“Let both [the wheat and the weeds] grow together until the harvest; and at harvest time I will tell the reapers, ‘Collect the weeds first and bind them in bundles to be burned, but gather the wheat into my barn’.”

Matthew 13.30
Chair’s Letter

This review covers the Ethical Investment Advisory Group’s (EIAG) activities from April 2013 to March 2014.

The year will be remembered for the media coverage of the Church Commissioners’ small and indirect investment in Wonga. This highlighted some misconceptions about ethical investment, and in particular that its objective is to achieve a morally perfect portfolio.

We addressed this concern directly in the presentation we were privileged to make to General Synod in February 2014, at which we looked particularly at the parable of the wheat and the weeds (Matthew 13.24-30), which we highlight on the cover of this report.

In our view, Christian ethical investment is about fulfilling responsibilities to beneficiaries and trying to make a positive difference in society. The Church’s national investing bodies seek to do the latter through engagement with companies, partnerships with other investors, and participation in public policy initiatives. In this way, they aspire to be part of the Church’s witness to the world.

We do take the view that it is inappropriate for the Church to provide capital to, or profit from, certain business activities, and the investing bodies take reasonable measures to avoid doing so, having regard to their financial resources and fiduciary duties.

Elsewhere, it is no more realistic to desire that they invest only in morally perfect companies than it is to desire that any of us should relate only to morally perfect individuals. In any event, such an objective would rather miss the point of the Gospel. It is not the healthy who need a doctor but the sick. When engaging with companies the investing bodies seek positive momentum not perfection. We usually only recommend divestment where we see no genuine desire for change.

Nevertheless, we are in the process of tightening our recommendations regarding investment restrictions, both in terms of the maximum percentage of restricted activities that may take place within permitted investments and our rules around pooled funds, which is where the investment in Wonga occurred. Pooled funds are often the only way to access certain asset classes and investment strategies – including venture capital, which can not only increase financial returns for investors but also serve society.

Even so, difficult choices remain and it is inevitable that the investing bodies will from time to time graze their knees as they interact with a complex and ambiguous business world. But in our view, it is better to stay on the field of play than to sit on the sidelines.

This year the EIAG has said goodbye to two of its long-standing members, Gavin Oldham and Ian Clark. Both have had a significant impact on the EIAG’s work, especially as advocates of
an increased emphasis on engagement. I thank them both for their tremendous contribution over many years. I welcome Bishop David Walker and the Rev Paul Boughton to the EIAG in their place.

The EIAG’s Secretary, Edward Mason, is also moving on to take up appointment as Head of Responsible Investment at the Church Commissioners. The creation of this new role indicates how the investing bodies continue to deepen and internalise their commitment to ethical and responsible investment. The EIAG is enormously grateful to Edward for his huge dedication and outstanding contribution to the work of the EIAG over the last five years.

New ethical investment approach to alcohol

The national investing bodies have traditionally reflected the Church’s concerns about the harms caused by alcohol misuse by avoiding investment in companies specialising in alcohol production or retail.

In 2011 the EIAG recommended a new approach designed to be truer to the Church’s view that alcohol is a gift from God that should not be abused – a policy that would put the Church on the field of play, not aside from it.

The new approach involves the EIAG recommending on a case by case basis which companies involved in alcohol are suitable for investment, according to whether they meet the EIAG’s standards of responsible practice. This puts supermarkets – now the UK’s main retailers of alcohol – under the ambit of the alcohol policy for the first time.

The EIAG completed its assessments of UK companies in 2013 – 14. Our recommendations are with the investing bodies and changes to the eligible investment universe will be announced in the autumn.

In the meantime we were pleased to tell Synod at our presentation in February that during our engagement all three major UK-listed supermarkets – Tesco, Sainsbury’s and Morrisons – had published alcohol policies newly acknowledging the potential for alcohol to cause harm.

James Featherby
Chair, Ethical Investment Advisory Group

EIAG lunchtime Synod fringe, Saturday 12 July 2014

The EIAG seeks active dialogue with Synod members on ethical investment and holds a fringe meeting at every York Synod. This year’s takes place at 1.15pm on Saturday 12 July in Room T006 in the Exhibition Centre. For those who have not yet registered, you are still welcome to attend. To do so, please email: eia@churchofengland.org
Between April 2013 and March 2014 the EIAG and its staff conducted engagement with 43 companies in face-to-face meetings or by video or tele-conference.

These companies comprised:

- Afren, AMEC, Anglo American, Antofagasta, Apache, Barclays, BASF, BHP Billiton, BP, Centrica, Chevron Corporation,

*Companies excluded from investment and not held by the national investing bodies.

Themes covered in our engagement meetings included: adult entertainment, arctic drilling, banking ethics and practice, breast milk substitutes, carbon emissions management and reporting, corporate governance, country-specific risks, climate change, executive remuneration, genetically modified organisms, high interest rate lending, human rights, lobbying, oil sands, pharmaceutical ethics, relationships with communities, responsibility in the marketing and retailing of alcohol, safety/operational risk, sustainability reporting and tax.

We concluded our intensive engagement with Barclays last summer but will remain in close contact, seeking on-going evidence of progress towards a more ethical culture.

We were delighted that the Commissioners were part of the consortium that bid successfully for the RBS branches in England and Scotland that will become part of a new challenger bank branded Williams & Glyn’s. We supported the Commissioners as they worked on ethical principles with their bid partners and following the success of the bid have maintained close and fruitful dialogue with the new bank’s executive team.

An important engagement success was achieved at the start of 2014 by church investors working through the Church Investors Group: after dialogue lasting several years, a major telecommunications company informed the CIG that they had, with immediate effect, ceased to promote pornographic material on their handsets in the UK.

**Engagement on climate change**

Every year, CCLA engages on behalf of the Church Investors Group with a group of UK companies on climate change. Companies are chosen for engagement if they do not provide information about their approach to climate change to CDP (the investor backed sustainability initiative formerly known as the Carbon Disclosure Project) or if their approach significantly lags behind that of their peers. In 2013, a remarkable 72% of companies subject to engagement improved their CDP score.

The national investing bodies are also part of a CCLA-led collaborative project – which participants are calling ‘Aiming for A’ – to encourage the major UK-listed carbon-intensive companies to achieve the highest possible CDP rating on climate change performance, an A rating. The initiative is backed by investors with over £100bn of assets. Investors have held private meetings with companies and are now attending AGMs in the 2014 AGM season to draw the initiative to the attention of the companies’ boards.
The EIAG Secretariat conducts voting at company general meetings on behalf of the Church Commissioners and Church of England Pensions Board in line with corporate governance and executive remuneration policies recommended by the EIAG and adopted by the investing bodies. CCLA votes on behalf of the CBF Church of England Funds against the same policies, but through a different proxy-voting provider for UK-listed companies to facilitate local ecumenical co-ordination.

This is a significant effort involving voting on over 30,000 resolutions at approximately 3,000 company meetings. It is an intrinsic part of good investment stewardship.

Problems in executive remuneration practice in the UK continue to be signalled by the investing bodies, who supported only 30% of UK executive remuneration reports in 2013.

Every year the EIAG writes to approximately 300 of the largest UK-listed companies to advise Chairs of Remuneration Committees of the views of the national investing bodies on good executive remuneration practice.

Further information about voting is published by the investing bodies.

The Stewardship Code

Since the financial crisis, the Government has been trying to encourage all asset owners and asset managers to act as stewards of their investments through both engagement and voting, as church investors seek to do.

The Government introduced a Stewardship Code in 2010 and made it compulsory for asset managers to publish Stewardship Code statements indicating the extent to which they complied with the Code’s principles. CCLA published a statement covering the CBF Church of England Funds.

A second version of the Stewardship code was launched in 2012. This time the Government encouraged asset owners to publish statements as well. Both the Commissioners and the Pensions Boards have published Stewardship Code statements.

The investing bodies’ Stewardship Code statements are published on their websites and can also be accessed via the Financial Reporting Council’s website.

While engagement with companies is an important component of an ethical investment response to climate change, it is not sufficient. We believe that engagement with policy makers is even more important: only policy makers can re-frame the market to disincentivise the use of fossil fuels. We do public policy work through the European Institutional Investors Group on Climate Change (IIGCC).

The IIGCC engaged intensively with the European Commission in 2013-14 when the Commission was considering whether to recommend to EU member states a greenhouse gas reduction target for 2030 of 35% from 1990 levels or a more ambitious reductions target of 40%. The Commission recommended 40%. Engagement by long-term investors acted as an important counterweight to lobbying by the energy intensive industries.
Policy advice

In the wake of the Wonga controversy, the Archbishop of Canterbury asked for aspects of ethical investment policy to be reviewed.

The EIAG has completed a review of the revenue thresholds used to determine whether companies should be excluded from investment on account of their involvement in business activities about which the Church has ethical concerns.

The revenue thresholds used to exclude companies from investment on account of their involvement in tobacco, gambling, high interest rate lending and human embryonic cloning have all been reduced from 25% of turnover to 10% of turnover.

This change would not have prevented the exposure to Wonga because the exposure arose in a pooled fund, which could not be screened in the way that direct holdings are screened. However, it represents an important tightening of ethical restrictions. None of the EIAG’s investment exclusions now use a revenue threshold higher than 10%.

The other aspect of ethical investment under review following the Wonga controversy is policy on pooled funds. The EIAG has not published a pooled funds policy before – it has only offered private guidance to the investing bodies – but will publish a full policy in 2014, based in part on the parable of the wheat and the weeds (Matthew 13.24-30), as soon as it has been agreed by the investing bodies.

A new policy will also be published in 2014 on Business and Engagement. The investing bodies’ Statement of Ethical Investment Policy will be updated.

A review of the EIAG’s policy advice on human embryonic stem cell research remains on the work programme, but will not commence until 2015.

One new policy was published in 2013-14, specifying an exclusion of manufacturers of non-military firearms which continue to cause huge loss of life, particularly in the United States.

Review of climate change policy

As we reported last year, the EIAG’s major piece of policy work at present is the development of updated and more detailed advice for the national investing bodies on climate change.

This work was given added impetus in February when General Synod overwhelmingly passed a motion – 274 for, one against – calling for investment policy to be aligned with the Church’s theological, moral and social priorities on climate change.

The EIAG has committed to publish a new policy in 2015 once it has been agreed by the investing bodies.
The EIAG believes that excellence and impact in its work are best served through working in partnership with church investors in the UK and internationally, and with the wider responsible and sustainable investment community.

The EIAG and national investing bodies participate actively in the work of the Church Investors Group (CIG). In November 2013, the EIAG Secretary was elected as vice-Chairman of the CIG, serving alongside Bill Seddon, Chief Executive of the Central Finance Board of the Methodist Church, who was elected Chairman. This will further strengthen the close relationship between the Church of England and Methodist Church on ethical investment. Our co-operation is supported by a reciprocal arrangement by which we attend the meetings of each other’s ethical investment advisory committees.

The CIG continues successfully to deepen its relationships with church investors internationally, with new partnerships formed in 2013-14 with the US Interfaith Center on Corporate Responsibility, the Norwegian Church Endowment Fund and the Evangelical-Lutheran Church in Bavaria.

The EIAG joined a number of new engagement and advocacy coalitions with responsible investors beyond the church investment community. These included an engagement coalition on corporate tax practice and an advocacy coalition for transparency in supply chains after the Archbishop of Canterbury and Pope Francis came together in March 2014 to give their backing to the Global Freedom Network, a major new initiative in the effort to eradicate modern slavery.

An important new commercial partnership was established with MSCI ESG Research who are conducting ethical screening of a universe of 9,000 listed companies for the investing bodies, as well as providing research on corporate performance on ESG (environmental, social and governance) issues.

EIAG constitution

The EIAG adopted a new constitution in January 2014 intended to improve its governance and effectiveness, for example setting a maximum term of nine years for non-executive members in line with our expectations of maximum service by non-executives on corporate boards. The new constitution is published on the EIAG’s website.

Feedback

We welcome feedback on this annual review as well as queries from within the Church about ethical investment. Please contact eiag@churchofengland.org
The Ethical Investment Advisory Group of the Church of England provides ethical investment advice to:

- **The Church Commissioners for England** who support the Church’s ministry, particularly in areas of need and opportunity, and meet historic pension liabilities. They are represented on the EIAG by the Rt Rev David Walker, the Bishop of Manchester (non-executive member), the Rev Canon Professor Richard Burridge (non-executive member and Deputy Chair) and Andrew Brown (Secretary of the Church Commissioners).

- **The CBF Church of England Funds** collective investment schemes managed by CCLA Investment Management Ltd in which Church of England parishes, dioceses, schools and church charitable trusts invest. CCLA is owned by its church and not-for-profit clients. The CBF Funds are represented on the EIAG by trustee director, the Rev Canon Edward Carter (non-executive member), and Michael Quicke (Chief Executive of CCLA).

- **The Church of England Pensions Board** which provides retirement services (pensions and housing) set by the Church of England for those who have served or worked for the Church. The Board is represented on the EIAG by Pensions Board trustee the Rev Paul Boughton (non-executive member) and Bernadette Kenny (Pensions Board Chief Executive).

The EIAG has representatives from other parts of the Church to provide broader expertise and insight.

- The General Synod is represented by Jenny Humphreys (non-executive member).

- The Mission and Public Affairs Council is represented by the Rt Rev Dr Lee Rayfield, Bishop of Swindon (non-executive member), and the Rev Dr Malcolm Brown (Director Mission and Public Affairs).

- The Archbishops’ Council is represented by Paul Boyd-Lee (non-executive member).

The EIAG has three further non-executive members. There are two co-opted non-executive members: Richard Harvey, Chairman of PZ Cussons Plc, and Elizabeth Haigh, portfolio manager at, and founder of, Rathbone Greenbank Investments. The EIAG has an independent non-executive Chair, James Featherby, a former partner of over 20 years’ standing at Slaughter and May. Only non-executive members of the EIAG may vote at EIAG meetings.

The executive Secretary to the EIAG is Edward Mason and the Ethical Screening and Stewardship Manager is Chris Anker. They can be contacted at:

- e-mail: eiat@chuchofengland.org
- telephone: 020 7898 1757
- mail: Investment Department, Church House, Great Smith Street, London SW1P 3AZ
- www.chuchofengland.org/about-us/structure/eiag

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The EIAG makes recommendations on ethical investment policy. The legal responsibility for managing the Church’s investments rests with the investing bodies. These bodies all have a moral and legal responsibility (known as ‘fiduciary duty’) to further the interests of their beneficiaries. While mindful at all times of beneficiaries’ need for financial returns, the investing bodies seek to align their investment policies with the ethics of the Church by acting on the recommendations of the EIAG.

The EIAG positively recommends investment in companies with responsible employment practices, best corporate governance practice, conscientiousness with regard to human rights, sustainable environmental practice and sensitivity towards the communities in which the business operates.

The EIAG recommends against investment in any company involved in indiscriminate weaponry. It recommends against investment in companies involved in conventional weapons if their strategic military supplies exceed 10% of turnover.

The EIAG recommends against investment in any company that derives more than 3% of revenues from the production or distribution of pornography and against investment in any company, a major part of whose business activity or focus (defined as more than 10% of group revenues) is tobacco, gambling, non-military firearms, high interest rate lending or human embryonic cloning.

A new policy on alcohol is in the process of implementation under which companies deriving more than 5% of their revenues from alcoholic drinks are only eligible for investment if they meet EIAG standards for responsible marketing and retailing.