mutual funds do not prove that socially responsible investing is more profitable than traditional approaches, nor do they suggest that socially responsible investing will always perform up to non-screened standards. Rather they show that it is possible to generate very high returns without sacrificing ethical standards.

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[55] Roger Bolton, personal communication, 13 November 1995.
[56] http: //condor.depaul.edu/ethics/bizsoc2.html, date?.
[57] S. Dorsey and J. Turner, "Union-Nonunion Differences in Pension Fund Investments and Earnings," *Industrial and Labor Relations Review.* 43(5) July, 1990, pages 542-545.

Turnover time. How long would it take for a college or university to rid its portfolio of investments in socially irresponsible companies if a screen were placed on all new purchases? Current turnover rates in the Williams endowment are about one third per year, but some stocks are held much longer than others.[58] This means that the portion of the endowment that trades regularly would be screened over the course of just a few years.

Market Time-Frame. The effects of a screen are immediate upon implementation, unless a school screens only incoming firms (new purchases for the portfolio). However, the immediate effect on the firm; with minimal market power, few schools own enough shares in any one firm to alter its trading price or the attractiveness of its securities to other traders. There may be longer term effects, especially in the debt market, associated with public relations: a divestment can cause a bond-issuing firm bad press and thus a lowering of the ratings of its bonds.

Application to Portfolio. Screens, unlike the other mechanisms, have the potential to affect to all forms of investment. Indeed, this is one of the qualities that makes them very attractive relative to the other two mechanisms we discuss.

Information Availability. Screens require detailed information and careful analysis to work effectively. The exact information necessary depends on the nature of the screen, but in all cases the administrators of the screen must be able to evaluate how responsible companies are. Several companies, including The Investor Responsibility Research Center (IRRC), the Council on Economic Priorities, and Kinder, Lydenberg and Domini, provide thumbnail sketches of firms to institutional investors. These services provide numerical ratings and qualitative descriptions of the social and environmental record of over 1,500 US companies, including all of the S&P 500. Much of this information is available on-line in a format that facilitates easy comparison of companies.[59] This information makes it fairly easy to implement certain types of screens (i.e. a screen that filters out companies that fail to comply with federal environmental and employee relations law).

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[58]Doug Phillips, personal communication, 9 November 1995.
[59]Douglas Cogan (responsible investment advisor, IRRC), personal communication, date?.

While the information provided by the services described above is generally accurate and useful, it alone cannot adequately inform the implementation of most screens. Deciding which companies meet the ethical standards set by the university takes a thorough understanding of all the companies' operations. This level of understanding can come about only through a rigorous analysis of primary information about the companies in question, and of the context in which they operate. It is with this in mind that we say that schools seeking to implement screens will almost certainly need intelligent and well qualified analysts working to implement the screens.

Institutional Decision Making. A screen requires that an institution of higher education make three sets of difficult decisions. First, the Board of Trustees, or whatever body is entrusted with the financial welfare of the university, must decide that a screen of some sort is necessary. Second, the screen itself must be formulated in a way that does not move the institution too far from the ideal of neutrality. This may mean that the screen has to be developed in a forum that exists largely external to the academic life of the college. The Board of Trustees is one such group. Another is an advisory committee, perhaps similar the one that currently exists at Williams. Finally, some body within (or, potentially outside of the school if the screen were explicit enough) the school, once again separated from academic life, has to make the day to day judgments necessary to implement the screen.

Legal implications. The legal ramifications of screens are not clear. The fiduciary duties that bind a university's Trustees take the form of the prudent man rule, which requires that all investments be made according to sound business judgment. This allows trustees to implement screens that have no adverse effect on overall earnings. Screens that do have an effect on earnings, on the other hand, may be problematic. It is, however, very difficult to establish that the portfolio managers were violating the prudent man rule, and not just taking reasonable risks. To fully understand the legal risks associated with screens, an institution would have to rely on the judgment of an attorney.

Ethical Implications. As we establish below, screens are not particularly effective ways of directly affecting the behavior of publicly traded firms. If the goal of a college or university is to use its endowment as a tool to work for positive social change, stock is the most effective strategy. If the goal of the institution is to invest in a manner consistent with its espoused values, however, then screens are clearly the best mechanism. They allow the college or university to move towards insuring that their endowment is not being put to uses that violate any of their core values, and that none of their income is derived from socially harmful activities.

Bonds and venture capital are a special case because screens are the only way that investors can address the ethical questions that accompany their ownership. When faced with a socially harmful investment, bondholders and venture capitalists have only two options: to continue maintain a financial stake in the firm, or to sell. They are forced to choose between moral purity and moral apathy.

Effect on Neutrality. The careful and thoughtful implementation of a screen would not necessarily compromise the level of neutrality requisite for a college or university to maintain the academic context necessary for the free exchange of ideas. Screen are more mechanisms that allow investors to make money without violating their moral values than they are tools for achieving social change. In this respect, screens are more overtly political than shareholder activism. The process through which a screen is designed and maintained, rather than the screen itself, poses the largest threat to neutrality. If this process is separated from the academic life of the college or university, it would be less problematic. We will spell out in detail how this might be accomplished in the final section of this paper.

Behavioral Impact. While screens are in most cases likely to be chosen for deontological rather than utilitarian reasons, they will have some impact on how firms behave. The magnitude of this effect is difficult to pinpoint. A screen is tantamount to a reduction of the demand for a security. If the demand is reduced enough, price will be driven down. While the firm will not be affected in the short run by a devaluation of a stock or bond, its ability to cheaply raise capital may be handicapped. Furthermore, cheaper stock renders corporations vulnerable to buyouts. If firms do not realize that social screens contributed to the decline of their stock or bond, these effects will have little impact on the behavior of firms. Currently, firms have no way of accurately determining what changes they need to make to gain the trust of socially responsible investors beyond what they can infer from shareholder resolutions.

Even the most highly endowed colleges and universities lack the capital to affect the price of the large companies favored by institutional investors. This may change if shareholders begin implementing similar screens, either through cooperation or through coincidental convergence. As firms become aware of commonly held screens, they may change their practices. While this effect is probably not affecting the way management makes decisions currently, the amount of capital subjected to screens is growing very quickly. In 1984, roughly $40 billion worth of investments were screened. By 1993, this figure reached approximately $1 trillion[60], or roughly 10% of the money invested in the United States.[61] The moral stance taken by respected colleges and universities set precedents that may affect the decision making of other investors, leveraging more money into screens. In the long run, the introduction of social criteria into decisions concerning the allocation of capital in the US economy may fundamentally alter the environment in which firms seek capital.[62]

[60]http: //www.bath.ac.uk/centres/ethical/books.html, date?
[61]Scott Klinger (responsible investment advisor, US Trust), personal communication, date ?.
[62]Severyn Bruyn, The Field of Social Investment, p.?.

PRINCIPLES FOR NEUTRAL RESPONSIBLE INVESTMENT

The simultaneous and equally important desires for academic neutrality and fiscal health burden the modern, private university with a challenging dilemma. They are each necessary at the most basic level for operating a university: neutrality must be defended as a basic characteristic of the academic sphere, and funding is necessary to operate the institution that protects the neutrality. Neutrality cannot be approached on a large scale without the institution, and an institution which does not defend neutrality cannot really be a functional, respected university.

How to invest the endowment for high return while minimizing the breaches in academic neutrality is an institutionally challenging task. As shown by our discussion of the political nature of investing, a profit-maximizing investment policy is not neutral. It simply ignores the ethical implications of the school's investing. Further, we feel that the historically prominent *University Neutrality* policy does not satisfactorily protect university neutrality in a transparent world. In the following section we draw from the ethical analyses above to develop a series of principles for designing investment responsibility policy for a university. By following these principles, a school can institute a policy that will defend university neutrality more effectively than *University Neutrality* does while allowing the school to invest without violating it members' values. The principles are organized into three categories: Decision-Making Mechanisms, Committee Structure and Actions.

Decision-Making Mechanisms. Responsible investment decisions depend on the way in which a school defines its moral personality (here the applicable possibilities falling between utilitarian and deontological) and the specific facts and values of the case at hand[63]. These two factors are discrete and require somewhat different handling; moral personality establishes a framework for choosing actions while facts and values (as used here) are specific to a particular

[63]We use "moral personality" to refer to a school's position along the spectrum from deontological to utilitarian; "values" are the issue-specific values/ethical systems that the members of a university community hold.

case or issue. The confluence of these two would lead to an utter collapse in neutrality because it would result in the school defining itself in terms of how it values specific issues. By identifying a position or range along the utilitarian-deontological spectrum, the school is recognizing part of its personality and staking a moral claim.[64] This act is not without risk to neutrality, for it does support one set of ideas over a field of others. However, because it is an issue of institutional personality, the associated loss of neutrality is implicit in the existence of the institution itself.[65] Further, because the recognition of an institutional personality is on a theoretical level, relatively distant from investment acts, it guides the Committee members (giving them a frame of reference so that their decisions are not arbitrary). This personality, which we conceive of as evolutionarily determined based on precedent, will change over time. We feel that, in the interest of neutrality, the members of the Committee must have the ultimate say in interpreting the precedent (because they will be applying it in investment decisions). However, it is not unreasonable to think that other university community members may have constructive input to give in formulating the interpretation of this personality.[66] We leave open the actual format by which the personality is framed: it could be simply informal discussion among the Committee or possibly as formal as a document guiding what type of actions (from deontological to utilitarian) to take based on the nature of a problematic investment.

Once specific applied values and actual investment decisions are on the table, decisions must be on a case-by-case basis, made by a single committee. Thus, the Committee takes its interpretation of the school's moral personality and uses it to frame its perceptions of the university community's values and the facts concerning a particular investment problem. The result should be a rational problem with an ideal answer (or set of answers): follow the

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[64]We suspect that all schools will identify a range somewhere in the middle of this spectrum, allowing it a variety of options.

[65]A school has a personality that colors the type of thinking that occurs there. This is unavoidable and is in fact a good, because without this coloring, all thinking at all institutions would be the same. Diversity in scholastic personality creates diversity in thought. The school must be careful not to settle on a fixed personality, however.

[66]As above, we use "university community" to indicate the students, faculty, staff and alumni of a school.

investment strategy that will most likely give a result that satisfies the values of the university members within the framework of the institution's personality.[67] Therefore, the role of the Committee is to judge what the values of the university members are, interpret the facts and then apply both of these within the university's personality.

To fulfill this role, the Committee must be able to judge the values of the university community. The Committee would have some sort of forum to actively elicit the opinions of the community members; the intent is to gather a well-founded impression of how various community members' values' fall in relation to corporate behavior. Further, because a school's investments are relatively distant from the bulk of the community, the Committee must establish mechanisms by which the community has access to information about the holdings in the portfolio. Additionally, to make its decisions the Committee needs high quality information about the case at hand. This requires the Committee to do research or otherwise acquire reliable data on the firm and the social/environmental issue.

Committee Structure. The university as an institution cannot make decisions and act upon them; this must be mediated by a functional entity. Because of the complexity of ethical/investing questions, this entity cannot be simply a set of rules, but rather it must be human and interpretive. As such, there must be a Committee within the university that will make decisions and act out the responsible investment policy. The Committee must speak for the university as a whole and thus should be comprised of university community members intimate with the school and its personality. Members should be selected based on capability of making judicial decisions. Importantly, the members should be non-representative; if members were to have constituencies, university neutrality would be disserved because the Committee

[67] For example, if a school were utilitarian (university personality, determined by the Committee), a majority of its members value biodiversity (members' values, as judged by the Committee) and Firm Y has a resolution debating the purchase of Old Growth forest for clear-cutting (facts), then the Committee would apply the members' values by voting shares against the purchase. This is within the university's personality because it seeks to prevent the corporate behavior, rather than separate the university from the behavior.

members would participate with a set agenda, not with the intent of designing actions that best fit the university's personality and the community's values.

Representational membership would be less neutral because it would tend towards polarization in the Committee and its membership; polarization causes individuals to be associated with specific policies/values and then invites action against the individuals as a means for mediating action against policies/values. Further, the polarization would make the committee's interactions less efficient and consensus more difficult to obtain. Lastly, the Committee should be large.[68] This will allow easier distribution of research and, more importantly, will dilute the values brought to the Committee with each member. This mechanism is not perfect: no individual can divorce him- or herself from a value-laden decision. However, careful selection of members and explanation of intent should help ensure that investment decisions reflect the values of the university as a whole. The intent is to have the Committee make judicial decisions, not value judgments, about each case.

Actions. The actions taken by the Committee to make the university's investing socially responsible will, most likely, draw from all three of the Mechanisms elucidated above.[69] This will allow the Committee to tailor its response to each case as necessary; although it is reasonable to suspect that each university's Committee will specialize in specific approaches for dealing with firms and social issues. The Committee's actions should be metered out by the severity of the effects of the corporate behavior that is at issue. This serves to focus the Committee's time and information investments and the University's financial power and "influence capital." Likewise, the intensity and severity of the Committee's actions should reflect the level of consensus about the issue in the university community. This is in part to avoid polarization on campus, which is detrimental to neutrality, and also for the reasons enumerated above. Connecting intensity with level of consensus serves as a means for resolving

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[68]We leave "large" undefined; it will depend on the size of the university, its endowment, the endowment's diversity, etc.

[69]We feel that this is likely for the same reasons that we suspect that university personalities will fall between utilitarian and deontological: no diverse institution like a university can be so extreme that its personality accepts only one of these in all cases.

the difficulty generated by trying to act on the combined values of thousands of people. Of course a simple average of values is impossible, but a majority-rules system is problematic because many investment decisions are integral--so there is no means for the minority to express its values. Thus, actions should be minimal when there is divergent opinion and greater when the community comes to a greater level of consensus.

To balance practicality with the needs generated by the "Prudent Man Rule" and liability law, the Committee should act independently in some cases (e.g., communicating with firms) but should act through the Trustees when taking more financially significant, formal actions (e.g., the sale of shares). This gives the Committee the flexibility and freedom needed to act efficiently while keeping their actions under the control of the legally liable Trustees. The autonomy given to the Committee by the Trustees will depend on a number of factors: experience of the Committee members, who the members are (if the membership includes Trustees, the Committee is likely to have more autonomy), history of the Committee, etc.

There is one specific action that we feel is a necessary part of any responsible investment policy and is, in fact, a part of being an active stockholder even without specific intent of social or environmental responsibility: voting shareholder resolutions. Stockholders are partial owners in firms and thus have a voice in the firm's operation. As such, we feel that it is a university's obligation to vote its proxies, whether the intent is for profit maximization or social responsibility or some fusion of the two.[70] Informed proxy voting does have costs (time, research costs, etc.) and needs to be performed in a way to minimize the risk to neutrality; however, both cost and risk are low.

[70]We feel that a blanket policy of voting with management is in effect not voting and thus unsatisfactory. While a profit-maximizer might argue that management knows what is best for the company's performance, it is clear that management's interests are not always the same as owners' (e.g., management compensation). It is in the university's best interest to examine each resolution, vote with management when the issue is one of business-only concern and for which management is unbiased, and vote independently of management when the issue is a social issue.

Additionally, we wish to recognize that responsible investment need not be solely reactive; universities may choose to invest proactively, choosing firms that stand out as having policies especially in line with the school's or its members' ethics and values.

We have interpreted the above principles graphically. Figure 1 visualizes the range of actions available to a university as a stockholder. Arrows indicate example actions that a school may take; a school would probably have all of its actions within a relatively narrow vertical range but a wider horizontally range, varying according to the issue and the level of consensus on campus.

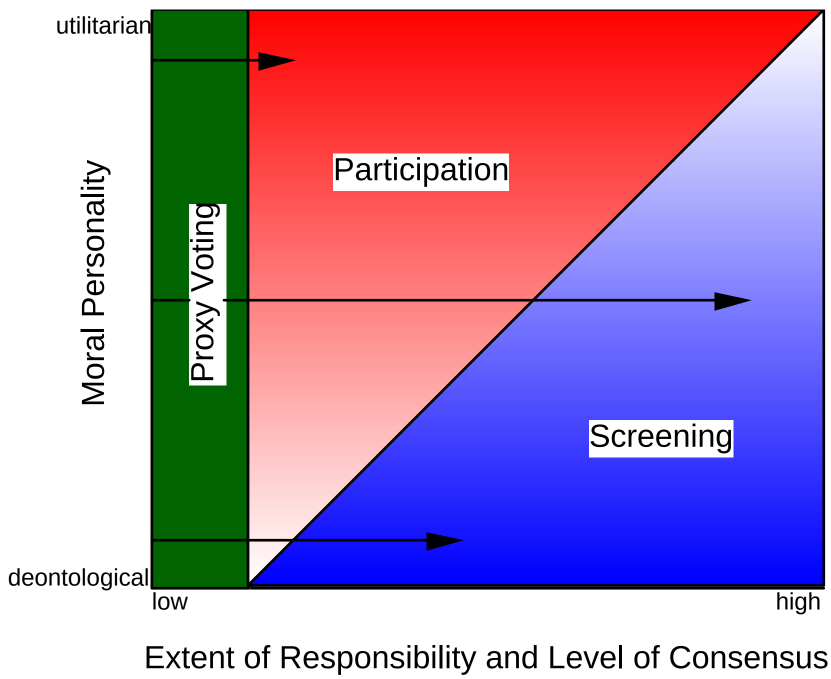

Fig. 1. Range of actions available to universities for influencing firms in which they own stock. Lines indicate individual investment actions.

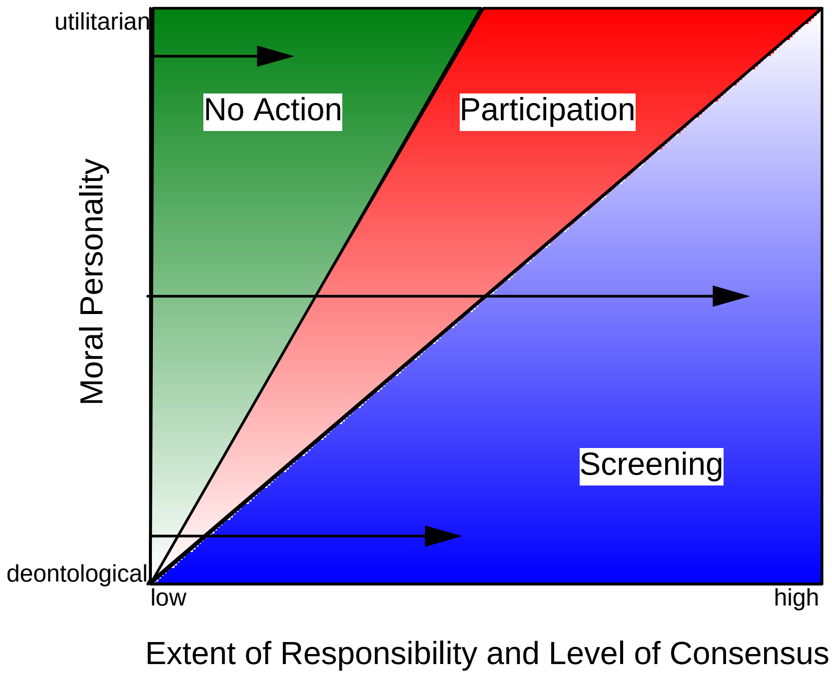

Fig. 2. Range of actions available to universities for influencing firms in which they are invested as venture capitalists, bond holders or other non-ownership means. Lines indicate individual investment actions.

Figure 2 visualizes actions available for non-stock holdings such as venture capital and bonds. Notice that it does not have proxy voting as an option and the participatory mode is limited (without the leverage of proxies, investors in venture capital and bonds cannot expect firms to be as responsive to direct communication). This leaves screening as the primary mechanism for influencing these firms.

We have presented a variety of principles that, when taken together and applied to a given university, should serve as good guidelines for designing a responsible investment policy that is responsive to the university's personality and its member's values. The principles' foremost aim is to coordinate the need for defending neutrality with the moral character of the university. Below, we apply these principles to Williams College, recommending a new structure for the Advisory Committee for Shareholder Responsibility and a new, reinvigorated approach to active responsibility.

RECOMMENDATIONS TO WILLIAMS COLLEGE

Two years ago the authors were independently elected the student members of the Advisory Committee on Shareholder Responsibilities (ACSR) by the students of Williams College. We chose to involve ourselves in the committee because we felt that issues of global equality, the environment, and the practices of transnational corporations in the developing world have emerged as key issues in the fiscal-ethical realm of responsible investment. We each suspected that because the ACSR was formed in response to a single issue (apartheid in South Africa) the Committee's structure and mandate were too narrow to respond to these issues. Now that apartheid has faded away (not independently of the responsible investment movement's actions), we expected that it would be necessary to re-evaluate the structure and purpose of the ACSR.

After a careful analysis of the issues surrounding socially and environmentally responsible investing, we have concluded that our initial impression was right. We find that the current functional structure of the ACSR is not optimal, and that the College can take steps in the direction increased responsibility without sacrificing the high fiscal returns necessary for the maintenance and growth of an excellent college. Further, our research and analysis has shown us that there exists the possibility to better balance the need to protect academic neutrality while investing responsibly. In fact, we feel that implementation of the changes recommended below will increase protection of university neutrality and responsibility simultaneously. Ultimately, our goal is to aid in the evolution of a more effective and thoughtful ACSR.

Our revisions are not designed to, and will not, result in massive change in the way the College invests its endowment or even in the way it addresses the ethical issues related to this investment. Rather, they re-focus the mandate and mission of the Committee, essentially within the parameters of its original (1979) and revised (1983) charter, to better address the ethical dilemmas of the coming decades. The new Committee will consciously attempt to implement the values of the College community within the framework of Williams' personality.

Functionally, the Committee will differ only in its selection, level of activity, and interface with the College community.

Our recommendations fall into three interconnected categories. The first set proposes a restructuring of the ACSR that we believe will increase its ability to deal effective, fairly, and explicitly with the ethical issues implicit in investing. The second describes how input from the college community[71] should play a larger role in guiding the ACSR. The final cluster of recommendations delineates changes in the types of actions routinely taken by the ACSR that we feel will match its actions to the magnitude and nature of the responsibilities it bears. While we feel that the three sets of recommendations dovetail and should be implemented together, we also believe that each stands independently.

Recommendations For a Restructured ACSR

We find that a change in the structure of the ACSR would allow the college to act more responsibly without sacrificing any of the neutrality it needs to maintain an academic context.

Role of Committee

Currently, the ACSR devotes nearly all of its energy to voting the college's shares in accord with the ethical positions of the individual members. We feel that the committee should expand its focus to include new forms of input and output. New input would take the form of improved channels allowing all members of the college community to bring concerns to the ACSR. New forms of output would entail an increase in direct communication with firms from all parts of the portfolio. ACSR members would continue to vote proxies, but they would also respond to concerns from all portions of the college community, all of whom are stakeholders in the endowment (and thus, to some extent, connected to it ethically). In Figure 3 we diagram the

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[71]The college community is defined as the students, faculty, administration, staff and alumni of Williams College.

revised structure for the Committee. Our goal is to separate the political actions of the Committee

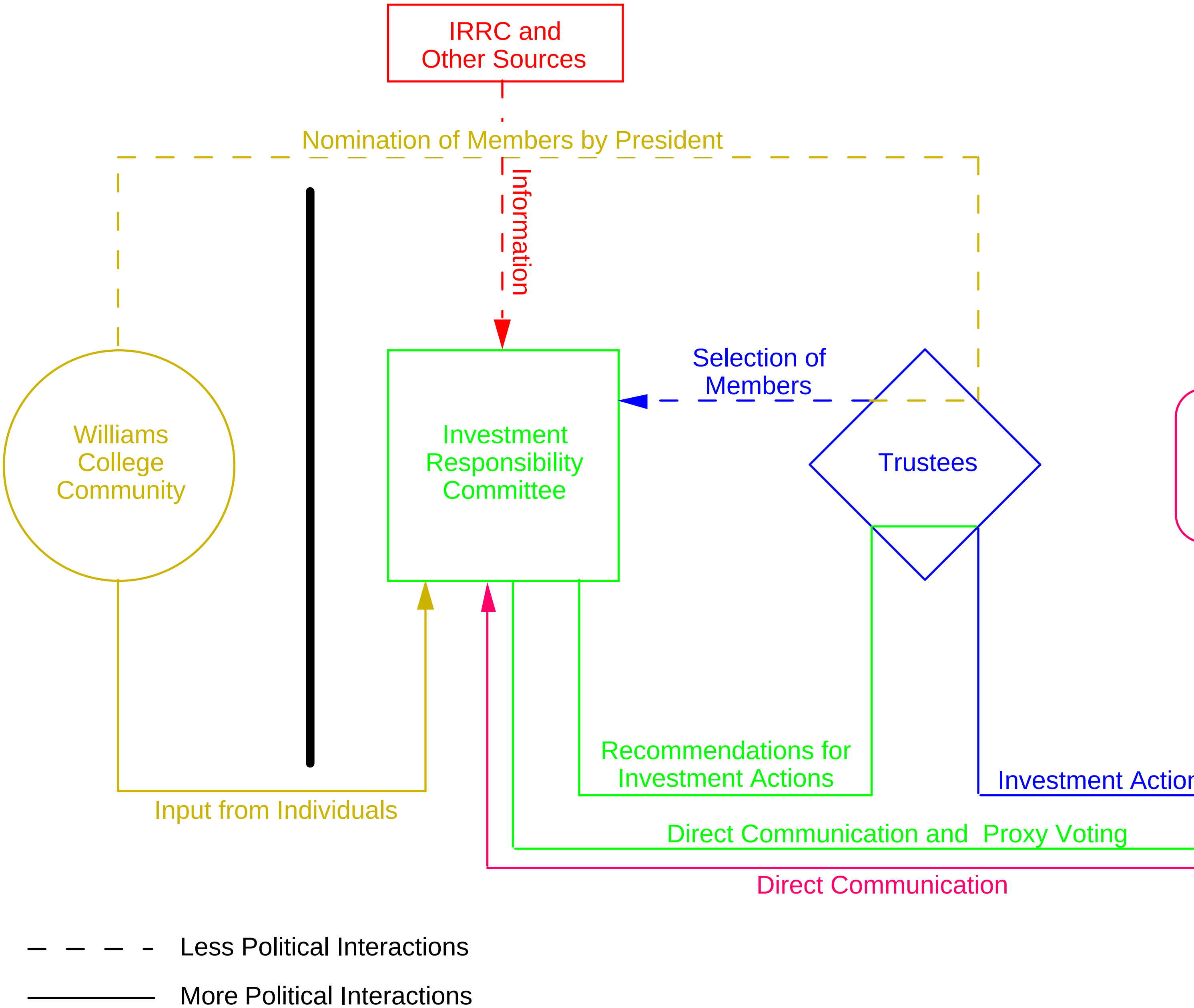

Fig. 3. Revised structure for the Williams College Advisory Committee for Shareholder Responsibility.

from the academic sphere of Williams, the institution, while maintaining and strengthening the connection between the members of the Community and the ethics. We do so by constructing a barrier between the Community and the Committee (vertical black line) which is bridged only by a limited set of interactions. These interactions are separated into two distinct sets according to level of politicization; these sets must remain differentiated. The remainder of the interactions, explained in the text below, set out to make an efficient, functional Committee.

How members are chosen

The current manner in which ACSR members are chosen should be changed to widen the gap between the politically charged ACSR and the campus. This division is designed to protect the free exchange of ideas that is at the heart of an institution of higher education. To accomplish this, members of the Committee should be nominated by the President and selected by the Trustees (or the Finance Committee of the Trustees): the President is close enough to the campus to keep the membership in line with the campus main stream and the Trustees are distant enough to make choices based on ability to analyze ethical arguments rather than personal values.[72] Committee members should be selected not on the basis of their personal politics, but rather on their ability to make careful, thoughtful ethical analyses that are firmly rooted in facts and just interpretation of the values of community members. This selection process is intended to avoid the development of constituencies for the Committee members. The members' positions are not representative of a part of the community but rather analytical and judicial.

Size of Committee

The number of committee members should be doubled to both lessen the influence of each member's personal political agenda and more widely distribute the work load of gathering and interpreting data about the firms in the College's portfolio.

Ability to do Research

Corporate responsibility is at its heart complex and ambiguous. In order to make wise decisions, the ACSR needs to have access to accurate and targeted information. While current

[72]The selection process will require nominees to present their ability to critically analyze ethical problems without undue personal influence. In the interest of practicality, this would probably amount to an essay.

reports from the IRRC are vital, we find that the revised ACSR will need access to someone with good research skills to track down information on specific companies and issues. A work study student might be appropriate for the task and might also serve as Committee secretary.

Openness to Community Input

The ACSR should actively solicit input from the college community, using the input to identify the values of the community and to determine what issues deserve specific attention. The ACSR described here relies on its members' perceptions of the community members' values to choose what issues should be addressed by investment actions. The Committee's identification of the College's moral character will also depend on its interaction with the college community; however, we believe that moral character is strongly influenced by institutional history and thus less variable. Therefore, the community's input on character will be less important than its input on specific political issues.

Availability of Information to the College Community

Information explaining the workings of the ACSR and detailing where and how the college invests its money should be readily available to the college community. Freely available information must form the backbone of any effort to encourage greater community participation. The ACSR should use innovative ways to reach different parts of the college community (i.e. the World Wide Web, the *Alumni Review*, etc.). Additionally, reports on the actions of the ACSR should be available to the college community.

Open Meetings

Meetings should be conducted in a fashion that is conducive to outside participation. They should be scheduled at times that are not likely to conflict with other schedules, and special steps should be taken to accommodate alumni that do not have ready access to the campus. In addition, to ensure a high level of participation, the ACSR should issue regular requests for input to the college community, as invitations to participate in meetings, regular "town (campus) meetings," requests for written input, etc.

Changes in Types of Actions Taken

The increased community participation described above will allow the ACSR to move beyond just reacting to resolutions proposed by other shareholders.[73] Issues identified by the community should be thoroughly investigated by the committee members and by the ACSR researcher. Investments or issues found to constitute serious ethical problems should be addressed by the committee. The type and extent of action taken should be a function of the severity of the ethical concern, the level of consensus about it within the College community and the investment type.

Increase in Direct Communication With Firms

The ACSR should regularly communicate with firms in which it has both a financial stake and an ethical concern. Managers should be well aware of the ACSR's concerns, and of how the ACSR proposes to solve underlying problems. Direct communication is of particular importance in cases where the college does not have the right to vote its shares (i.e. venture capital and bonds). In these cases, short of divestment, communication is the only means for the college to influence the behavior of firms.

Move Towards writing Shareholder Resolution

As the ACSR becomes better versed in the mechanics of shareholder action, it should begin to write shareholder resolutions. Shareholder resolutions should be the result of careful

[73]This shift towards proactive behavior is designed, in part, to help resolve the recurring problem of well-intentioned but poorly constructed shareholder resolutions. Members of the ACSR frequently vote against proxies not because they differ with its intent or ethical motivation, but rather because it is poorly worded or unclear in suggesting actions. The Williams community could do a public (and private) good by proposing resolutions itself because the authors (presumably members of the ACSR) would be capable analysts and authors.

and protracted analysis; the Committee will likely need legal counsel to write effective resolutions.

Consideration of Divestment in More Cases

While divestment is expensive and politically problematic, in some cases it is the only appropriate action. We recommend that ACSR consider divestment as a reasonable solution to protecting the College's ethical interest when firms are unresponsive to other actions. In the case of non-stock holdings, divestment is the only formal recourse the ACSR has and should thus be a viable option for action.

The Power to Propose Screens

If the ACSR identifies a sector of the economy that is, in the eyes of the college community, morally abhorrent it should have the privilege to design and propose a ban on purchases within that sector. The ban would be regularly reevaluated by the Committee and likely also by interested members of the College community.

Focusing Mechanisms

If the ACSR finds that is unable to give adequate attention to all the issues being raised (as will be the case, to at least some extent), it should focus its attention on some subset of the portfolio or ethical issues. The most logical ways to focus are on one type of investment (i.e., stocks, bonds, or venture capital) or on a specific issue (e.g., environment, tobacco, etc.).

Conclusions

The above recommendations, through their active recognition of the challenges of protecting university neutrality and defining the values of a diverse community, have the potential to improve the ability of the ACSR to serve the moral personality of the College and values of its community while bettering the separation of the academic from political. They do not take significant authority for financial decisions away from the College's investment advisors. We hope that they will give rise to a process of scrutiny and dialogue among the members of the ACSR, the Trustee and the College community as a whole, and that they will ultimately inform a change in the structure and functioning of the ACSR.

ACKNOWLEDGMENTS

Our membership on the Williams College Advisory Committee for Shareholder Responsibility and our discussions with its other members has been a primary inspiration for writing this paper. We would like to thank all the people who helped us grapple with these varied, complex issues. All organizational references here and in the footnotes are for identification purposes only. In particular: Roger Bolton, Harvey Carter, Doug Cogan, Stuart Crampton, Steve Gerrard, David Healy, Scott Klinger, Kai Lee, Michael McPherson, Stan Parese and Douglas Phillips. We also thank Barbara Fusco for helpful comments on the text.

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