Ethical Investment and the Challenge of Corporate Reform

A critical assessment of the procedures and purposes of UK ethical unit trusts.

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Abstract

There are 30 ethical investment funds in the UK, managing £1.3bn of assets on behalf of 150,000 investors. Just 13 years ago there were none. One goal of ethical investment is to allow people to invest in the stockmarket while not supporting companies with unethical practices. The other is to persuade such companies to reform. I offer a detailed case-study of the leading ethical fund, Friends Provident Stewardship, which describes the 'screening' procedures used to achieve these two goals. Ethical funds are fairly effective at the first goal, but they are not good at persuading companies to reform. One reason for this lack of success is that the two purposes of ethical investment can frequently conflict. The procedures used by funds to enable people to avoid investing unethically are not well suited to the pursuit of corporate reform. In order to rise to the challenge of corporate reform, ethical funds need to become better at engaging with companies and persuading them to change. This may require a significant shift in priorities from 'screening' to engagement. This thesis offers evidence in support of these claims, and makes a case to justify this shift in priorities.

Contents

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Introduction

This thesis is about ethical investment in companies listed on the stockmarket. The first ethical unit trust, Friends Provident Stewardship, was set up in 1984. There are now thirty ethical funds in the UK, investing £1.3bn on behalf of around 150,000 individual investors. Ethical investment is one of the fastest growing sectors of the unit trust market. Ethical funds respond to two problems which we will call the ‘corporate harm’ problem and the ‘investment ethics’ problem.

From the point of view of ethical investment, corporate practice is frequently harmful to people, animals and the environment. A typical list of ethical concerns of ethical funds might include ‘alcohol, animal testing, gambling, greenhouse gases, health and safety breaches, human rights abuses, intensive farming, military...involvement, nuclear power, ozone depletion, pesticides, pornography, roads, South Africa...third world concerns, tobacco, tropical hardwoods, water pollution’ (EIRIS, 1996a:5). These topics relate to corporate practice in a variety of different ways. Not everyone would agree that all of these issues relate to examples of harm or unethical practice. However, many people would probably accept that at least some of these topics relate to genuine ethical problems and forms of harm. They would also accept that these forms of harm are partly caused, or sustained by the activities of companies. While companies are the basis of the world economy, and so may be regarded as doing considerable good, these examples illustrate that they also contribute to some of the more pernicious forms of harm in the world today. This is the corporate harm problem.

This problem is not the only ethical problem from the point of view of ethical investment. For investors, in particular, there is also a secondary ethical problem. As the Friends Provident Stewardship marketing material puts it:

> ‘Through their investments, many people may inadvertently support practices which they would find objectionable: pacifists may support the arms trade, conservationists may contribute to environmental destruction, religious people may support oppression and exploitation, non-smokers may help the tobacco industry, and vegetarians may invest in factory farming.’ (Stewardship, 1995:1)

While the corporate harm problem is a problem that affects everyone, investors have another more personal problem. By investing in a company that is engaged in unethical practices, ethical investors believe that they may be regarded as supporting these practices. It is a shared understanding of the ethical investment community that this makes investment in such companies unethical. This investment ethics problem is secondary to the corporate harm problem in that it would not exist if corporate practice was not considered harmful or unethical.

The two primary goods pursued by ethical funds are to offer a response to each of these two problems. If ethical funds are successful at addressing the investment ethics problem, it becomes possible for investors to invest in the stockmarket without doing injury to their personal ethical convictions. If ethical funds can offer a significant contribution to persuading companies to adopt more ethical and environmentally sustainable practices, they deserve widespread interest. The purpose of this thesis is to assess to what extent ethical funds can offer solutions to these problems, and to consider how they might improve their effectiveness.

In order to achieve this purpose a number of questions need to be asked. How do ethical funds enable investors to avoid ‘supporting’ companies with unethical practices? Who decides what counts as unethical? How do they decide? Are their procedures adequate from an ethical point of view? How exactly might investors be considered to ‘support’ companies with unethical practices? How significant is this ‘support’ as a ethical problem? What methods do ethical funds use to address the corporate harm problem? What evidence is there that these methods work? Can ethical funds hope to address both the corporate harm and investment ethics problem at the same time? If not, which problem should have priority? If the corporate harm problem and the investment ethics problem are serious ethical problems, and if ethical investment might offer a solution to them, then it is important that we are able to answer these questions.

Unfortunately, these questions have not yet been addressed in a concerted manner by the academic community. While there is a modest literature on ethical investment, there is very little work in business ethics or elsewhere which considers these questions in detail. One problem is that to answer these questions properly one needs a rather detailed understanding of the procedures of ethical funds. While the literature contains certain clues, nowhere does it offer an account which is sufficiently detailed to provide the answers we need. Without a detailed understanding of how ethical investment is practised it is difficult to engage critically with its approach, and easy to make mistakes.[1]

The contribution made by this thesis

This thesis is an attempt, firstly, to provide the detailed descriptive research necessary to address these questions, and secondly to attempt to answer them. In the pursuit of the first goal I have engaged in a detailed case study of the first and by far the largest ethical fund in the UK, Friends Provident Stewardship. In order to produce this case study I have interviewed a number of Friends Provident staff, attended private committee meetings, and read various confidential materials. I am the first researcher to have been given access to Stewardship in this way, and Friends Provident have commented heavily on my drafts. I have also completed a wider survey of ethical investment, during which I have talked to some 60 people involved in various ways with ethical investment. My focus in this descriptive work is on the procedures used by ethical funds to make ordinary unit trusts into *ethical* unit trusts; the procedures used to address the investment ethics and corporate harm problems. My case study of Stewardship, and my wider survey appear in Chapters 3 and 4. I consider the new facts my survey reveals to be one of the original contributions this thesis makes to the study of ethical investment, and to business ethics more generally. In Chapter 1, I describe my programme of research and the qualitative methods I have used in this work.

However, this thesis is not simply a work of description, it is also a work of business ethics. And like much work in business ethics, it seeks to engage critically with a particular domain of business practice. I will be making arguments about the ethical assumptions of ethical funds, and offer criticisms of their procedures. This means that I must set out my approach to ethics. I have attempted to do this in Chapter 1. My attempt to make use of previous work in business ethics for this purpose has been fruitful, but one particular problem has emerged. Conventional approaches to business ethics follow the philosophical ‘applied ethics’ model. This uses philosophical ethical theories as the

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[1] Anderson et al., (1996), provide the most substantial critical engagement with ethical investment in the UK to date, unfortunately their work is dogged by significant misunderstandings about the nature and practice of ethical funds. See Chapter 7 for a detailed discussion.

basis for justifying ethical claims. Lacking a philosophical training, it is difficult for me to make use of this model. Instead I have tried to adopt another approach to justifying ethical claims. Briefly, I have sought to borrow the methodological approach developed by some recent work in ethical and political theory: the ‘interpretive’ approach to ethics recommended by Michael Walzer (1983), Alasdair MacIntyre (1994) and others. This approach seeks to justify ethical claims on the basis of interpretations of the shared understandings of particular traditions and communities. For MacIntyre, goods are internal to human practices (1994:183ff). So the most important shared understandings are understandings about the goods internal to particular practices. I have sought to justify my ethical claims against my interpretations of the shared understandings of the ethical investment community. In particular, I have sought to justify my arguments with regard to my interpretation of the primary goods pursued in the practice of ethical investment. I discuss the issues arising from this approach, and my attempt to develop it in more detail in Chapter 1. I hope that this attempt may be considered to be a modest methodological contribution to the business ethics literature.

On the basis of this method, and on the basis of my survey work on ethical funds, I believe that I am able to offer a number of critical insights into the practice of ethical investment. For example, the distinction made above between the corporate harm problem and the investment ethics problem is a new one, so is the distinction I make in Chapter 7 between ‘investor-led’ and ‘deliberative’ ethical funds (see p.164). My arguments are partly in the form of critical responses to the work of the relatively few researchers who have already written about the subject of ethical investment, and partly arguments of my own, which I believe are new to the field. There have been several dozen academic papers on the subject of ethical investment and perhaps a dozen books. The majority of the papers concern ethical investment in the US. The majority of the books are practical guides to ethical investing rather than academic studies. As I claim in my literature review, in Chapter 2, very few of them attempt to describe or criticise the procedures of ethical investment in the way I do. The procedures and purposes of ethical funds, particularly those in the UK, are therefore a considerably open field of study, partly, no doubt, because ethical investment is a rather recent phenomenon. This makes the task of ‘advancing the study’ of my subject rather easier than it would be in a mature and crowded field. However, it makes it harder to show clearly the respects in which this work advances study of the subject. In an old and well established field, most positions have been taken, most claims have already been made, attacked and defended, often many times over; so highlighting what is new about one's contribution is a matter of differentiating one's own claims from the pre-existing literature. However, when the subject area is open and unexamined, a large number of the claims one makes will not have been made previously in the academic literature. This alone is not an indication of merit. New claims might be intelligent, well founded claims, but they might also be stupid, ill founded ones. I hope at least some of mine fall into the former category.

Limitations to the scope of the thesis

In order to do justice to the particular issues and problems with which I am concerned I have been forced to limit the scope of this thesis in a number of important ways. I constrain myself to one particular part of ethical investment: the ethical investment unit trusts (and, occasionally, investment trusts) which invest in the stockmarket and offer retail investment products for sale to the public. This excludes 'alternative' ethical investments such as Shared Interest and Triodos Bank, as these do not invest in the stockmarket; and it also excludes institutional ethical investments such as the funds of the Central Finance Board of the Methodist Church because it does not retail services to the public. Henceforth, I shall generally use the term 'ethical funds' to refer only to the funds which satisfy this scope. The issues raised by a discussion of ethical funds have a bearing on other forms of ethical investment, particularly other kinds of ethical stockmarket investment, but I will not address this explicitly. A number of the issues which ethical funds consider are environmental issues, rather than general ethical ones. Indeed a number of funds market themselves as environmental, or 'green' funds, rather than as ethical ones. However, for reasons of simplicity, and for the reason that environmental issues have an ethical component, in most cases I will use the term 'ethical funds' to include environmental funds.

This thesis will also be limited to a particular range of questions about ethical funds. It will concentrate on questions about the ethical procedures and the goals of ethical funds. It will not consider at any length financial issues - such as the difficult question of whether ethical investments underperform relative to other conventional investment funds.

In order to concentrate on description and criticism of the procedures used by ethical funds, this thesis will also not consider questions about the validity of various aspects of the ethical investment enterprise. One aspect of ethical investment which I will not be considering in detail, for example, is its views on the ethics of corporate practice. This is a central topic for ethical funds. Adopting sensible criteria on which to count corporate activities ‘ethical’ or ‘unethical’ is a central purpose of many of the procedures of ethical investment. There are many difficult and important issues to be discussed here. For example, many ethical funds have criteria on tobacco, alcohol and arms manufacture. There is little doubt that these products can be harmful. Should the companies that make them be considered culpable for this use, or misuse? There are many difficult issues here.[2] While I touch upon these issues in Chapter 8, my main concern in this thesis is not the issues themselves, but the more general question of whether the procedures used by ethical funds are adequate for giving these issues sufficient consideration.

Nor will I challenge the premise that many companies frequently act in ways which may be regarded as unethical. This premise is a central understanding of ethical funds, and it is constitutive of ethical investment practice. The methodological approach I have adopted implies that to some degree I should work within the frame of understandings shared by the ethical investment community. I will therefore assume that this premise is correct, while simply acknowledging that this assumption can be challenged. For example, Milton Friedman has famously argued that

> ‘there is one and only one social responsibility of business - to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception and fraud.’ (Friedman, 1962:133).

On Friedman’s argument, apart from questions of deception and fraud, companies are excluded from standard ethical evaluations. For example, on this argument, so long as it is profitable, and legal, manufacturing landmines and selling them indiscriminately to foreign regimes may be a perfectly ethical thing for company to do. This raises a large number of interesting and important issues which will not be considered in this thesis.[3]

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[2] See Sorell and Hendry (1994:59-61) for examples of these issues.

[3] See de George (1990) for objections to Friedman’s arguments.

Another premise of ethical investment is that it is ethically desirable for investors to use their power as shareholders to persuade companies to adopt more ethical practices. There have been some objections to this. It has been argued for example that shareholders should not impose their values on other shareholders, or the business as a whole (Sternberg, 1994:261). I will consider these objections briefly in Chapter 2, but in general, I will work within the shared understanding of the ethical investment community which considers that it is desirable for investors to seek to persuade companies to adopt more ethical, and less harmful policies.

To deal adequately with each of these important matters would require detailed and lengthy consideration which would limit the ability of this thesis to achieve its primary goal, which is to describe, and critically examine the ethical issues surrounding the procedures and purposes of ethical funds. This is a thesis about how ethical funds go about their business; their conceptions of the ethical problems and challenges raised by investment in the stockmarket; the efficacy of their responses to these problems and challenges; and this thesis is about how these responses might evolve in the future. This thesis is not about whether ethical funds are financially attractive, whether they have a right to be going about their business at all, or whether they have adopted adequate substantive ethical positions on each of three dozen ethical and environmental issues.

The main claims of this thesis.

To conclude this introduction, I will summarise the main claims I will be making in the rest of this thesis.

The practice of ethical investment is directed towards the pursuit of two primary goals: providing a solution to the investment ethics problem, and addressing the corporate harm problem. The response ethical investment offers to the investment ethics problem is to provide ethically screened investment funds. These avoid investing in companies with unethical practices and, instead, invest in companies which can be regarded as making a positive contribution. The response ethical investment offers to the corporate harm problem is less clear. Some argue that as ethically screened funds grow, they will deny capital to companies with unethical practices, and so hurt their share prices, while supporting the share prices of ethical companies. They hope that this will send signals through the stockmarket incentivising companies to adopt better practices. Others seek to address the corporate harm problem more directly, by engaging with companies, policy makers, and the public at large in order to persuade companies to change.

I will claim, in Chapter 5 that ethical funds offer a simple and reasonably effective solution to the investment ethics problem. The criteria the funds use are effective at avoiding companies engaged in certain kinds of ethically controversial practices; they are applied rigorously and are based on good information. This is a considerable achievement. For the founders of the first UK ethical fund in 1984, the existence, 12 years on, of 300 rigorously researched ethical criteria, applied by 30 ethical funds to screen £1.3bn of investment assets would have been regarded as an inconceivably successful start. However, while in general ethical funds offer a fairly effective solution to the investment ethics problem, I note one or two limitations of this solution. I also argue that the level of explanation by ethical funds of their policies could be higher.

I claim in Chapter 6 that, on the other hand, the principal mechanisms by which ethical funds claim to persuade companies to reform are *not* very effective. The idea that ethical funds can deny capital to companies with unethical practices and hurt their share prices is, in general, misconceived. The attempt to engage with companies and policy makers in order to persuade them to change is a promising approach, but it has not been widely adopted, and where it has, it is not pursued as vigorously as it might be. The lack of success in this area is perhaps the most significant challenge facing ethical funds, because addressing the corporate harm problem is one of their primary goals.

In Chapter 7 I claim that in order to decide what is ethical and unethical about corporate practice; in order to produce the ethical arguments which are needed to engage effectively with companies to persuade them to change; and in order to contribute to the development of wider traditions of ethical thinking about business practice, ethical funds need to engage in sophisticated ethical deliberation. While I reject the arguments of Anderson et al. (1996) that suggest that ethical funds do not even deserve the name ‘ethical’, I argue that most funds are not in a position to engage in ethical deliberation. Some funds, however, have made progress in this area but, I argue, are limited in various important respects.

In Chapter 8 I argue that there may be important conflicts between the screening approach, used to address the investment ethics problem, and the attempt to develop the effective procedures of engagement and deliberation which are necessary to address the corporate harm problem. If ethical funds are to become more effective at addressing the corporate harm problem, I argue that they may need to shift their emphasis from screening to engagement and deliberation. I then attempt to justify such a shift by raising questions about the conception of the investment ethics problem used by ethical funds, and by offering an alternative conception of the responsibilities of investors as shareholders.

If ethical investment is to achieve its full potential, it must be effective at pursuing both of its primary goods. It must both solve the investment ethics problem and address the corporate harm problem. In this thesis I claim that ethical investment has some way to go before it is very effective at the latter. I argue that addressing this challenge is a demanding task that may require a substantial shift in the practice of ethical investment. I then offer a basis on which such a shift can be justified. In so doing, I hope to establish corporate reform as the foremost challenge for ethical funds.

1. Methods

1.1 Ethical method

This thesis does not comfortably belong to any traditional academic discipline such as sociology, economics, psychology or philosophy. It can however, be regarded as falling into the newer field of academic study, business ethics. The thesis falls into the domain of business ethics because of its subject matter and because of the kind of analysis it does. Its subject area, the practice of ethical unit trust investment, is a particular ethical activity in the business sphere, and so is properly a topic of business ethics. Its analytical approach is to provide a critical evaluation of ethical investment practice. Critical evaluation has an ethical component, and so brings this work within the fold of business ethics.

The fact that this thesis falls under this newer academic area rather than the old established ones poses a problem. Traditional academic disciplines have their canonical texts, approved methods, and a range of disciplinary journals offering examples of how the discipline should be 'done.' This disciplinary fabric provides a conventional framework for theses within these disciplines. This framework offers a range of approved methodological and theoretical approaches. Business ethics does not have such a disciplinary fabric. This is partly because it has only recently been regarded as an academic discipline. Of course business ethics has been discussed since business began (McHugh, 1988:3), but only in the last quarter century or so has the subject become part of institutional academic study. Indeed, on some accounts, business ethics as an academic discipline is even more recent - as little as 15 years old (Solomon, 1991: 354). Another reason why business ethics may lack a disciplinary fabric is that it has attracted academics from many different disciplines - philosophy, sociology, theology, management studies, law, policy studies, economics, history, psychology to name a few (McHugh, 1988:16). There is therefore a lack of agreement about theory and method. While there are a growing number of textbooks on business ethics (Beauchamp and Bowie, 1983; de George, 1990; Harvey, 1994; Sorell and Hendry, 1995), there are no canonical text books on theory or method in the way that there are in economics and sociology, for example. This means that a thesis in this new discipline has a harder job to do in order to establish its methods. Nevertheless, the attempt to establish the empirical and analytic methods to be used in this thesis is the subject of this chapter.

1.1.1 Business ethics

I have said that this thesis can be regarded as a work of business ethics because it studies ethical investment funds which invest in businesses on the basis of ethical considerations; and because it seeks to engage critically with the ethical practices of these funds. One piece of evidence which supports the argument that ethical investment may be regarded as a proper topic of business ethics is that it has been considered at some length in a few significant works on business ethics (De George, 1990:173-180; Sorell and Hendry, 1994:129-135). If this thesis can be regarded as a work of business ethics, then what can I learn from business ethics about my approach to theory and method?

As I have indicated, business ethics is a recent arrival in the academy. It has not established a widely approved theoretical or methodological framework. However, there are many things to learn from the literature. For example, there have been several useful attempts to divide business ethics into different domains, which will allow me to locate my thesis more precisely within the literature. Solomon (1991) talks of micro-, macro-, and molar-business ethics. Micro-business ethics is concerned with, for example, the rules for fair exchange between individuals; macro-business ethics is concerned with the 'institutional or cultural rules for commerce in an entire society'; and molar business ethics is concerned with the 'basic unit' of contemporary commerce, the corporation (1991:359). Another different way of making the division is Sorell and Hendry's distinction between 'narrow' and 'broad' business ethics.

> 'A code of ethics for a firm is narrow when its provisions concern only those employed in the business or, in addition, only groups who are directly concerned financially, such as shareholders or current customers. By contrast, a code of ethics for a business can be said to be broad when it declares responsibilities to all those mentioned by the narrow code as well as to the community or society in general, or to the environment.' (Sorell and Hendry, 1994:28).

While this definition is couched in terms of codes of ethics, Sorell and Hendry apply it widely to business ethics, and the distinction is an organising feature of their text, *Business Ethics* (1994).

In terms of Solomon's categorisation this thesis sits within 'molar' business ethics, and in terms of Sorell and Hendry's definition, it sits within narrow business ethics. It is the study of the procedures of a particular set of business institutions: ethical unit trusts, and the companies which manage them. However, ethical unit trusts are not ordinary companies, and the main reason why business ethics is interested in them is not as conventional companies, but in their role as a special kind of shareholder in ordinary companies. Of course ethical unit trusts and the companies that manage them themselves have stakeholders. Unit trusts have unit holders, and trustees appointed by their fund managers. Investment trusts have shareholders and directors. The fund management companies that manage unit trusts have employees, directors and shareholders (or members in the case of the mutual insurance companies which run many ethical funds). For the most part the relationship between these stakeholders and unit trusts is not the concern of this thesis. However we will be interested in the relationship between unit holders and their unit trusts, and in particular with the way ethical funds serve as a conduit by which investors can indirectly invest in companies. But in general the interest of this thesis in ethical investment is in the relationship between ethical funds as shareholders and the companies they invest in.

While this thesis is interested in ethical investment as a topic in narrow business ethics, ethical investment as an activity is frequently concerned with broad or macro-business ethics issues. While some ethical criteria used by ethical funds relate to narrow issues such as corporate employment policy, many of the criteria relate to broad issues like the relationship between corporate practice and the environment, animals, warfare, and the health and well-being of communities. Indeed the corporate harm problem I described in the Introduction, is a problem as much concerning these broad business ethics issues as it does the narrow ones. While these broad issues will always be in the background, this thesis will not consider broad business ethics questions, but questions about the role of ethical funds, and the relationship between ethical funds and companies.

Another kind of distinction made by Sorell and Hendry which is useful for locating my proposed approach to business ethics is the distinction they make between 'essentialist' and 'generalist' business ethics (1984: 8-9). Essentialist business ethics seeks to comment on the morally significant characteristics that are common or essential to all businesses. Generalist business ethics on the other hand 'keeps the variety of business activity...to the fore' seeking to build a 'composite picture...drawn from the moral characteristics that are peculiar to different branches of business' (1984:9). Sorell and Hendry say that both these approaches seek to get beyond particular businesses, or sectors of business, to business in general. How does my approach fit with this? Well it is certainly not essentialist, and is more akin to the generalist approach. However, it does not seek to get beyond the particular business sector of ethical investment. One might risk introducing a third category of 'particularist' business ethics which seeks not general lessons for business as a whole, but seeks to comprehend and engage with the peculiar problems of a particular business sector.

Sorell and Hendry offer a metaphor to show the difference between essentialist and generalist business ethics. The metaphor refers to the impression one gets of a town from two kinds of photography. An essentialist perspective, on their metaphor, is one derived from an aerial photo of a town, and a generalist one arises from viewing a collection of photos of various individual buildings and landmarks. The latter approach 'leaves out a great deal and is openly selective, but it does show a few important things in life-like detail. The aerial photograph, on the other hand, while it includes everything, is unlikely to give an impression of life on the ground. This thesis is certainly not an aerial photo. However, it is more focused than a generalist study of a town. It is in the sense a set of photographs of an individual building, many of them taken from the inside, frequently with the permission and help of the inhabitants. It is not the architectural plan of the building, it does not reveal the building's essence but instead uses several photographs to give a feel for the place, the people who live in it, and its day to day operation. Like Sorell and Hendry's generalist approach, it gets its 'ethical content...its sense of what is morally problematic and what is not, of what is right and wrong' (1984:10) from a range of different sources including many of the ones they list (interest groups, newspapers, television, academic literature etc.), but mostly it gets its sense of what is important from the views of the people who live in and visit the 'building' - the ethical investors, the advisors and managers who run and sell ethical funds, and the various commentators on ethical investment.

In delimiting my field of study, and in other ways, the business ethics literature is useful in my attempt to establish the theoretical and methodological framework for this thesis. But business ethics is of limited use, on its own, for answering the most important question that I need to address in this chapter. While the first half of this thesis is a work of description, the second half is a critical assessment of the ethical approach of ethical investment. What is the ethical basis on which I should engage in such ethical criticism? One way of approaching this question is to determine on what ethical basis business ethics in general seeks for its ethical claims. One common way of conceiving of business ethics is as a part of the literature of ‘applied ethics’ (Beauchamp and Bowie, 1983:7; McHugh, 1988:3; Solomon, 1991:354). The term ‘applied ethics’ implies a particular way of going about ethical thinking: theory applied to practice. In business ethics as elsewhere, by applied ethics people usually mean applied philosophy. The theories that are applied in applied ethics are philosophical theories such as varieties of Kantianism or utilitarianism. Typically the theories are applied to specific issues such as abortion and euthanasia, or to more general ones such as distributive justice or the environment. In business ethics, theories are applied to specific issues such as ‘whistle blowing,’ broader ones such as the duties of the company to its stakeholders, or broader ones still such as the merits of capitalism.

If the applied ethics model is the only way to do business ethics, then this poses a serious problem for would-be business ethicists who are not trained philosophers. If one wants to do a good job of applying, say, Kantian ethical theory to practice, then ideally one would need a thorough knowledge of Kants’s works and of the large critical literature on Kantian ethics. Usually this only comes with a formal philosophical training, probably to a doctoral level.[1] However, there are many published academics in the field of business ethics - including some professors - who also lack this philosophical background. Indeed, if the current journals on business ethics are a reliable guide, business ethics is a thoroughly multi-disciplinary subject (Shaw, 1996:492). The *Journal of Business Ethics* ‘the oldest and best established professional publication in the field’ (Shaw, 1996:491), makes the following statement of its scope:

> *Journal of Business Ethics* publishes original articles from a wide variety of methodological and disciplinary perspectives concerning ethical issues related to business. Since its initiation in 1980, the editors have encouraged the broadest possible scope. The term 'business' is understood in a wide sense to include all systems involved in the exchange of goods and services, while 'ethics' is

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[1] One might object that one can apply Kantian ethics, with only a simple knowledge of key Kantian maxims, such as the categorical imperative. However, how exactly such maxims should be applied, and their role in Kant’s overall ethical thought are matters of considerable philosophical debate, and a proper application of Kantian theory would require knowledge of these such debates.

circumscribed as all human action aimed at securing the good life. (Journal of Business Ethics, November, 1996.)

As Shaw (1996) indicates, a substantial majority of the articles in recent years have been written by non-philosophers. However, while this gives some practical support to the idea that a work of business ethics need not be a work of applied philosophy, it raises an important problem. If business ethics is to be worth anything surely it must at the very least be able to offer authoritative ethical arguments about business practice. Business ethics as applied philosophy can reasonably claim that it has a clear basis for such authoritative arguments in ethical theory.[2] A philosophical business ethicist has a substantial arsenal of philosophical theories of ethics available for defending ethical claims: varieties of Kantianism, act- and rule-utilitarianism, Aristotelianism, neo-Aristotelianism, and other virtue theories, ethical egoism, prescriptivism, existentialism etc. (see Beauchamp and Bowie, 1983:21-39; Sorell and Hendry, 1994:35-49). If a would-be business ethicist is to make claims about the ethics of business, but does not have access to philosophical resources, on what basis can his ethical claims have authority? If I am to make claims about the ethics of ethical investment, what is the basis of authority for my claims?

In recent years, there has emerged within philosophy a literature which takes a new kind of approach to applied ethics. One which does not set a gulf between theory and practice in ethics, but sees ethical deliberation as a contextually situated practice. This approach seeks to ground ethical argument not on an ‘archimedian point’ (Williams, 1985:22ff) provided by philosophy and outside the realm of practical concerns, but on reasoning and reflection within the practices of everyday life. Examples of ethical work which seeks to develop this approach are Michael Walzer’ *Spheres of Justice* (1983) and *Interpretation and Social Criticism* (1987), Alasdair MacIntyre’s *After Virtue* (1984); Bernard Williams’ *Ethics and the Limits of Philosophy,* and various papers by Annette Baier (collected in Baier, 1994). In the remainder of this section I will offer a brief summary of this programme in ethical theory, and describe its relevance to my work.

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[2] But we should note, no single philosophical theory of ethics has yet achieved commanding acceptance among philosophers as authoritative (Shaw, 1996:495). Utilitarians dispute the authority of deontological theories, rule-utilitarians dispute the authority of act-utilitarian theory etc.

1.1.2 Interpretive ethical theory

These theorists are rather diverse, but nevertheless hold a few conceptions in common. They seek a position between objectivism and relativism in ethics. They argue that the attempt to ground theories of ethics in ahistorical, absolute foundations has not been successful. While some of them may accept a place for ethical theory, they are doubtful that it is as authoritative as it has sometimes pretended to be. As Williams argues, ethical theory cannot offer us compelling reasons to choose one intuition over another (1985:99). However these theorists also tend to claim that the collapse of ethical thinking into radical relativism is both ethically pernicious, and based on flawed epistemology. Instead, in various different ways, these writers seek to establish a space for intelligent reasoned ethical thinking, which is historically and culturally situated, but is nevertheless an authoritative basis for ethical thinking. The typical language used is the idea that ethical authority can be derived from 'shared understandings,' (Walzer, 1983) 'intersubjective meanings' (Taylor, 1971), inherited 'moral ideals' (Taylor, 1992), 'traditions' and 'social practices' (MacIntyre, 1984 & 1988), of particular historical communities. The ethical method of these writers is to seek to interpret the beliefs and purposes of particular communities. Indeed in some ways this approach to ethics could be called ‘methodological communitarianism’. Rather than appealing to philosophy or revelation, say, as the basis for ethical thinking, these theorists appeal to the understandings of a particular community. This methodological communitarianism is different from what one might call political communitarianism in that, in modern liberal societies at least, it does not necessarily favour conservative social values. In modern liberal societies the values of communities are as much the values of the liberal Enlightenment, as they are of older conservative religious traditions.

1.1.2.1 Walzer’s interpretive approach

What might this interpretive approach to ethics look like? Michael Walzer claims that the theory of justice he outlines in his *Spheres of Justice* is different to the theories that proceeded it because it is based, not on abstract, metaphysical ideas with universal application, but on interpretations of 'Our shared understandings’ (xiv). He says:

> My argument is radically particularist. I don't claim to have achieved great distance from the social world in which I live. One way to begin the philosophical enterprise - perhaps the original way - is to walk out of the cave, leave the city, climb the mountain, fashion for oneself (what can never be fashioned by ordinary men and

> women) an objective and universal standpoint. Then one describes the terrain of everyday life from far away so that it loses its particular contours and takes on a general shape. But I mean to stand in the cave, in the city, on the ground. Another way of doing political philosophy is to interpret to one's fellow citizens the world of meanings that we share. (1984: xiv).

Instead of seeking to ground their theories on general philosophical concepts, these theorists attempt to ground them on 'the world of meaning that we share', 'shared understandings', 'social meanings', (1983:9) 'social goods' (1983:7). For Walzer, this shift is based on the idea that 'justice is a human construction, and it is doubtful that it can be made in only one way.' (1983:5) He argues that it is unlikely that we are well served by adopting a single universal conception of distributive justice that applies generally to all societies and to all aspects of our society because, he claims, distributions take place in a variety of different specific contexts for a variety of different reasons. Chief among the reasons is the fact that the goods that are distributed have particular, contextually defined meanings; goods are not abstract but 'social' goods. They 'come into people's minds before they come into their hands; distributions are patterned in accordance with shared conceptions of what the goods are and what they are for' (1983:7). Because of this pluralism, Walzer divides his theory of justice into a number of different 'spheres', with different principles of justice for each. What counts as just for one sphere, may not necessarily count as just for another. In the same way, he claims, even more controversially, that what counts as just in one culture may not for another. Walzer summarises this by saying that:

> 'the principles of justice are themselves pluralistic in form; that different social goods ought to be distributed for different reasons, in accordance with different procedures, by different agents; and that all these differences derive from the different understandings of social goods themselves - the inevitable product of historical and cultural particularism.' (1983: 6).

Walzer's approach to justice is to interpret the social meanings as a result of which goods have their sense for the particular communities in which they find their use. He seeks, in particular, to interpret what 'our' various goods 'mean to us' (1983, xvi). A first step in this interpretive process is to realise that 'Social meanings are historical in character' (1983: 9). He urges us to attend to 'conception and creation: the naming of goods, and the giving of meaning, and the collective making.' (1983:7)

1.1.2.2 Rawls' new approach

This interpretive approach is not confined to the margins of contemporary ethical theory. Even mainstream ethical theorists like John Rawls have moved in this direction. Rawls is often credited with the revival this century of grand liberal ethical theory, not seen since the work of Bentham, Mill and Sidgwick. So he is often considered a classic case of a political philosopher offering a view from the mountain, and the opposite of particularists like Walzer.[3] However, in his work since his 1985 paper 'Justice as Fairness: Political not Metaphysical', collected in *Political Liberalism* (1993),[4] Rawls demonstrates a strong particularist, anti-universalist shift. This, he says, is not because of communitarian criticisms of abstraction and universalism, but because he noticed a practical problem with his theory (1993: xvii). The problem is that he considers his earlier foundationalist approach to be inconsistent with certain facts about modern liberal democracies. Rawls' project, in *A Theory of Justice* (1972) and since, has been to unearth the principles of justice which can serve as the basis for a stable, well-ordered society. He had thought that the philosophically grounded principles of justice set out in *A Theory of Justice* could serve as such a basis. He now sees a fatal flaw in this plan. He claims that there are, as a matter of empirical fact, a diversity of incompatible, yet reasonable, philosophical doctrines affirmed by the members of modern liberal democracies, and that it is a feature of liberal democracy to perpetuate such diversity. This he calls 'the fact of reasonable pluralism' (1993: 36). Rawls thinks that, in the light of this fact, it is unrealistic to expect that these diverse, reasonable doctrines be dropped in favour of the foundational philosophical doctrine contained in his earlier work. People, he thinks, already affirm their own doctrines; pragmatically, he does not think he can expect them to drop their cherished beliefs in favour of the philosophical theory outlined in his earlier work. Because of the 'fact of reasonable pluralism' Rawls now thinks that 'philosophy as the search for truth about an independent metaphysical and moral order cannot provide a workable and shared basis for a political conception of

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[3] It is increasingly argued that this characterisation of Rawls, though warranted, is not entirely accurate. See for example, Plant (1991: 354ff).

[4] Though *Political Liberalism* is a collection of earlier papers, Rawls has altered some papers significantly, changing their titles, and merging them together into single chapters. This makes referencing difficult. On the assumption that the book is more widely available than the papers, I cite the book rather than the papers. Occasionally, I have been unable to find a passage in the book that corresponds to one in the papers, so the paper is cited instead.

justice in a democratic society' (1985: 230). He therefore believes that any principles of justice should be capable of achieving principled endorsement by an 'overlapping consensus' (1993:133ff) from the variety of reasonable philosophical doctrines affirmed in modern societies, and not endorsement on the basis of the single philosophical doctrine he articulated in his earlier work. Rawls believes an overlapping consensus might be possible because, fortunately, despite the fact of reasonable pluralism,

> 'the political culture of a democratic society, which has worked reasonably well over a considerable period of time, normally contains, at least implicitly, certain fundamental intuitive ideas from which it is possible to work up a political conception of justice suitable for a constitutional regime.' (1993:38, n.41.).

These intuitive ideas are to be found in 'our public political culture itself, including its main institutions and the historical traditions of their interpretation.' They take the form of 'settled convictions [such] as the belief in religious toleration and the rejection of slavery' (1993:8). Rawls thinks the way to proceed is to collect these settled convictions and

> 'try to organise the basic ideas and principles implicit in these convictions into a coherent conception of political justice...We hope to formulate these ideas and principles clearly enough to be combined into a political conception of justice congenial to our most firmly held convictions.' (1993:8).

Rawls' idea is not that these shared and settled convictions have any metaphysical privilege, but that because they are widely shared and have a long pedigree they are the best chance we have to find some basic principles that can be used to 'construct' a concept of political justice that can achieve principled endorsement by the range of incompatible moral and philosophical doctrines that he assumes are a fundamental political fact of modern societies. This kind of foundation for political theory is a pragmatic one rather than a metaphysical one.[5] Principles of justice constructed from it are 'securely founded in public political and social attitudes' (1985: 230), not in a philosophical theory grounded in metaphysics. A final feature of Rawls' approach is that not only is the basis of his theory of justice built up from the settled moral convictions of the community, but the recommendations that arise from the theory are constrained by these convictions. This is Rawls' idea of 'reflective equilibrium' (1972:48ff.). While

[5] A point on which Rorty has placed much emphasis (Rorty, 1991b).

it allows that a Rawlsian theory of justice, built from our settled convictions, might then challenge some of those convictions, it may also, reciprocally, be contested by them.

1.1.2.3 The need for an empirical turn

Before concluding the discussion of what has been called the ‘interpretive turn’ (Warnke, 1993) in ethics, I want to consider some criticisms of this approach. In concluding my account of Walzer’s approach I said that a first step in this interpretive process is to realise that 'Social meanings are historical in character' (1983: 9). He urges us to attend to 'conception and creation: the naming of goods, and the giving of meaning, and the collective making.’ (1983:7) From the point of view of ‘methodological communitarianism’ we must be attentive to the social and historical processes by which particular shared understandings arise, and the particular interests and institutions which create, support and promote them. Walzer and other communitarians have been criticised for being insufficiently attentive to these factors.

In the space of some 300 pages Walzer considers issues concerning the welfare state, health-care, charity and dependency, money, markets, conscription, public office, dangerous and dirty work, free time, education, kinship and love, religion and the state, public honours, political power, and citizenship. Even this long list doesn't fully convey the enormous breadth of Walzer's work. Walzer interprets our social meanings with respect to the various goods in the domains listed by means of 50 case studies embedded in an argument peppered with instructive references to various significant figures in the history of political and social thought, and to the work of some of his contemporaries. Only a few of the case studies Walzer uses directly interpret the shared understandings of contemporary Americans, the majority are drawn from other, often distant, times and places. Examples from contemporary America include a refuse collectors' co-operative in San Francisco, and the idea of 'dating'. More distant examples are the classical Chinese meritocracy, the Israeli Kibbutz, Aztec education, and Athenian ostracism. These studies vary quite considerably in texture, some are more historically detailed than others. But none are very detailed, most rely on rather venerable, secondary literature. Neither the lack of historical detail, nor the reliance on secondary sources are criticisms in themselves. Walzer has won considerable praise for including the wide and fascinating historical data that he uses. However, he does claim to be 'radically particularist' and he has said that he means to 'stand in the cave, in the city, on the ground' (1983: xiv), and if he is right to urge us to attend to 'conception and creation’, he needs to demonstrate that he does stand on the ‘ground’, and that he is attentive to the processes by which shared understandings emerge and change. His vast sweeping historical approach does not achieve this. If this ambition is taken seriously (and it should be: he is, after all, claiming to base his theory of justice on these interpretive claims) then the historical materials he actually uses are placed under considerable strain; a weakness of which his critics have been able to make much.

Susan Moller Okin asks, parodying MacIntyre, 'Whose traditions? Which Understandings?' (1989: 41). She criticises MacIntyre and Walzer for paying insufficient attention to the fact that the appeals they are making are to the shared understandings of certain dominant classes, rather than to the shared understandings held by *all* their contemporaries. She claims that the understandings they appeal to do not represent the shared understandings of, say, the feminist tradition.[6] This criticism is partly one concerning the empirical claim that where MacIntyre and Walzer see single shared understandings, there are in fact a plurality of competing shared understandings;[7] and partly a criticism about the uncritical, nature of the communitarian appeals to the shared understandings of an existing order. The use of the former criticism is not limited to feminists. Ronald Dworkin has criticised Walzer in much the same way (Dworkin, 1983). Dworkin says that where Walzer argues that there are single shared understandings implicit in the social meanings of various goods, in fact there are plural understandings. Taking the example of health-care, he says that Walzer argues that there is one shared understanding operating: health-care should be distributed on the basis of

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[6] Okin argues that there is a recognisable feminist tradition (1989: 60), that could well be appealed to as an alternative source of shared understandings.

[7] While I am claiming that Okin is arguing that there is a plurality of shared understandings, she in fact claims that there are '*no shared understandings*, even amongst women' (1989: 67). This apparent contradiction rests on differing interpretations of the meaning of 'shared'. When Okin claims there are no shared understandings, she is discussing the plurality of different understandings about gender held by the members of our society. Because there is a plurality of different understandings held by people, there are no understandings shared by *everyone*, so in this wide sense there are no 'shared' understandings. But this doesn't mean there are no shared understandings of any kind. One might assume that understandings can be shared to various different degrees. There are, I think, various factions in the feminist movement that do share understandings about gender. So, while one can readily concede that there are no universally shared understandings about gender, one can say that there are many different shared understandings of gender; shared, that is, by various different groups of people.

need. Dworkin denies that this is so. He says that 'the brutal fact is that we do not provide anything like the same medical care for the poor as the middle classes can provide for themselves, and surely this also counts in deciding what the "social meaning" of medicine is for our society' (1983:6). More generally Dworkin argues that the various spheres of justice are in fact characterised by disagreement between different kinds of shared understandings. Dworkin's criticisms, in part, rest on the common liberal claim that modern societies are characterised by a deep-seated moral pluralism, which Dworkin indicates that Walzer, despite his claims to particularity, ignores.

While there are wider issues here about communitarian approaches to ethics in general, the central issue that I want to address is that Walzer, MacIntyre and other interpretive theorists have failed to fill in a range of social, historical and institutional details. As Bernard Williams has said of the interpretive turn in *Political Liberalism*, Rawls' work lacks,

> 'the dimension of what might be called sociological imagination, a sense that the peculiarities (...) of American constitutionalism may depend on features of American society which are grounded neither in its political organisation nor in its ideas, but in such things as the history of its immigration and its dedication to the aims of commercial society' (Williams, 1993:7).

The general problem, I wish to suggest, with methodological communitarianism is that it fails to pay sufficient attention to the detailed historical and socially situated nature of the shared understandings of particular communities. One resolution to this problem is recommended by Ian Hacking in various recent papers (1990; 1991).

1.1.2.4 Hacking's recommendation of a historicist turn in ethics

Hacking's recommendation of a interpretive, historicist version of moral inquiry is most explicit in his paper 'Two Kinds of New Historicism for Philosophers.' In this paper, Hacking's concern is to draw out the possibility of an approach to philosophical problems inspired by what Foucault called the 'history of the present' (Hacking, 1990:343). He is particularly interested in the problems of moral philosophy. Hacking argues that the present tradition in Anglo-American philosophy is profoundly anti-historical, and that this is severely limiting. Hacking recommends a different approach. He wants to historicise philosophical problems. The way he wants to do this is by 'taking a look' (1990:354) at the local, empirical facts that surround their emergence as problems. This is 'a local historicism, attending to particular and disparate fields of reflection and action' that 'discourages grand unified accounts' and demands 'taking a look at lots of little facts.' (1990:345). He illustrates this local historicism by describing the work of 'a generation of post-Kuhnian students of science...[that] takes construction as its motto' (1990:356). Here he mentions the work of Latour and Woolgar (1979), Pickering (1984) and Schaffer and Shapin (1985).

In this paper, the main collection of philosophical problems which Hacking wants to historicise are problems in moral philosophy. Hacking believes that the concepts and problems in this area of philosophy are ripe for the kind of local historicism he is advocating. In fact he says that morality is an arena where we would be even more likely to find concepts 'moulded by history' (1990:358) than the arena of science. Hacking observes that just as philosophy of science has dealt with abstract concepts, like truth, reality and fact, moral philosophy has dealt with abstract topics like right, good and justice. Interpretive historicists have challenged the abstractions produced by philosophers of science by investigating 'not truth, reality and fact, but truths, real things and facts' (1990:358). Hacking urges us to follow post-Kuhnian science studies and to do the same to the abstractions of moral philosophy[8]: by turning away from abstract concepts to concrete ideas of the good, particular rights, and varieties of justice and to what Bernard Williams has called 'thicker...more specific ethical notions' (Williams, 1985:129) like treachery, brutality, promise and courage. This returns us to the interpretive turn in ethical theory, advocated by Walzer and others that I have been describing. However, where Hacking is different from Walzer and the other interpretivists that I have been discussing, is his focus on much more specific shared understandings. Where Williams' 'thick' concepts are still rather abstract, Hacking's main work in this area is not abstract at all: it concerns child abuse.

Hacking is explicit in linking his work on child abuse to his programmatic recommendation of turning his empirical, historical, 'constructionist' approach to morality. Concerning the interpretive, historicist approach to ethical concepts he advocates, Hacking says 'The example of this sort on which I have done the most work

[8] Hacking is not the first to recommend this move. In the late 1960s, J.B. Schneewind wrote: 'If the study of the history of science is still at a comparatively early stage of development, the study of the history of moral systems has hardly even begun. At this point it can only be proposing a hypothesis to say that the pattern of thought revealed in [Kuhn's] studies of "scientific revolutions" may be useful as a guide in investigating the development of norms and values.' (1983:124)

is child abuse' (1990:360). In his papers on child abuse (1988, 1991), Hacking reports 'lots of little facts' that collectively demonstrate how our beliefs about the harm adults do to children have changed in the last thirty years. He shows how 'new methods, new agencies, new laws, new education of children, new information for parents, new therapies, and above all new and growing knowledge [has] transform[-ed] the world' (1991: 258). An important part of the world that has been transformed is the moral world; the domain which specifies the rights and wrongs of the relations between adults and children. As Hacking says,

> 'People do many of the same vile things to children, for sure, that they did a century ago. But we've been almost unwittingly changing the very definitions of abuse and revising our values and moral codes accordingly. (1991: 253)

Hacking is very positive about the emergence (or construction) of the concept of child abuse in the last thirty years. He says that, in contributing to this process, 'the child abuse movement may have effected the most valuable, albeit the most discouraging, heightening of awareness that has taken place in my lifetime' (1991: 257). However, Hacking has certain ambivalences. He worries, for example, about the way a wide variety of very different kinds of harm perpetrated on children by adults are lumped together under a single, all-embracing category. He is particularly concerned because he thinks that we may have constructed this umbrella category in an unfortunate manner. Though we use the single, blanket concept 'child abuse' to talk about these different kinds of harm, we are quite able to separate them out into different categories. Hacking quotes some research that shows how Californians are readily able to distinguish many varieties of harm: 'Physical Abuse, Sexual Abuse, Fostering Delinquency, Supervision, Emotional Mistreatment, Drugs/Alcohol, Failure to Provide, Educational Neglect, Parental Sexual Mores' (1991: 283).[9] Despite our ability to separate them, these forms of harm are persistently lumped together.

If this lumping was a case of mere descriptive convenience it would not matter much. However, Hacking demonstrates that subsuming many kinds of harm under this one concept has many significant repercussions. In particular, it has powerful consequences for our moral beliefs about harm to children. Hacking presents these consequences by disclosing certain features of the local, historical origins of our concept of child abuse.

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[9] See Giovannoni and Becerra (1979).

He reports that the concept of child abuse first gained wide public usage following the publication of a paper, by some doctors, which announced the existence of 'battered-baby syndrome.'[10] Hacking argues that, ever since then, the development of child abuse has been controlled by the medical profession. Consequently it has become a strongly medicalised concept. One key feature of this medicalisation is that child abuse has been constructed as a kind of disease (1991:280ff). This has certain implications. One is that all cases of child abuse have a common cause, as it is a general feature of our ideas about diseases that they have common causes. (The cause of AIDS, for example, is a virus). Another consequence of identifying child abuse as a kind of disease, is that, like a disease, the evil of child abuse can be communicated. Parents can be infected by, say, violent pornography and, later on, in the course of abusing their children, they can pass on the disease to them. Another implication is that a mild case can develop into a serious one, if left untreated. Smack a child in anger today, and, unless you receive therapy, sometime in the future you may be at risk of succumbing to the full-blown disease: sexual assault.

If Hacking is right that the concept of child abuse has been constructed on a disease model, and if he is right that we make certain assumptions based on this model, then there are several implications for our beliefs about child abuse as a social problem and, of particular significance here, as a moral problem. The assumption that all the kinds of harm adults inflict on children share a common cause, may encourage the idea that all these different kinds of harm should be tackled by rooting out and eliminating this single cause; rather than by searching for a wide variety of potential causes, and developing a range of policies to address them. It also changes our moral beliefs. One possible example concerns our moral beliefs about parents smacking children.[11] If the same causal processes are present both in the most vicious sexual assault and in a parent's disciplinary smack, parents who smack their children therefore risk succumbing to the full-blown disease of child abuse. And, worse still, they risk infecting their children with the disease, and so making them more likely to, later, abuse their own offspring. This confers on smacking a grave status in our inventory of moral evils, a status which the Victorians may have found ridiculous. The point here is not to defend

[10] Kempe, C.H. et al. (1962).

[11] Hacking doesn't use this example, though he does mention our shifting attitudes to corporal punishment (1991: 284).

smacking, but to illustrate the critical power of Hacking's history of the emergence of our concept 'child abuse'. Hacking's work indicates that our ideas about child abuse rest, at least in part, on a disease model. This makes possible the hypothesis that the idea of a common causal link, operating subconsciously, like a hidden psychological disease, may have been a powerful motor in the 'revision of our values' concerning corporal punishment. If, as seems likely, little evidence emerges for thinking that there is in fact a common cause to the forms of harm currently characterised as child abuse, then lumping them together, while rhetorically powerful,[12] is empirically dubious. Consequently, those moral beliefs and public policies that employ the disease model of child abuse begin to look unjustified.

Hacking’s work offers one powerful methodological approach to the interpretation of shared understandings. Unlike Walzer, he concentrates explicitly on the 'conception and creation’ of our shared understandings about child abuse. His critical engagement with child abuse is based directly on an understanding of these processes. While Hacking’s local, historicist, or ‘social constructionist’ approach offers one model for implementing the interpretive approach to ethics, I have described, there are other models available. Hacking himself also refers to wider kinds of interpretive writing in social science such as the ethnomethodology of Garfinkel (1967), and the sociology of Gusfield (1981) as examples, but others such as Barry Hoffmaster (1983), have also recommended various ethnographic approaches to ethics. Hoffmaster cites particular examples of how ethnographic studies of surgeons (Bosk, 1979) and neo-natal care (Frohock, 1986) are useful for addressing problems in medical ethics. I am not arguing for the superiority of a particular approach, only arguing that approaches that attempt to fill in the detailed, social, historical and institutional details of the emergence of the shared understandings of particular communities, and their traditions, seem to offer considerable depth and sophistication to the interpretive approach to ethics which I have been discussing.

1.1.3 Interpretive business ethics

We have by now moved a long way from conventional business ethics. While Rawls, Walzer and other theorists of justice are often referenced in the business ethics literature, it is for their substantive contributions to ‘broad’ theories of economic justice,

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[12] See Hacking (1991: 284) on this.

rather than on methodological grounds. And child abuse is certainly not a conventional topic for business ethics. However, I believe that it is appropriate to attempt to turn these recent methodological developments in ethical theory to the consideration of business ethics. The lesson that the interpretive turn offers is that intelligent ethical arguments can be built on the basis of critical engagement with the shared understandings of a particular community, tradition, or institution. On this approach one can evaluate the ethics of a particular practice, or a particular community, not primarily with reference to a philosophical theory, but by means of critical engagement with the shared understandings of the people who engage in various ways in the practice concerned. I can evaluate the ethics of ethical investment by means of a critical engagement with the shared understandings and traditions of the ethical investment 'community'. I can engage with the ethics of ethical investment without, as Walzer puts it, having ‘to walk out of the cave’ or ‘leave the city’ but can do so from standing ‘in the cave, in the city, on the ground.’ This is good news because it offers an intellectually defensible basis on which non-philosophers can engage critically with the ethics of business practice.

It is possible that the attempt to introduce this new kind of ethical theory to business ethics has already been made and I have not found it. While I can claim that my literature survey on ethical investment has been exhaustive (see below), my literature survey on business ethics methodology has unfortunately been less so. While I have searched fairly widely, I cannot claim with confidence that my attempt to draw on these methodological resources is original to business ethics, though I have not come across other similar attempts.

Examples are widespread within the business literature, however, of implicit references to some of the concepts interpretive ethical theory introduces. For example, Beauchamp and Bowie state that ‘Many people go through life with an understanding of morality largely given to them by their culture’ (1983:3). A basic assumption of interpretive ethical theory is that morality is given by our culture. Interpretive ethical theory seeks to interpret and argumentatively engage with this ‘given’ morality. Beauchamp and Bowie refer in particular to ‘special moral norms for business activity, norms usually devised by businesspersons themselves’ (1983:3). These norms can, I think, be regarded as the ‘shared understandings’ of business practice.

Another example is, I think, provided when Sorell and Hendry argue that one important factor in determining corporate practice is the 'moral climate' or 'climate of expectations' in which companies operate (1994:6). The best example Sorell and Hendry give of the role of the climate of expectations is the case of the take-over, by Grand Metropolitan - a British conglomerate - of Pillsbury in the US. At the time of the take-over, the question arose of whether or not, as a subsidiary of Grand Met, Pillsbury would continue its generous level of corporate philanthropy (at least by Grand Met's British standards). Grand Met decided to commit to a generous programme, because, according to Sorell and Hendry

> 'In America, as Chandler [Howard Chandler, Group External Relations Director of Grand Met] saw things, employees and consumers expected more of business than in the UK: if business did not make conspicuous efforts, e.g. to demonstrate concern for the environment, or to benefit the communities from which they drew skilled labour, they would lose out in the competition for both customers and employees. It was in order to satisfy general expectations, then, that companies had to associate themselves with corporate responsibility.' (1994:30)

I think it is reasonable to see conceptions such as the 'climate of expectations' as another way of talking about the 'shared understandings' held by the wider public about how businesses should and should not operate.

When Sorell and Hendry suggest that the climate of expectations can be changed, they refer to a wide range of factors as being 'influences on moral opinion', including: religion, law, interest groups, newspapers, television, and academic work, including philosophy (1994:10). The possibility that shared understandings can change is central to the conception of the idea of an ethical tradition I have discussed. The idea that particular institutions can have an important role in contributing to this change is one of the key points I offered in my discussion of Ian Hacking's work. In some ways, an interpretivist approach to business ethics may be considered to recommend a study of the processes by which the moral climate changes, and a critical engagement with these processes. Of course, in this particular work, my central concern is not with the climate of expectations about business as a whole, but rather with the expectations of the ethical investment community as to what ethical investment should be about. However, the underlying idea is similar.

There are two qualifications I would like to offer concerning my appropriation of this interpretivist approach to ethics. Firstly, the fact that I plan to borrow a methodological approach from these interpretive theorists does not mean that I agree with their ethical outlook and conclusions, or that I accept their theoretical approaches entirely. Indeed there is wide disagreement between the 'interpretive' ethical theorists I have mentioned, both about how their methods should be applied, and where theory based on them leads in normative ethical and political terms. Many interpretive ethical theorists seem to reject the role of traditional philosophical theory in ethics entirely. MacIntyre offers us a chapter which tells us 'Why the Enlightenment Project of Justifying Morality Had to Fail' (MacIntyre, 1984). He offers us a fairly apocalyptic picture of an 'emotivist' culture where morality has lost its way, and in which 'the new dark ages' (1984:245) are already upon us. This it seems to me is overdone. In general the interpretive ethical theorists tend to reject what they describe as the foundationalist ethical theories which seek to ground ethics in metaphysics, or other 'meta-narratives' (see Rorty, 1991a and 1991b). Such arguments are part of much larger debates between foundationalists and anti-foundationalists, essentialists and anti-essentialists, modernists and post-modernists, theorists and anti-theorists in philosophy. While to a certain extent these arguments are unavoidable, in this thesis I will be steering clear of them. It is true that many of the interpretive theorists I have discussed tend to line up on the antifoundationalist side of the argument, but the methodological approach that I am borrowing from them need not require making negative claims about traditional philosophical theory. One can interpret the shared understandings of a moral community while remaining agnostic about whether, for example, Kantian theories of ethics are or are not in fact securely grounded in metaphysical conceptions of Reason. One can work critically *within* culture without rejecting the philosophical project to find sources of authority beyond it.

The second qualification is that I do not want the length of discussion of the interpretive approach to raise the expectation that this thesis will be citing theoretical literature at every turn - I certainly have no intention of using Rawls' work as the basis for ethical criticism, for example. Neither do I want to raise expectations that I will be rising to the challenge of full-blown ethnography. With a few significant exceptions, this work lies in the background. It provides the intellectual justification for my approach, and frames some of my particular arguments. However, I do not use it as the basis for drawing particular lessons about the nature and purpose of ethical investment. I turn to the shared understandings of the ethical investment community for this.

1.1.4 Applying the interpretive method to ethical investment

My discussion of interpretive approaches to ethical theory began as a response to a problem of where to locate ethical authority for my work in business ethics. Because the approach I am taking is rather unconventional, it has been important for me to establish it in some detail. My intention in the previous pages[13] has been to indicate the viability of an approach to ethics which proceeds by interpreting the shared understandings of a particular community, and by engaging argumentatively with its traditions.

In my approach to interpretive ethics I have taken a robustly empirical turn, the practicalities of which I discuss at the end of this chapter (see p.38). My reading of the ethical investment marketing literature, my interviews and discussions with the founders and leading opinion formers in the ethical funds, my participation in the routine workings of ethical investment in the UK, and my interviews with ethical investors are all directed to building a fairly solid empirical picture of what the shared understandings of ethical investment are. My thesis is directed primarily at ethical unit trusts, so most of my work has been devoted to interpreting the shared understandings of those who run these organisations. In particular I have sought to understand what these people believe to be the purposes of ethical investment. This interpretive work forms part of my perspective for evaluating the procedures, purposes and problems of ethical investment. I have tried to evaluate the methods of ethical funds against my understanding of their own convictions about the purposes of ethical investment. Similarly, when I talk about the 'effectiveness' of ethical funds, I am discussing how effective their chosen means are for achieving what I consider to be *their* purposes.

This interpretive, engaged form of business ethics offers a model for how I intend to proceed in this thesis. From my point of view, one of the most useful ways of framing the interpretive approach has been offered by Alasdair MacIntyre:

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[13] Which I expand on in more depth in my paper ‘Social Constructionist Political Theory’ (Mackenzie, forthcoming).

> 'all reasoning takes place within the context of some traditional mode of thought, transcending through criticism and invention the limitations of what had hitherto been reasoned in that tradition; this is as true of modern physics as of medieval logic. Moreover when a tradition is in good order it is always partly constituted by an argument about the goods the pursuit of which gives to that tradition its particular point and purpose. So when an institution - a university, say, or a farm, or a hospital - is the bearer of a tradition of practice or practices, its common life will be partly, but in a centrally important way, constituted by a continuous argument...The living tradition then is an historically extended, socially embodied argument, and an argument precisely in part about the goods which constitute that tradition.' (MacIntyre, 1984:206-207)

This statement provides a useful way of thinking about how to move from interpretive ethical theory to ethical investment. Ethical investment is an example of what MacIntyre calls a practice, a 'coherent and complex form of socially established co-operative human activity through which goods internal to that form of activity are realised' (1984:175). And for MacIntrye, goods are to be understood in relation to the practice which they partly constitute. There are two primary goods to be found in the shared understandings of the ethical investment tradition, which give it its point and purpose. They are the quests to provide a solution to the investment ethics problem, and to address the corporate harm problem. I will offer evidence for this in Chapter 5 (see p.118) and 6 (see p.134). In some ways, because ethical investment is a new kind of practice, a new institution, and its tradition is still in an emergent phase, the argument about what goods ethical investment should be pursuing is muted. This means that these goods are not as clearly defined as they could be, or as they perhaps need to be. As I claimed in the Introduction, there is little writing about the procedures and purposes of ethical investment, particularly in the academic literature, so part of the burden of this 'early' work is to help bring these goods into clearer focus, to develop the terms of the argument, and to provoke critical consideration.

In order to apply the interpretive approach to ethical investment, one thing that will need to be established is the extent to which ethical investment can be considered to be a community and a tradition. This I will do in the conclusion of Chapter 3 (see p.86). If ethical investment cannot be sensibly regarded as a community or a tradition, then it is hard to see whose shared understandings I would be seeking to interpret. At this stage all that needs to be said is that I think I can show that ethical investment can plausibly be regarded as a community, albeit of a rather permeable kind. It is certainly not self-contained. It grew out of wider communities and traditions, and still gets some of its strengths from these sources. It also not easy to distinguish from wider communities, because it has itself sought to popularise itself amongst the wider investment community in the UK, with some success. An NOP poll carried out for Friends Provident Stewardship found that around 20% of the UK adult population had heard of ethical investment (NOP, 1995). This implies that its ideas, concepts and understandings are now more widespread than the small community of participants in ethical investment.

As I noted in the Introduction, I intend to limit the focus of this thesis down to a narrow range of questions about ethical investment. This means that when I seek to interpret the shared understandings of the ethical investment community, I will also constrain myself to a small number of important conceptions. My purpose in this thesis is primarily to evaluate the efficacy of the procedures of ethical investment as a means of addressing the corporate harm and investment ethics problems. As I mentioned in the Introduction, while I have invented the terms, these problems are key shared understandings in ethical investment, and the resolution of these problems are, in MacIntyre's language, the principal constitutive 'goods' of ethical investment. Most of my argumentative work is devoted to the task of critically engaging with these the conceptions of the problems held within ethical investment and the solutions offered by ethical funds.

1.2 Empirical methods

1.2.1 Theoretical issues

Given that an important part of my claim to be advancing knowledge in this field of business ethics relates to my descriptive study of the procedures of ethical funds in the UK, it is important for me to establish the methods I used to compile these studies. The approach to ethics that I am taking requires the attempt to interpret the shared understandings, settled convictions of a particular community. In this case the ethical investment community. The methods required for this kind of task require the interpretation of a particular social context, and of the meanings, beliefs and motives of the participants. As I said in the first part of this chapter, interpretive ethical theorists have been criticised for failing to show that they are 'on the ground', interpretively speaking. I hope not to make this mistake. I reported suggestions made by Hacking and

Hoffmaster about the empirical models that might be used. While I will not be adopting Hacking's 'social constructionist' approach in detail, and while this work will not be a proper ethnography, my methods are largely qualitative.

In social science as a whole qualitative methods have had mixed support. In many disciplines, apart from anthropology and sociology, they have frequently been marginalised as a supplement to core quantitative methodologies (Silverman, 1993:20). The suspicion that qualitative methods are not reliable arises from traditions of positivism in social science originating in the work of Auguste Comte in the 1830s, and coming to dominate social science in the mid-20th century. Positivism limits the world of possible data to verifiable, observable 'facts'(Hacking, 1983:41). The impressions, hunches, interpretations, and understandings produced by qualitative studies are generally not easy to verify, and certainly not observable. However, there have been strong counter traditions which emphasise interpretative methods, starting perhaps, with Dilthey in the 1860s, and exemplified in the interpretive method of Weber (Swingewood, 1984: 141).

Many attempts have been made to formalise qualitative methods, and so to lend them a more 'objective' and rigorous feel. However, such attempts have not in general been very successful. Ultimately, as Clifford Geertz (1975) argues, interpretative method comes down to 'thick description'. And, the job of the interpretative social scientist is not dissimilar to that of an author, convincing his readers that he has 'been there'. (Geertz, 1988). One of the most productive sub fields in sociology in the 1980s was 'social studies of science' which largely involved sociologists in lengthy studies of the daily activities of scientists (see for example, Pickering, 1992 for an overview). The methodologies used were largely qualitative, and rely mostly for their authority on the plausibility of the narratives of authors who sat and observed the activities of practitioners, and discussed matters with them. Indeed, Lynch (1993), a prominent sociologist of science, advocates a 'nothing fancy' approach to methodology which means:

> 'juxtaposing (arguably) comparable cases, citing testimonies and reports, drawing out common themes, noting relevant discrepancies and trends, and appealing to common intuitions and judgements. [A method which] uses ordinary modes of observing, describing, comparing, reading and questioning, and its constituent activities are expressed in vernacular terms' (1993: 304-5).

If Geertz's anti-formalist position is right, then the most powerful thing about my description will be the plausibility of my observations, descriptions, comparisons, and questions. As Lynch says, this approach to method trades on 'an immense and varied set of competencies that "we" already have available' (1993:305). I take Lynch to be arguing that as encultured human beings, we are very good at interpreting each others actions and beliefs, and detecting flaws in the secondary accounts of those actions and beliefs.

I am persuaded by this literature and so I will not adopt formal approaches to method, but rely on a 'nothing fancy' approach. In the rest of this section I will describe my programme of practical research, and establish the basis for my claims to be getting close to an accurate interpretation of ethical investment practice in the UK. As a first step in this process it is important for me to describe the basic activities I engaged in order to pursue my research.

1.2.2 Practical research

Much of my research was conducted as part of the 'Morals and Money' project at Bath University, funded by the Economic and Social Research Council.[14] I have been the research officer for this project since October, 1994. In the course of my research I have interviewed around 50 people involved in ethical investment, and have been a participant-observer at a number of ethical investment events and activities. The core of my research is a detailed case study on the workings of Friends Provident Stewardship, the first ethical fund in the UK, and by far the largest, accounting for 70% of the total ethical investment market. It is sensible to begin with an account of the research undertaken for this case study.

1.2.3 Stewardship case study

My study of Stewardship draws on five principal sources of information:

1. interviews with key Stewardship personnel;
2. observation of Stewardship committee meetings;

[14] Grant No. L122251017 awarded to Dr. Alan Lewis and Dr. Adrian Winnett of the University of Bath, and Dr. Paul Webley of the University of Exeter.

3. reading of private Friends Provident and Committee of Reference[15] documents;

4. Friends Provident Stewardship publications;

5. discussion with third parties

I am the first external researcher to have been given permission to attend Committee of Reference meetings, and to see private Committee documents. I am also the first to interview the key personnel involved in the Stewardship process. I was made privy to a considerable amount of information that is not yet in the public domain. In the past it has been believed by some within Stewardship that much of this information is commercially sensitive, and so researchers have not been granted access. Fortunately, my request for access came at just the right time when those who run Stewardship were changing their view on these matters. However, my access was subject to my signature to a confidentiality agreement. This agreement effectively gives Stewardship a veto on the publication of any information not already in the public domain, gained as a result of my privileged access. In practice this has meant that the vast majority of Chapters 3 and 4, which relate to Friends Provident, are based upon a draft agreed and approved by the Stewardship Committee of Reference, which includes two members of the board of Friends' Provident Life Office. In fact the veto was never used. However, the agreed draft is the third draft to have been discussed with Friends Provident. I received comments on the drafts by the company secretary, the members of the Committee of Reference, two members of the marketing department, and by a representative of EIRIS, the independent research body used by Stewardship. In addition to detailed textual comments, the draft attracted some 30 pages of additional notes and suggestions. Many details in the draft were changed to reflect these comments. In addition, there are certain items of information which I have voluntarily chosen not to discuss. The confidentiality agreement has had some moderating effects on my tone, and the topics I have addressed. However, I am confident that generally speaking a full and accurate picture has been given. Of course the fact that Friends Provident has scrutinised and approved my draft means that it is more likely that my description of the Stewardship process is accurate, contains no substantial errors, and reflects the understandings held by those who run

[15] For information on the Committee of Reference, and various other participants in the Stewardship process, see p.71ff.

Stewardship about the work that they do. This helps underwrite my claim to be an accurate interpreter of the shared understandings ethical investment community.

Subject to this confidentiality agreement, I have completed lengthy interviews with Frank Blighe, head of marketing for the Stewardship funds; Charles Medawar, and Charles Jacob, members of the Committee of Reference; and Richard Lowman and Richard Singleton, investment managers for Stewardship. I have also had occasional supplementary conversations with several of these individuals. In addition I have various occasional conversations with Lyn Wilson and Roger Morton of the Committee of Reference, Phil White in the marketing department, and Roger Whiffin and Diana Monger in the Secretariat.

The main focus of my empirical study was my attendance at meetings of the Stewardship Committee of Reference and its Investment Sub-Committee. Prior to these meetings I was sent the agenda, and copies of the papers which are circulated to the Committee members. These documents totalled over 200 pages. At these meetings I took detailed notes, but I did not have permission to tape-record the meetings. Much of Chapter 4 is a description of the deliberations of the Committee at these meetings.

I have also read a number of private papers, including the main statement of the Stewardship ethical policy, documents circulated to those attending the Committee of Reference meetings, and some private documents produced by members of the Committee of Reference. I have also read most of the published material which Friends Provident have published about Stewardship since 1984, and many of their more recent press releases. And finally, I have consulted commentary about Stewardship in several popular and academic publications.

1.2.4 Other practical research

In addition to my studies with Stewardship, I have also interviewed - on the phone or in person - a number of other insiders in the ethical investment business. These break into the following categories.

- Those responsible for running ethical funds: Tessa Tennant, head of ethical and environmental investment at NPI, and Chair of the UK Social Investment Forum; Anne Maree O'Connor, researcher at NPI Global Care Fund; Emma Howard Boyd and Charles Millar, researchers at Jupiter Ecology Fund, Charles Henderson, manager of Scottish Equitable Ethical Unit Trust; Kate Murphy, manager of Henderson Ethical Unit Trust; Fleur Leach, of Albert E. Sharp; and Mark Hayes, director of Shared Interest.

- Those responsible for providing research to ethical funds: Peter Kinder, president of Kinder, Lydenberg and Domini; Peter Webster, executive director of EIRIS, and Ros Haverman, researcher, EIRIS.

- Financial advisors who specialise in selling ethical investment products: Lee Coates, of Ethical Investors Group; Pat Meehan, of Holden Meehan, Brigid Benson of Gaiea.

- And finally, David Fawell, marketing manger of the Co-operative Bank.

This list is not exhaustive, I have spoken to another 30 or so individuals involved in the provision of ethical investment in the course of this study. The interviews did not follow a set schedule of questions. In each case I prepared some questions in advance. My questions typically ranged from their specific role in ethical investment, to their conceptions of the origins, procedures, problems and prospects of the ethical investment business. I recorded the interviews with Blighe, Singleton, Medawar, Tennant, Hayes, Coates, and Fawell. I made notes on the rest during and after the interviews.

In addition to interviews with industry insiders, I also interviewed a number of ethical investors. The primary purpose of this work was to gather data about the motives of ethical investors for research on the 'Morals and Money' project. In all I have conducted 20 telephone interviews with ethical investors. Ten of these were supplied by Shared Interest, a specialist kind of ethical investment institution that takes deposits from people in the UK and lends them to sustainable co-operative business in the third world. The other ten were supplied by EIRIS. All but one of these currently invested in ethical unit trust funds. My interviews loosely followed a script which asked questions in particular about the motives people had for investing ethically, what they thought was ethical about their investment, and how they reconciled the fact that they tended to invest ethically and non-ethically at the same time. The interviews were recorded and transcribed. The interviews with EIRIS members were then coded in HyperResearch, a qualitative data analysis software tool. I have not reported this work in detail here. Accounts of it are contained in two conference papers Lewis and Mackenzie (1995) and Mackenzie and Lewis (1996). However, I have referred to the transcripts frequently in the development of my arguments here, and occasionally quoted from them.

Over the period of research I also attended a number of conferences and seminars on the subject of ethical investment. These were attended by ethical investors, industry insiders or both including: The United Nations Environment Programme conference on ethical investment and local authorities (1996), various UK Social Investment Forum seminars, the UK SIF AGM in 1995 and 1996, the 1995 Shared Interest AGM, the 1995 INAISE Birmingham conference, and the Christian Ethical Investors Group AGM.

Finally I have participated in a number of discussions devoted to ethical investment on email 'lists' such as SRB (Socially Responsible Business) and SIF-L (Social Investment Forum).

1.2.5 Personal experience

Ordinarily one might expect to find 'personal' comments related to a PhD in the acknowledgements section, or in a foreword. However, in this case, these comments have significant methodological implications so it is appropriate that they are introduced here. I am not a researcher independent from the field of ethical investment, researching it entirely impartially and objectively. In 1991-92 I worked as a researcher for New Consumer. New Consumer is a public interest research charity devoted to the promotion of ethical consumerism. This is not quite ethical investment, but it a is strongly related field. In 1992 I was commissioned by the Joseph Rowntree Charitable Trust to write a guide to shareholder action. My remit was to produce a practical guide to show people how to take shareholder action on UK companies. *The Shareholder Action Handbook* (Mackenzie, 1993) was the result. Shareholder action is one important part of what some ethical investment funds do. I happen to know that my book has been bought, and occasionally read, by a number of those involved in running ethical funds. Also, in 1995 I founded a 'Website' on the Internet called Ethical Business (http://www.arq.co.uk/ethicalbusiness). This site contains, among other things, links to many of the key ethical investment institutions, and I have been personally involved with helping several such organisations make use of the Internet. I have also been working with the UK Social Investment Forum on the proposed *Investing for Change* Website. These activities make me, to some extent, an insider. This has the advantage that I am perhaps more easily trusted by other insiders. It was probably an important factor in gaining privileged access to Friends Provident Stewardship, for example. It also may mean that I have developed an insider's understanding of some of the issues.

This is an important point to make considering that one central part of the methodology I set out in the first half of this chapter involves the interpretation of the shared understandings of the ethical investment community. If I am already an insider, to some extent I may perhaps be regarded as having a more immediate access to these understandings than an independent external observer. It is also true to say that being an insider meant that the problems of ethical investment, are to a certain extent *my* problems. Engaging argumentatively in debate with the traditions of ethical funds is a natural activity for me. The drawback of this intimacy is that I risk, as anthropologists put it, 'going native,' and thus compromising my reliability as an 'objective' observer. There is some truth in this. It may be possible to be too 'close' to the shared understandings I am interpreting, and thereby failing to grasp important aspects of them.

2. Survey of the Literature

In the previous chapter, I offered a survey of some of the important literature which provides the disciplinary and methodological framework for this thesis. However, I have not yet considered the literature which is related to ethical investment itself. There are two important reasons why I need to do this. One is to provide some general background into the kind of work that has been done in this area, indicating where it relates to my work. The other is to support the claim that my descriptive account of the procedures used by ethical investment funds is an original contribution to the field of business ethics. As I said in the Introduction, I do not believe that another study of this kind has yet been produced. This is not easy to prove. It is difficult to prove the *absence* of a literature. However exhaustive one's literature search is, one can always feel that somewhere, someone might have published a detailed report on the subject. I cannot prove that this is not so. In a lengthy search on various bibliographic databases and thesis bibliographies I have found no such texts. I have found over 100 books and articles on issues relating to ethical investment, but, in none of the bibliographies of these works have I found reference to a text that describes in detail the procedures used by ethical funds. This increases my confidence in the belief that no such work has so far been produced.

One consequence of the fact that the particular topic of this thesis has not been addressed any detail in the literature is that most of the articles and books I refer to are only tangentially related to my key topics. Therefore, for the most part I confine this review to a brief survey of their topics, and forego the detailed critical engagement which would ordinarily be appropriate. Ordinarily many of the works cited in a literature review would be making claims which directly relate to the topic of the thesis; claims which should be assessed, accepted or rejected. Because these circumstances do not apply in this case, I have not considered it sensible to embark on this difficult task. There are however a small number of exceptions which I identify below.

The literature on ethical investment is written by writers from many disciplines, and falls into various categories. The disciplines represented include philosophy, law, economics, sociology, policy studies, psychology, management studies, and theology. One should also note a large number of works by journalists and other non-academic writers. The topics under which the articles fall can be categorised in various ways. I have chosen the following headings: work by business ethicists; work on ethical investors and their motives; work on the financial performance of ethical funds; and general surveys, and guides to ethical investment for investors.

2.1 Business ethics and Ethical Investment

While I have argued that this thesis can be regarded as a work of business ethics, comparatively little work has been done within business ethics on the subject of ethical investment. However, there have been some significant attempts by business ethicists to address the topic, notably de George (1990) and Sorell and Hendry (1994), and to a smaller extent in Sternberg (1994). Perhaps the most argumentative contribution on the ethics of ethical investment to be published, at least in the UK, is *What has "Ethical Investment" to do with Ethics?* (Anderson, et al. 1996). While none of the authors of this report can properly be regarded as a business ethicist, two of the co-authors are reasonably well known philosophers - Anthony O'Hear and Roger Scruton. And the report certainly does engage with the *ethics* of ethical investment. I will be considering this report in considerable detail in Chapter 7, so I will not do so here.

De George covers ethical investment in a miscellaneous chapter on 'Corporate Responsibility, Social Audit, and Ethical Investing' (1990). He opens with a discussion of the responsibilities of shareholders, making the arguable claim that shareholders are part-owners of companies (1990:173). De George goes on to claim that 'Shareholders cannot be held morally responsible for what the firm does since the shareholder is in fact very distant from the causal relations between an action of the corporation and its effects - but this does not relieve shareholders of all moral responsibility' (1990:174). Indeed he argues that if a 'company has a policy of engaging in unethical practices, then no one can morally support its activities through the purchase of its stock' (1990:174). This, and the various other claims he makes based on it, are important for this thesis because they accord with the conception held widely within ethical investment of what I have called the 'investment ethics problem'. I return to discussion of this in Chapters 5 and 8. De George's account of ethical investment is generally a normative one - it asserts what ethical investment should involve, rather than offering any practical account of what is actually involved in practice. In general though de George is strongly supportive of the idea of ethical investment and takes the trouble to rebut various criticisms of ethical investment - that ethical investment, if done properly, is too demanding to follow in practice; that if ethical investors divest from companies with unethical practices, they will loose their ability to influence the company and other less scrupulous investors will invest instead; that ethical investment fails to consider the fiduciary responsibility of investment managers; that there is no evidence that ethical investment actually applies pressure on companies to change their policies. The most important of these arguments for this thesis are the second and final ones. The second is considered at length in Chapter 8, the final one is a central topic of the second half of this thesis. De George notes the existence of ethical mutual funds - the American form of ethical unit trusts- but does not subject them to any detailed examination or criticism.

Sorell and Hendry discuss ethical investment within the framework of a chapter on ‘Shareholders’ (1994), and like de George, they begin with a discussion of the responsibilities of shareholders. Unlike de George, they claim that shareholders are not the owners of companies (1994:113). This question of whether shareholders can be regarded as owners is an important issue which will be discussed in Chapter 8. However, despite their rejection of the conception of shareholders as owners, Sorell and Hendry accept that shareholders do have responsibilities for companies. Their discussion is not related to the kind of issues ethical investors are concerned about but to more general considerations of, for example, the duties of loyalty owed by shareholders to companies in the event of a take-over bid (1990:117). Like de George, Sorell and Hendry have a separate section on ethical investment. Unlike de George’s discussion, their account does go into a fair amount of detail about the practice of ethical investment, briefly reviewing three ethical funds, including Friends Provident Stewardship which is the main focus of the first part of this thesis. Sorell and Hendry also consider various ‘alternative’ ethical investments, such as Shared Interest, Traidcraft, Mercury Provident (now Triodos), and the Industrial Common Ownership Foundation. Shared Interest, for example, is an industrial and provident society which takes deposits from first world investors, and lends them to small co-operative business in third world countries. During this thesis I interviewed 10 Shared Interest members to seek to understand their motives. However, Shared Interest is not a conventional ethical fund, and according to the definition of my topic in the Introduction, I will not be considering it, or any of these other alternative investments in any detail.

Another important issue raised by Sorell and Hendry is the question of whether the ethical concerns of ethical investors conflict with their other objectives or duties as shareholders. As they say ‘aren’t the interests of ethical investors in things other than owner value going to conflict with the interests of those shareholders who *are* concerned with owner value and nothing else?’ (1994:131). If so, can ethical investment be properly regarded as an ethically appropriate activity? In my definition of the topic of this theses in the Introduction I have said that this important issue is beyond the scope of this thesis. My intention is to describe and critically engage with the procedures and purposes of ethical investment, not to assess whether it is an ethically appropriate enterprise to begin with. However, given the importance of the issue, it is appropriate that I at least attend to it, even if I do not attempt to reach a conclusion. Earlier on in their book, Sorell and Hendry argue that

> ‘To purchase shares other than for the purpose for which they were intended is...to misuse the relationship of shareholding to the potential detriment of the business and so is morally questionable. The same argument can be applied to any investor who...is investing on a basis that is at variance with the concept of shareholding.’ (1990:119).

Ethical investment might be construed as motivated not by a desire to increase long term owner value, but as an attempt to persuade the company to change its ethical policies. Corporate reform is certainly one important goal of ethical investment. In certain circumstances ethical investors may wish the company to reform its policies in ways that harm its long term value. Seeking to persuade an arms company to stop producing arms, or a brewery to stop making beer, would seem to be good examples. Alternatively, one might consider a pressure group such as the RTZ campaigning group Partizans, which routinely buys token shareholdings so as to attend RTZ AGMs in order to put public pressure on the company to persuade it to change its environmental policies.

Sorell and Hendry’s response is to argue that it is possible for an investor to be simultaneously interested in increasing long-term owner value and in pursing ethical goals. This in general would seem quite plausible. Indeed, there are some, such as the members of the Tomorrow’s Company committee (Tomorrow’s Company, 1995) who argue that the pursuit of certain ethical and environmental objectives can be regarded as *improving* the long term performance of the business. There are many ways in which improving ethical and environmental status can do this; by, for example, enhancing the corporate reputation, anticipating environmental legislation, improving relations with consumers and employees, as well as direct improvements to profitability which sometimes arise. The basic argument is that ethical business is often good business. Indeed the new Kleinwort Benson 'Tomorrow's Company Fund' is based on the premise that by investing in enlightened, 'inclusive' companies, one should expect long term financial performance significantly *higher* than average. However, while it is possible that ethical investors' ethical objectives will not conflict with the objective of maximising long term owner value, in the examples I gave in the previous paragraph conflicts may well arise. Sorell and Hendry do not give a full answer to this problem. However they suggest that it involves deep questions about 'how far the obligations that derive from the roles one has, including that of investor, can free one from the obligations that one is under as a human being' (1990:131). This could be taken to imply that there may be circumstances when one may regard one's wider ethical responsibilities to be over-riding the narrow ones due to a particular role. If so, ethical investors may claim that their more general ethical responsibilities are more important than their narrow concerns as shareholders. Another somewhat similar response to this is provided by Sternberg:

> What if owners want something other than maximum financial value from their organisations?...Owners are perfectly entitled to devote their organisations to all sorts of ends. To the extent that they pursue something other than maximum long-term owner value, however, they are simply not engaging in business.' (Sternberg, 1994:45)

One might argue that in their role as human beings, shareholders may have higher goals which lead them to devote their company, at least in part, to objectives other than the maximisation of long term owner value. Sternberg does consider shareholders to have certain responsibilities, particularly to other shareholders, but, at least in her more recent writing,[1] she does not appear to consider shareholders to have general responsibilities of

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[1] In an earlier paper quoted by Sorell and Hendry, Sternberg says 'Real corporate loyalty is...being true to the proper purpose of the corporation - in the case of a business, to maximising shareholders' long term value.' (Sternberg, 1992:196) This approach would seem to rule out certain kinds of ethical investment, much as Sorell and Hendry's does. However, this sentence is not present in an otherwise nearly identical passage in her more recent book (1994:206). In her new account, shareholders do not appear to have particular responsibilities to corporations, only to *their* proper ends for investing in the company.

loyalty to companies. She seems to suggest that the main reason to be a 'responsible shareholder' arises from the requirements of prudence to insure that the companies the shareholder invests in are well managed (1994:207). However, Sternberg's teleological approach to ethics places the maximisation of long term owner value as the defining purpose of business. With some general exceptions, its pursuit over-rides all other concerns, so she would rather that ethical investors (and ethical consumers) do not seek to divert business from its primary purpose, but instead commit their resources to other charitable ends. (1994:261). However, one of the ideas behind ethical investment and ethical consumerism is that the most effective way of addressing social and environmental problems is not by engaging in charitable works, but by seeking to harness the vast economic power of business to these ends. Sternberg's teleological approach limits her ethical domain to the world *within* the business enterprise. The activities of managers are to be justified in terms of their consistency with the end of 'maximising owner value over the long term by selling goods and services' (1994:6).[2] It is hard to see what resources she can draw on to challenge ethically motivated owners of business if they want the business to pursue non-business objectives as well as long term owner value. On Sternberg's definition of business, this would mean that the resulting entities will be to some extent quasi-businesses, rather than pure businesses *per se.* But on what basis can she claim it is wrong for owners to urge their companies to be quasi-businesses, pursuing both owner value and wider ethical goals at the same time?[3]

2.2 Ethical investors and their motives

One area of research on ethical investment is empirical research on the attitudes and behaviour of ethical investors. This research is motivated by two concerns in particular: the desire to understand the behaviour and motives of ethical investors, and the desire to use ethical investors as counter examples to the narrow assumptions of human motivation sometimes made in rational choice and consumer choice theory in economics. Conventional economic theory, at least on some standard interpretations,

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[2] Sternberg, like de George, but unlike Sorell and Hendry, considers shareholders collectively to be owners of the business (1994:200).

[3] Ironically, if the Tomorrow's Company report is right, such quasi-businesses might actually be more effective at achieving owner value than those which focus on the narrow pursuit of this goal. But this raises deeper issues than I am able to address here.

assumes individuals to be selfish utility maximisers. However, there is a long history of criticism of this narrow view. Recent examples include, Elster, (1983), Etzioni (1988), Simon (1976), and Hausman and McPherson (1993) provide a useful survey. Much of this work on ethical investors has been carried out within the field of economic psychology, or behavioural decision theory. A central preoccupation of these sub-disciplines is to provide a more psychologically sophisticated account of economic action than is available in standard economics (see for example Thaler, 1994). It is argued by Lewis and Cullis (1990) that the behaviour of ethical investors might offer a useful case study for this approach. Ethical investors are, on the face of it, engaging in economic action on ethical grounds as well as simple financial ones, and may even be prepared to accept financial loss in order to achieve their ethical ends (Cullis, et al. 1992; Lewis and Webley, 1994). This work sometimes relies on experiments (Webley, 1992), sometimes statistical analysis of the relationship between different kinds of ethical concerns among investors (Anand and Cowton, 1992), and sometimes qualitative interviews with investors (Mackenzie and Lewis, 1996), and sometimes a combination (Lewis, et al., forthcoming). In an early paper of this kind, Lewis and Cullis argue for further research, particularly in the areas of 'interviewing and rhetorical analysis', 'case studies' and 'experiments and simulations.' (Lewis and Cullis, 1990:408.). By interviews they particularly refer to interviews with fund managers, and by rhetorical analysis, they refer to an analysis of the marketing material of ethical funds. By case studies they refer to participant observation of ethical investment. During the writing of this thesis I have interviewed a number of those who provide and sell ethical funds, I have examined the marketing literature, and I have engaged in participant observation with the largest ethical fund, Friends Provident Stewardship. Examples of work on ethical investors that does not have this theoretical agenda are fewer, but include, for example, the work of Rosen et al. (1991), and Inskeep (1992), and a number of market research surveys including NOP (1995) and NPI (1995b).

2.3 Financial performance of ethical funds

There has been some writing on the relative performance of ethical investment compared to conventional investment (Lashgari and Gant, 1989; Mueller, 1991, 1994; Joly, 1992; Luther and Matatko, 1993; Sparkes, 1995). One impulse for such studies is that for ethical investment to be 'authentic' it must involve some financial cost

(Mueller, 1991). Some studies indicate some underperformance over particular periods. (Luther and Matatko, 1993; Mueller, 1994; Mueller, 1991) Luther and Matatko offer evidence that ethical funds have underperformed the UK stockmarket as a whole between 1985 and 1992. However, they say that ethical funds are heavily concentrated in the smaller company sector, which performed poorly over the period they studied. If this factor is removed, they conclude that 'ethical investment appears to have been financially as well as morally rewarding' (Luther and Matatko, 1993:9). Mueller's study (1991) of US mutual funds between 1984 and 1988 shows that most funds underperformed an appropriate index by 1% per year taking risk into account. His (1994) study of one particular Islamic ethical fund found that it underperfomed over 1987-1992 period. Although what is true for one Islamic fund may not be true for non-Islamic ethical funds, or for ethical funds as a whole.

However, Lashgari and Gant (1989), argue that companies which adopted the Sullivan principles in South Africa, outperfomed the Dow Jones index. Sparkes and Joly both argue that ethical funds need not lead to underperformance, and several ethical or green funds have performed excellently. According to the quarterly PIRC Index of Ethical funds in the UK, 'ethical and green funds have tended to outperform conventional unit trusts over the medium and long term, though individual performance between funds can vary markedly and the market as a whole has generally done better' (PIRC, 1996:3). The outcome of these debates is, however, not settled. Assessing stock market performance is in general a notoriously difficult task. For example, it is very difficult to establish an agreed means for deciding what counts as a benchmark against which to measure the performance of a company or a fund. It is not surprising that assessing the performance of ethical funds is controversial.

2.4 General surveys

The most substantial work of any kind on ethical investment is the vast *Social Investment Almanac: a comprehensive guide to socially responsible investing* (Kinder, Lydenberg and Domini, 1992). The eponymous claim is certainly ambitious, but at 900 pages the guide can generally claim to be fairly comprehensive. It contains papers by a number of leading figures in the social and ethical investing movement, particularly in the US, detailing the history, shape, research, diversity of method, and international distribution of socially responsible investment. However, it does not contain a detailed account of the procedures used by ethical funds. Perhaps one small oversight in its claim to be comprehensive!

There have also been a number of general surveys on ethical investment. Cowton (1994), in his survey of ethical investment, defines ethical investment as ‘the exercise of ethical and social criteria in the selection and management of investment portfolios, generally consisting of company shares’ (1994:215). This definition is not quite accurate for two reasons. Firstly, as we shall see in Chapter 4, the selection of investment portfolios by ethical funds is not only based on criteria, but also on wider kinds of judgement. Secondly, ethical funds may also pursue more active engagement with companies in order to persuade them to change. Furthermore, for some funds at least, this is an important distinction which will be considered at length in this thesis. The rest of Cowton’s article is a survey of the shape of ethical investment in the UK, primarily based, it seems, on a study of ethical funds’ marketing material. He is critical of some of the language used by ethical funds to describe their criteria. This is a problem we will consider in Chapter 5. Cowton also emphasises the marketing dimensions of ethical funds. For example, he suggests that the selection of the particular criteria used by ethical funds is ‘essentially...a marketing question’. This may be true for some funds, but as we shall see in Chapters 4 and 7 it is probably not true for others. In particular it may not be true for Friends Provident Stewardship, which appears to choose its criteria at least as much on ethical grounds as on marketing ones (and this fund comprises more than half of the overall ethical investment market).

Other surveys include Rockness and Williams (1988), and Perks et al. (1992) and there are some journalistic surveys (Dowie, 1993; Entine, 1994, 1996; Millar, 1991). Rockness and Williams’ work is based on a large questionnaire survey of ethical funds in the US. It focused on how ethical funds choose companies for investment, what criteria they use, how ethical funds monitor companies, the sources of information the funds used, the shape of the ethical funds’ portfolios, and their perceptions of the need for greater corporate social reporting. Many of the issues this research raises are of direct relevance to this thesis. In particular I am interested in the procedures by which ethical funds choose companies for investment. This is a central topic in Chapter 4. However, Rockness and Williams’ study has not been as useful to my research as I had initially hoped. This is partly because it is nearly 10 years old, partly because it concerns US mutual funds, but mainly because it gives very little detail about procedures. In fact the question about how ethical funds choose companies for investment follows a multiple choice approach. Five of the six funds which filled in the questionnaire agreed that 'When evaluating firms with your social criteria, which of the following best describes the process you use?...b.)To be included in the portfolio a firm's performance on each criterion must meet some minimal level.' (1988:399). As my task is to develop a *detailed* understanding of how ethical funds operate, this is not a very informative finding.

Bruyn's work (1987) is the largest general academic study in the area of ethical investment. However, Bruyn's concerns are rather different from those in this thesis. To begin with he is only marginally concerned with ethical unit trusts or mutual funds but is more concerned with much wider questions about the role of investment in society. His aim is to develop a new kind of normative theory of investment which seeks to balance social and market objectives. This takes his study far into considerations about what Sorell and Hendry have called 'broad' business ethics. As I have said, my thesis is concerned with ethical investment in a much 'narrower' way. Bruyn's work has received thorough criticism by Owen (1990).

There have been a small number of surveys on certain aspects of ethical funds' procedures. For example, Buzby and Falk (1978; 1979) did surveys of the social responsibility attitudes of mutual funds and of university investors. This research is useful but extremely dated. It took place before there were any ethical funds in the UK. Cowton, on the other hand, has done a more recent survey of EIRIS clients (Cowton, 1989). It reports the frequency of selection of particular kinds of criteria by 111 EIRIS clients, including ethical unit trust clients and private clients. It also sketches how EIRIS works. He reports a 'core' set of exclusions by ethical unit trusts: armaments, alcohol, gambling, tobacco and South Africa, and said that most of EIRIS clients went beyond this core. Cowton identified environment and employment as areas which he believed there was demand for, but which EIRIS did not cover well in 1989. He has also done work on company size as a dimension of ethical investment (1990b). While Cowton's work touches on certain aspects of the ethical funds process, notably their choice of ethical criteria areas, this is tangential to the main thrust of this thesis. Indeed, in the Introduction, I explicitly excluded detailed consideration of the particular criteria chosen by ethical funds from this study. However, in Chapter 5 I discuss the narrowness of the ethical concerns adopted by most ethical investment funds. This issue has been touched upon by Entine (1996) and Langbein and Posner (1980).

Another area of work which touches on an issue that I consider in this thesis concerns the efficacy of ethical investment as a means of changing companies through what I call in Chapter 6, ‘market signalling’. Some of the journalistic, non-academic surveys on ethical investment have argued that ethical funds are unlikely to be effective in this respect (Miller, 1991; Dowie, 1993). Folger and Nutt (1975) have, in passing, suggested that the idea that ethical funds might exert long term downward pressure on share prices is dubious. Lundahl (1984) and Kaempfer et al. (1987) raise questions about the efficacy of investment sanctions as a means of ending apartheid in South Africa. Shoenenberger (1993) also directly addresses the efficacy of ethical funds as an ‘instrument of change’. His work is based on a questionnaire survey of UK ethical funds, and is relevant to my argument, and I have referenced it where appropriate.

2.5 Practical guides to ethical investment

Many practical guides to ethical investment, oriented to the investing public have been written in the last decade. Lang (1996), Mackenzie (1993), Sparkes (1995), and Ward (1986) have written guides to various aspects of ethical investment in the UK. Alperson (1991), Brill and Reder (1992), Domini and Kinder (1986), Harrington (1992), Judd (1991), Kinder (1993), and Lowry (1991) have done the same in the US. These guides are not academic studies. Many of them are written by people who work within the ethical investment business - notably Sparkes, Ward, and Domini and Kinder. This means that they provide useful insights into the shared understandings of the ethical investment community. In addition, they all contain interesting accounts - often not entirely consistent - of the history, purpose and practicalities of ethical investment. Sparkes’ work in particular contains a very recent survey of ethical unit trust investment in the UK, covering such topics as the history of ethical investment, a brief account of how they work, the role of financial advisors in selling ethical investment, the financial performance of ethical funds. This, and some of the other guides, offers valuable material for this study which is referenced elsewhere in this text.

2.6 Conclusion

This literature review has frequently been rather cursory and has not attempted to engage in detailed critique of each of the works cited. The principal justification for this is that few of them address the central topic of this thesis: the procedures and ethical purposes of ethical investment. Where they do I have tried to either offer more detailed consideration or note where in the main text further reference to the issues they raise can be found. In my study of the literature on ethical investment I have not found any studies offering detailed, descriptive accounts of the procedures used by ethical funds like that given in Chapter's 3 and 4. With one or two exceptions, I have also not found concerted attempts to argue about the ethical efficacy and purposes of ethical funds in the way I have attempted in the second half of this thesis. This can perhaps be regarded as evidence that such works do not exist. There are several possible reasons why this work has not been done. Ethical funds were only established rather recently, particularly in the UK. And it is only even more recently that they have grown to a significant size. Doing the kind of qualitative interview work I have undertaken to prepare Chapters 3 and 4 is time consuming and difficult. The payback in terms of published papers may well be higher for quicker, easier questionnaire surveys than it is for qualitative work. Ethical funds may have been reluctant to let researchers gain the necessary access. As I have said, I am the first to have been given this access to Stewardship, which would be the obvious fund to choose for anyone doing a case study of ethical investment in the UK. I am not sure which, if any, of these reasons are correct, but they may help support my claim that important parts of the work contained in this thesis are original and advance the study of the subject.

The methodological preliminaries now over, we can move to the main topic of this thesis, beginning with an account of the history of the emergence of the first ethical unit trust in the UK.

3. History and Structure of Ethical Investment

3.1 Introduction

This chapter provides an overview of the history of the emergence of ethical unit trust investment in the UK, and an outline of the institutional apparatus by which ethical funds are provided. This chapter, like the next, focuses largely on Friends Provident Stewardship. From a historical point of view this is entirely appropriate as Stewardship was the first ethical fund. By understanding how Stewardship came to be, one thereby understands most of the story of how ethical funds came to be. But Stewardship is a uniquely useful case study in another sense. Friends Provident Stewardship is the largest family of funds in the retail ethical investment market. In September 1996 its main Stewardship Unit Trust had over £303.7m under management, and the Stewardship Pension Fund had £301.9m invested with it. Together with three smaller funds there was a total of £650m of funds under Stewardship management. This means that Stewardship comprises over half of the total ethical unit trust market. While the 30 or so ethical funds which have followed Stewardship differ in important details, many have followed elements of the Stewardship approach. In addition most of them derive their research from the EIRIS research organisation (see p.75ff.), which has been heavily influenced by Stewardship in its development. All this means that in attempting to understand how ethical unit trusts work in the UK, there is no better place to start than Stewardship.

The following is an attempt to summarise key elements of the Stewardship process, its history and management. While some attempt is made to consider the financial management of the fund, the central focus of this study is the *ethical* elements of the Stewardship process.

3.2 The emergence of the first ethical unit trust[1]

The first and main Stewardship fund was founded in 1984 when the ethical investment concept was taken up by Friends Provident. To some extent, the emergence of the Stewardship fund is the result of two separate stories: the birth of the Stewardship concept, and the history of Friends Provident. First is an account of the emergence of the Stewardship concept.

Ethical investment is a venerable idea. The question of the ethics of investment goes back at least to Biblical times and the prohibition in Jewish law on usury. John Wesley, founder of Methodism, emphasised in the 1700s that the use of money was the second most important subject of New Testament teaching. He gave four consecutive addresses entitled: ‘Earn all you can’; ‘But not at the expense of conscience’; ‘Not at the expense of our neighbours’ wealth’; ‘Not at the expense of our neighbours’ health’ (Jacob, 1996:2). These themes have influenced ethical investment since then. However, what is currently recognised as ‘ethical investment’ - the practice of investing funds on the basis of a set of ethical criteria - is more recent. In the first half of this century a number of Church organisations had adopted various ethical prohibitions on certain kinds of investment, particularly those which have become known as ‘sin stocks’: alcohol, tobacco, gambling and arms. In the US in 1928, the Pioneer fund was set up, with a policy of deliberately screening certain investments on ethical grounds (Harrington, 1992:6). However, the current interest in ethical investment began in the late 1960s. A number of church investment funds started to explore ways of avoiding investments in companies operating in South Africa or involved in the Vietnam war. In 1970 the first ethical mutual fund, the Pax World Fund, was established (Harrington, 1992:7). This was shortly followed by the Dreyfus Third Century Fund in 1972. In the UK, the Church Commissioners of the Church of England had imposed some ethical restrictions on their investments since 1948 but as in the US, it was not until the late 1960s that discussion began about ethical unit trusts.

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[1] On matters of fact this history relies heavily on unpublished manuscripts by Lyn Wilson (Wilson, 1994) and Charles Jacob (Jacob, 1996). Wilson has been a board member of Friends’ Provident Life Office since 1981, and is a member of the Religious Society of Friends. Jacob is the originator of the Stewardship concept. Both have been members of the Stewardship Committee of Reference since it was founded in 1984.

In the late 1960s, Charles Jacob, soon to be the investment manager of the Central Board of Finance of the Methodist Church, began to explore the possibility of setting up an ethical unit trust in the UK, similar to the US ethical mutual funds. He received the practical support of First Investors, an asset management company, and encouragement from Richard Rowntree of the Joseph Rowntree Social Services Trust. In 1973, together with Jeremy Edwards, of First Investors, he prepared a proposal for a trust entitled 'Stewardship' inspired by a passage on the rightful use of money in the 'Parable of the Talents' in St. Matthew's Gospel (Matthew 25: 14-29). One aspect of the US ethical mutual funds which dissatisfied Jacob and Rowntree was their dominant negative emphasis on avoiding companies engaged in unethical activities. He therefore sought to develop a trust with a more positive approach. As Richard Rowntree put it later, in a letter to the Financial Times

> 'the initial plans for a Stewardship trust have always been clear that the essential criteria must be the positive aim of investing in companies, the bulk of whose products, services and operations are of benefit to the community rather than the negative withdrawal from specified activities.' (Rowntree, 1984) .

This can be seen in the objectives of the trust as they appeared in the initial proposal document.

> 1.To provide a unit trust suitable for corporate and individual investors, who for social or religious reasons are concerned that their investment should be confined to companies whose operations are of benefit to the community. As a result, industries such as tobacco, breweries, gambling and armaments, would be among those to be excluded as would investment in companies whose income was largely derived from countries which adopt a policy of apartheid.
>
> 2. Through the formation of the trust, to create an increased awareness of the responsibility of ownership at national level and to provide a suitable avenue though which those members of the public already conscious of their social responsibility, are enabled to invest in equity (in some cases for the first time) without disturbing conscience and with the diversification advisable for their requirements.
>
> 3. By using votes and influence to support and provide encouragement to companies fulfilling a useful purpose in the maintenance of their standards.
>
> 4. To obtain growth of capital values and reasonable yield by investment in a selected portfolio on the lines of that shown in Appendix 'A' to this proposal.

(Jacob and Edwards, 1973:1)

Over the years support was sought for the Stewardship idea from a large number of financial institutions and individuals, including, for example, Legal & General, Kitkat & Aitken, the Cadbury Trusts, John Govett Group and Lord Seebohm.[2] However, in the end the progress of the idea was halted by the Department of Trade, which objected on two grounds. First, because it considered there to be a conflict between the demands of capital and the demands of conscience. It is the legal responsibility of unit trusts to produce a financial return for the investors, but it was argued that by restricting its investment by ethical criteria a Stewardship trust would jeopardise that goal. The other objection was that, as public opinion changes over time, there may be pressure for an ethical fund to change its ethical policies; but if an ethical fund responded to this pressure by making changes, it would then be in conflict with the previous ethical policy endorsed by earlier investors.

Despite this setback, discussion about ethical investment continued in the UK during the 1970s, particularly among the Churches. According to Jepson (1995:6), the British Council of Churches published a report in 1973 advocating shareholder action on companies operating in South Africa. Christian Concern for South Africa (CCSA) was established. Part of its role was to advise the churches on their investment in South Africa (Jepson, 1995:12). In 1978, Trevor Jepson, chairman of CCSA wrote a report suggesting the need for a research body to provide the churches with information about various ethical aspects of corporate practice, which could be used to guide their investment policies. In 1980 the Young Friends Central Committee published ‘Responsible Investment - A Challenge to Quakers’ which examined the investment of Quaker funds (Jepson, 1995:12). Jepson drafted a plan in 1981 for establishing an ‘ethical investment information service’ (1995:12), that would employ one full-time staff member plus some secretarial support, and would be controlled and financed by participating organisations such as Joseph Rowntree Charitable Trust (JRCT) and the Society of Friends. In the 1970s JRCT was gradually diversifying its investments out of the Rowntree company. In doing so it became increasingly concerned to develop ethical

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[2] Coincidentally Lord Seebohm was a non-executive director of Friends Provident at that time. Back then, Seebohm thought that it would not be possible for Friends Provident to support a trust that was curtailed in its actions by ethical constraints.

criteria by which investments could be selected. In Jepson's plan, the proposed research organisation would mainly provide information on matters requested by its participants and gradually build up a regularly updated dossier on companies which fulfilled certain criteria (1995:12). Whilst discussions were underway about the founding of this ethical investment research service, the Political Ecology Research Group at Oxford was thinking of setting up a similar research body, devoted to compiling information on corporate environmental practice, focusing not just on the negative aspects, but also positive environmental practices. However, the idea was not pursued when this group learnt of the plans for EIRIS (Jepson, 1995:13). Finally, EIRIS was established in 1983 with the help of the Joseph Rowntree Charitable Trust, the Joseph Rowntree Social Services Trust, the Society of Friends, the Methodist World Development Action Fund, Oxfam, the Church of England's Board of Social Responsibility, the Presbyterian Church in Ireland and the Church in Wales. The 'launch edition' of the EIRIS Newsletter states four main aims for EIRIS:

> Firstly, to provide information to individual investors who wish to avoid certain forms of investment, such as brewing, tobacco or armaments.
>
> Secondly, to provide information on a wide range of issues, such as employment policies, environmental impact, advertising, involvement in South Africa or the third world, which will provide positive, as well as negative, criteria for investors.
>
> Thirdly, to identify forms of investment which meet certain non-commercial requirements on the part of the investor.
>
> Fourthly, to promote a wider public understanding of and debate on corporate social issues. (EIRIS, 1983:1)

At around the same time as EIRIS was being prepared for launch, discussions were also taking place at the West Midlands County Council about the investment policies of local authority pension funds. These discussions led to the foundation of Pensions Investment Research Centre in 1984 (Jepson, 1995:13), which has subsequently become PIRC Ltd. and which in 1995 received considerable press attention for its shareholder resolution on director's pay at the British Gas AGM.

In 1978, with the support of Sir Nicholas Goodison, Chairman of the Stock Exchange, a new application for a Stewardship fund was made to the Department of Trade and Industry, as a joint venture between Goodison's firm Quilter Goodison, and Jacob's

Linvest Securities. This time the concept was approved in principle. One reason for the change of heart is believed to be that the application was made at a much higher level, by a top City figure. It is also possible that social change in the 1970s had put ethical and environmental aspects of corporate behaviour rather higher up the public agenda than they were previously. Having achieved approval in principle, Charles Jacob approached Richard Rowntree for support. While the Joseph Rowntree Reform Trust was no longer inclined to participate financially, the Joseph Rowntree Charitable Trust pledged its support and helped to form a new committee to develop the fund. By the time this development had been completed, Jacob's own circumstances had, however, changed, and he no longer felt able to provide the depth of research which was essential for the efficient management of an ethical fund. While an alternative management structure was being contemplated, a timely meeting between Rowntree Trust Committee members and directors of Friends Provident provided the solution. We now take up the history of Friends Provident.

Friends Provident was established in 1832 as a mutually owned 'friendly society' to provide life insurance for its members. It was founded by two members of the Religious Society of Friends, or Quakers: Samuel Tuke and Joseph Rowntree. Friends Provident started as a solely Quaker institution, indeed membership was only available to members of the Religious Society of Friends. However, this century has seen a gradual weakening of Quaker influence in Friends Provident. In 1915 the society converted into a corporate institution with membership no longer limited to Quakers. In 1918 it bought the Century Insurance Company, and two, non-Quaker, representatives from this company were appointed to the Friends Provident board, which until then had been constitutionally restricted to Quakers. In 1942, the Quaker restrictions on board membership were relaxed further, when only a majority of Quakers was required on the board. In 1975 this process continued, requiring that there be a minimum of five Quaker members, rather than a majority; but stipulating that these five, if unanimous on issues of Quaker principles, retained the power of veto (although it was never used). Up to this point Friends Provident had been managed in accordance with Quaker beliefs and abstained from investing in companies involved in arms, alcohol, tobacco and gambling. In 1980 the board, now mostly secular, resolved to remove these restrictions on investment. This was partly because Friends Provident by now managed funds on behalf on many non-Quaker investors and it was felt that imposing Quaker restraints on investments was inappropriate. One of the Quaker directors dissented from this resolution and resigned. In mid-1983, the board of Friends Provident discussed whether to have a policy of not investing in arms companies. A vote was taken - perhaps for the first time on the Friends Provident board, which operated on a consensus model - and the policy was rejected. Two further Quaker members resigned as a result. Lyn Wilson, a Quaker board member, says that some of the Quaker board members saw themselves as representatives of the Society of Friends, and felt compelled by Quaker pacifist principles to resign, whereas others, himself included, believed that it was best to champion the cause of ethical investment from the inside. By the early 1980s Friends Provident had moved some distance from its Quaker roots, and had no explicit ethical policy for its investments. However, the board did not want to sever the connection with Friends completely. It was at this time that the possibility of managing an ethical unit trust came up. This offered the possibility of giving the Quakers and others concerned about the use and misuse of investment assets the prospect of a new 'ethical' home for their money, while not requiring Friends Provident as a whole to be limited in its investment by these principles. The board decided that Friends Provident should take up the ethical idea and launch the UK's first ethical unit trust - the Stewardship Unit Trust.

3.3 Overview of Stewardship

Friends Provident launched the Stewardship Unit Trust[3] on 1 June 1984, with the financial aim of achieving long term capital growth. Investment managers at Friends Provident and elsewhere in the City did not consider that Stewardship was likely to have a major impact, or to have strong prospects. Indeed for a time it was known as the 'Brazil' fund because it was considered a bit 'nutty'. It was estimated that it might grow to have £3m under management within a few years. However, these expectations were rapidly exceeded. In the first year the Stewardship Unit Trust had raised £1.5m in new

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[3] The first unit trust in the UK was launched in 1931 by M&G, inspired by the idea of mutual funds in the United States. In July 1996 there were 1,667 unit trusts operated by 164 unit trust management companies with combined funds under management of £123bn. These funds are largely made up of the private savings of small investors. Unit trusts are investment vehicles which pool the capital of a large number of small investors, and invest it most commonly in listed companies in the UK. Unit trusts can be distinguished from one another in two broad respects: one is the range of investment products they sell, and the other is investment policies they follow.

investment and outperformed the FT-SE A All Share Index. By the end of 1986 the fund was managing over £10m, and by mid 1996 it had over £303.7m under management. At the same time as launching the Unit Trust, Friends Provident also launched the Stewardship Individual Pension Fund, which has also done well and in September 1996 had £301.9m under management. In October 1987, the Stewardship Income Trust and the North American Stewardship Trust were launched. The Stewardship Income Trust followed Stewardship Unit Trust's ethical policy, but invested with a bias towards achieving income rather than capital growth. It was the first ethical income trust in the UK, and in September 1996 was valued at £66m. The North American Stewardship Trust aimed at longer term capital growth, and was managed by Vilas Fischer, a New York fund manager and associate company within the Friends Provident Group, which subsequently became Friends Vilas Fischer Trust Company when completely taken over by Friends Provident in 1995. The North American fund has assets of £6.6m. In 1993 the Friends Provident Ethical Investment Trust plc was launched to take the Stewardship approach into the investment trust market and in September 1996 had an asset value of £33.4m.

Friends Provident, more formally known as Friends' Provident Life Office, controls a group of companies which collectively manage over £19bn of assets. It can broadly be split into two, a retail Business Operations Group including provision of life and health insurance, personal pensions and unit trusts, actively marketing the Stewardship Unit Trusts; and the Stewardship Life and Pension Funds, as investment links to the various life and pensions products. The other business activity provides institutional fund management services through the Friends Provident Asset Management Group of companies. In the last two years Friends Provident Asset Management Group has proved effective at selling ethical and environmental versions of its asset management services - based on the Stewardship Unit Trust model - to a number of local authority pension funds, including Berkshire, Lothian, Lincolnshire, Merseyside, and Hampshire.

On the retail side, Friends Provident doesn't simply sell unit trusts, but sells a wide variety of financial products including unit trusts. It sells a number of life assurance products such as regular savings plans, capital investment bonds, and whole of life insurance and endowment mortgages offering the Stewardship Life Fund as one of its investment options. The Life Fund is worth £175m and around 99% of it is invested in the Stewardship Unit Trust (making up some 60% of the Unit Trust's total funds). It sells various personal and group pension plans again offering the Stewardship pension fund as an investment option. Finally it sells PEPs and unit trusts. It is therefore able to offer ethical funds links to a wider range of products than several of the other providers in the market place, which is an important reason for its continuing dominance.

Taken together the Stewardship funds have a very significant position in Friends Provident’s fund management operations. While collectively the Stewardship funds account for only about £700m of Friends Provident’s £19bn of funds under management, the Stewardship Unit Trust is now their largest unit trust. And its importance does not stop here. Stewardship receives rather more than its proportionate share of executive attention. Two main board members of Friends’ Provident Life Office sit on the Stewardship Committee of Reference (John Whitney and Lyn Wilson) and, until his retirement in 1995, Peter Silvester, managing director of Friends Provident Asset Management, and main board director at Friends’ Provident Life Office, took a very strong personal interest in the development of Stewardship. Within the marketing department more senior staff time is allocated to Stewardship than to the other unit trusts; Friends Provident also publishes detailed brochures for the Stewardship unit trusts, whereas some other trusts make do with more basic literature. Also, in the summer of 1996, Friends Provident began to issue a newsletter for Stewardship investors in addition to the half-yearly manager’s report. Frank Blighe, market development manager for Stewardship, also notes that Stewardship gets substantially more publicity than the rest of Friends Provident. Stewardship also has its own site on the Internet, ahead of the rest of the organisation.[4] One result of this preferential treatment is that the rate of growth of Stewardship has tended to be greater than that of Friends Provident’s other funds. Stewardship also boosts the image of Friends Provident as a whole. In addition, the high rate of retention of Stewardship investors makes this business more profitable.

Friends’ Provident Life Office is a mutual insurance company, which means that rather than being owned by shareholders, it is owned mutually by its members. This institutional structure is shared by a number of life insurance companies in the UK. It is a feature of their origins and it has had some influence on the development of the company. However, in recent decades it has become harder to distinguish differences in

[4] The author assisted Friends Provident in the development of this Internet initiative.

the behaviour of mutual insurers and other provident societies from those of ordinary public companies.[5] And the argument for mutual status has been losing support. A number of building societies have argued that mutual structure makes them ill suited to compete in the modern financial services market, and have converted to plc status. This trend is now making itself felt among the mutual insurance institutions. Norwich Union, one of the largest such insurers, has announced plans to convert to a public limited company. There is speculation that other institutions will follow suit. Friends Provident is often mentioned in the press as a hot tip for conversion or take-over by an existing company, notwithstanding Friends Provident's clear and publicly stated commitment to remaining mutual. If, notwithstanding Friends Provident's aversion to demutualisation, it were to convert into a quoted company, there may be consequences for Stewardship. But, given that the Stewardship brand has proved profitable, it is probable that it would be left reasonably untouched by demutualisation. However, for those attracted to Stewardship because of the arguably ethically superior status of its parent institution, demutualisation might be a disadvantage.

3.4 Overview of other ethical funds

The history of ethical investment consists of rather more than the formation and development of Friends Provident Stewardship. Friends Provident now provides five of more than 30 ethical funds. Stewardship is still by far the largest group of funds, which is one reason why it makes such a significant case study. But it is important to give a more general picture of how Stewardship compares to other funds within the ethical investment business. Table 1. (below) provides a list of the ethical funds currently in existence ordered according to their launch date, and giving their total funds under management as of November, 1996.[6]

Table 1.[7]		**Value of funds**
Fund	**Date of Launch**	**November 1996**

[5] Having said that, in the last two years some of the building societies that have opted to retain mutual status have started to make a virtue of not having to please shareholders, by offering savers higher interest rates and borrowers lower ones than their demutualised competitors.

[6] Note the table does not include data about the few ethical funds which have been closed or taken over.

[7] Source of data: EIRIS, November 1996.

Table 1.[7] Fund	Date of Launch	Value of funds November 1996
Friends Provident Stewardship Unit Trust	1984	£303.7m
Friends Provident Stewardship Pension Fund	1984	£310.3m
Credit Suisse Fellowship Trust	1986	£36.2m
Ethical Investment Fund	1986	£1.3m
Abbey Life Ethical Trust	1987	£33.7m
Framlington Health Fund	1987	£49.1m
Friends Provident Stewardship Income Trust	1987	£65.9m
Allchurches Amity Funds	1988	£26.0m
Jupiter Ecology Fund	1988	£30.9m
Acorn Ethical Unit Trust	1989	£4.2m
Eagle Star Environmental Opportunities Trust	1989	£16.4m
HFS Green Chip Fund	1989	£12.4m
Jupiter International Green Investment Trust	1989	£30.6m
Scottish Equitable Ethical Unit Trust	1989	£51.0m
Sovereign Ethical Fund	1989	£14.9m
TSB Environmental Investor Fund	1989	£15.1m
CIS Environ Trust	1990	£98.4m
Clerical Medical Evergreen Trust	1990	£18.8m
Barchester Best of Green Life Fund	1991	£7.8m
Barchester Best of Green Pension Fund	1991	£0.8m
NPI Global Care Unit Trust	1991	£31.1m
Abtrust Ethical Fund	1992	£3.4m
CU Environmental Trust	1992	£19.4m
Sun Life Global Portfolio Ecological Fund	1992	£3.6m
Co-operative Bank Ethical Unit Trust	1993	£12.6m
Friends Provident Ethical Investment Trust	1993	£32.2m
Equitable Ethical Trust	1994	£16.2m
Friendly Endeavour Broker Bond	1994	£1.2m
NPI Pension Global Care	1994	£3.5m
HTR Ethical Fund[8]	1995	£15.2m
Merchant Investors Assurance Ethical Fund	1995	£1.2m

[8] Also known as Henderson Ethical Fund.

Table 1.[7] Fund	Date of Launch	Value of funds November 1996
NPI Global Care Income Unit Trust	1995	£5.9m
NPI Pension Global Care Managed Fund	1996	£2.0m
United Charities Ethical Trust	1996[9]	£6.3m
Total		**£1,300m**

The financial institutions that provide ethical funds are quite diverse. Most ethical funds are, like Stewardship, provided by insurance companies; either mutual insurers, like Friends Provident, or ordinary insurance companies. One, CIS Environ, is provided by the Co-operative Insurance Society. A small number of funds are provided by banking groups. Some ethical funds are managed by brokers. Compared to the rest of the unit trust market, relatively few ethical funds are provided by dedicated fund management companies, and none has been launched by the major investment banks. Many of the institutions that provide ethical funds are themselves owned by other institutions. For example, the Jupiter Ecology Fund is managed by Jupiter International Group plc which is a subsidiary of Commerzbank AG, Germany's third largest bank. The Eagle Star Environmental Opportunities Trust is managed by Eagle Star, an insurance subsidiary of BAT plc (also known as British American Tobacco).[10]

Two ethical funds, Friends Provident Ethical Investment Trust, and Jupiter International Green Investment Trust are not unit trusts, but investment trusts. Investment trusts differ from unit trusts in that they are publicly quoted companies, the object of which is solely to invest in the shares of other companies. Investment trusts are allowed to borrow money in order to make the most of favourable investment situations. The value of investment trusts depends not on the value of their assets - the total value of the shares they invest in - but on their share prices, which are often at a premium or discount to their asset value. Investment trusts typically charge lower management fees than unit trusts.

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[9] While the United Charities fund was launched in 1982, it did not become an ethical fund until 1996.

[10] This might been seen as a contradiction because many ethical funds have criteria excluding tobacco companies from their investment. However, the Eagle Star Environmental Opportunities Trust does not

Unlike Stewardship, not all ethical unit trusts invest in companies directly. A handful - Ethical Investors Group, Genesis, Lincoln National, and Skandia - are 'funds of funds' investing their assets in other ethical funds.

In the previous section I noted that Stewardship has a very significant place in Friends Provident as a whole. This is not true of many of the other ethical funds provided by big insurance companies, where the ethical funds are rather small compared to the other funds managed. However, there are some institutions, such as NPI, appear to have invested more heavily in the development of the ethical research and procedures than other institutions.

Perhaps the biggest innovation in ethical funds since the launch of Stewardship, is the emergence of 'green' funds. The first of these funds was the Merlin Ecology Fund, launched in 1988, and now known as the Jupiter Ecology Fund. These funds responded to the emergence of the environment as a considerable issue of public concern in the late 1980s. The advent of green funds can perhaps be seen as bringing a new kind of interest group into ethical investment; one that moved beyond the religious origins of ethical investment to a broader constituency of environmental and third world 'pressure group' interests. There are now perhaps 10 explicitly environmental funds. However, the difference between environmental funds and ethical funds is now generally not that great. Many ethical funds, including Stewardship, responded to the growth of environmental concern by adding a range of environmental criteria to their ethical criteria, and most of the environmental funds also employ the same core ethical criteria (concerning tobacco, alcohol and arms, for example) as the ethical funds. One of the principal differences is the way in which the green funds are marketed. However, some of the environmental funds (such as the Eagles Star Environmental Opportunities Trust and the CU Environmental Trust) do seek to distance themselves from conventional ethical funds, and do not adopt conventional ethical criteria. Instead it seems that these funds have a purely commercial rationale for investing in environmental companies. As CU Environmental Trust put it: 'Investment is in those companies which are, or will become, major beneficiaries of environmental protection or expenditure' (EIRIS, 1996a:78).

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have such restrictions. Indeed it claims not to be an ethical trust at all, but aims to share in the success of environmentally progressive companies.

In recent years some ethical funds have disappeared. In 1993 the TSB Target Global Opportunities Fund, founded in 1987, was sold to Edinburgh Fund Managers, and lost its ethical status. Friends Provident acquired the NM Financial Management Group, and with it the NM Conscience Fund, also founded in 1987. The Conscience Fund was gradually phased out, with unitholders being given the opportunity of switching to Stewardship (Jepson, 1995:40) In 1994 the MI Environmental Fund was closed after three years of trading because it had been unable to attract sufficient funds (1995:40).

Another important development in the history of ethical investment was the foundation of the UK Social Investment Forum in 1990. According to Jepson (1995), the purpose of the forum was ‘promoting and encouraging the development and positive impact of socially responsible investment throughout the UK’ (1995:37). While not all the ethical funds are members of UK SIF, many are and it provides a valuable forum for discussion and dissemination of information and ideas about ethical investment.

3.5 Participants in the Stewardship process

On 21 March 1996, I attended a meeting of the Stewardship Committee of Reference. This is the heart of the Stewardship process. In all 17 people were present including the six members of the Committee of Reference; the Stewardship fund managers Richard Lowman and Richard Singleton, and one other fund manager; three members of the marketing team including John Bounds, Assistant General Manager Marketing, and Frank Blighe, the Stewardship market development manager; Roger Whiffin, secretary to the Committee, and Deputy Company Secretary to Friends’ Provident Life Office, and Diana Monger, assistant secretary to the Committee; Peter Webster, Executive Director of EIRIS and Karen Eldridge, the Head of Client Services at EIRIS; and myself. The members of the Committee, and representatives of the fund manager, EIRIS and the Secretariat always attend the meetings. The contingents from the marketing and fund management departments fluctuate from meeting to meeting. Outsiders such as myself are present only very occasionally. The Committee usually meets quarterly, each meeting usually beginning at 2 p.m. and proceeding until 5.30 p.m. or so. These meetings are where the ethical policy and direction of Stewardship is worked out. The following is an account of the various participants in the Stewardship process.

3.5.1 Committee of Reference

The Committee of Reference is responsible for establishing the Stewardship ethical policy and for ensuring that investments are made in accordance with the policy. The Committee currently has six members: John Whitney (Chairman), Charles Jacob MBE, Charles Medawar, Roger Morton, Lyn Wilson, and Marlene Winfield. Joanna Lumley OBE was also, until recently, a member of the Committee.

- John Whitney is also Chairman of Enterprise Radio Holdings Ltd., RAJAR Ltd. (Radio Joint Audience Research Ltd.), and the Sony Radio Awards Committee, Non-Executive Director and former Chairman of The Really Useful Group Ltd., and Non-Executive Director of VCI plc, Former Director General of the Independent Broadcasting Authority and former Managing Director of Capital Radio, Non-Executive Director of Friends' Provident Life Office and Chairman of Friends Provident Ethical Investment Trust plc.

- Charles Jacob MBE, who was responsible for the original proposal for the Stewardship Unit Trust, is currently Director of the UK Social Investment Forum, Councillor and Finance Board member of the Methodist Church, Charity Trustee and a Director of Friends Provident Ethical Investment Trust plc. His MBE was for services to Educational and Charitable Organisations in Wales.

- Charles Medawar is Founder Director of Public Interest Research Centre Ltd. and Social Audit Ltd and a council member of SustainAbility. He has previously worked for Ralph Nader (US) and with the Consumers' Association (UK).

- Roger Morton is an Independent Investment Adviser to pension funds and charities, a Trustee of the Joseph Rowntree Charitable Trust, and a Director of Friends Provident Ethical Investment Trust plc.

- Lyn Wilson was a business school lecturer at Cambridge and Durham. He worked in marketing for BOAC and Reckitt & Colman, and with the Committee for Corporate Social Responsibility at Stanford University Business School (US). He later worked in management consulting and education with Harbridge Consulting Group. Former vice chairman of Friends of the Earth. Non-Executive Director of Friends' Provident Life Office and member of the Quakers' Finance, Investment and International Relations Committees.

- Marlene Winfield is a consumer advocate and researcher, who has written influential works on self-regulation in companies, improving services to carers, and the criminal justice system. A founder of Public Concern at Work - a free legal advice centre for employees worried about serious malpractice at work. Member of the Board of the Ethical Investment Research Service (EIRIS).

The Committee has a semi-detached relationship with Friends' Provident Life Office. The members of the Committee are paid modestly for their services by Friends Provident; also two of its members, Lyn Wilson and its chair, John Whitney, are also members of the main board of Friends Provident. However, the Committee is considerably independent in other respects. Particularly important is the fact that in practical terms it nominates its own members.[11] However, this power has not been used often as five of the six committee members, Charles Jacob, Charles Medawar, Roger Morton, Lyn Wilson, and John Whitney were all on the original Committee appointed in 1984 when the Stewardship Unit Trust was established. There is at present no term-limit on the Committee members, nor retirement age, and no procedure for the removal of Committee members. The members of the Committee who have resigned so far, namely Trevor Jepson and Joseph Sewell, felt that they had served long enough, and Joanna Lumley left because she had too many other commitments to do justice to her work for Stewardship. There is no formal process by which the Committee members are accountable either to Friends Provident or to the unit holders and pension fund beneficiaries. However, the fact that two members of the Committee are on the Friends Provident board provides some accountability to Friends Provident. And, ultimately, Friends Provident could sack the Committee, but such an act would probably do considerable damage to the Stewardship reputation, the strength of which derives partly from its use of an autonomous committee of socially concerned experts. There is some informal accountability of the Committee to unit and policy holders. One member of the Committee, currently Charles Medawar, has the special responsibility of helping the Committee secretary deal with correspondence with unit holders and the public. In addition every letter written to Stewardship is circulated to all members of the Committee, and is noted and, if necessary, discussed at the next Committee meeting.

Apart from responding to letters from investors, and the occasional individual public speech, the members of the Committee have, until recently, had no direct means of communicating with the public. The principal documents used to speak about Stewardship are prepared by the Friends Provident marketing department. From time to time this has imposed some limitations on the Committee. The problem is that the ethical issues with which they deal are rather complex, but published material, perhaps of necessity, tends to simplify them. There has been a desire among members of the Committee to establish a more direct means of communication about their views. Recently the Committee appointed an experienced, retired executive to draft fuller statements of the Committee's view on issues where there had been controversy. The first such paper was issued in October 1996 on the subject of animal testing. This was converted into a printed document by the Friends Provident marketing department and made available to investors and advisers. The advent of the Stewardship newsletter also contributes to this purpose. Charles Jacob wrote a short article for the first issue (in mid -1996) and John Whitney, Marlene Winfield and Lyn Wilson have written for the second (late 1996). Frank Blighe, of the marketing department, has requested that the Committee members continue to supply material for subsequent issues.

The primary function of the Committee is to establish and develop the Stewardship ethical policy. As we shall see below, this mainly involves establishing a series of negative and positive screening criteria. The Committee is also responsible for applying these criteria to companies which EIRIS uses to produce an 'acceptable list' of qualifying companies. However, this process is quite complicated, so there is an investment Sub-Committee of the Committee of Reference responsible for this task.

3.5.2 Investment Sub-Committee

If the criteria agreed by the Committee of Reference could be applied mechanically, without the need for further ethical judgement, then all the Committee of Reference would have to do is to specify the criteria, and instruct EIRIS to apply them to FT-SE A All Share Companies, and let the fund managers choose a portfolio from the resultant

[11] Strictly speaking the Committee nominates new members and they are formally appointed by Friends' Provident Unit Trust Managers Ltd. It is also worth noting that when Stewardship was founded, the Joseph Rowntree Charitable Trust was responsible for nominating four of the initial Committee members.

list of acceptable companies. The Committee of Reference would then simply have to keep a watchful eye on the process. However, the majority of the ethical criteria used by Stewardship cannot be applied mechanically. As the marketing literature says, the Committee is prepared to allow that 'less extreme malfeasance may sometimes be counterbalanced by exceptional performance on the positive side of the equation.' (Stewardship, 1996:6b). In other words, the Stewardship ethical policy recognises that the good a company does may sometimes outweigh the bad.[12] This means that the policy cannot be mechanically applied. Someone has to make the judgement about what counts as less extreme malfeasance, and under what circumstances the performance on the positive side of the equation is sufficiently high. This means that in addition to specifying the criteria, the Committee has to make judgements in the large number of borderline cases which arise. In order to exercise these complicated judgements, which are often time consuming, the Committee of Reference has an Investment Sub-Committee which is chaired by Lyn Wilson and includes Charles Medawar, Charles Jacob and Roger Morton. The Secretariat, the fund managers and representatives of EIRIS also attend in an advisory capacity. The decisions of this committee are made by the members of the Committee of Reference who attend it, but are ratified by the full Committee of Reference at its next meeting. While the views of those attending the Investment Sub-Committee are sought, it is only the opinions of the four Committee of Reference members which are decisive in making final decisions about which companies are acceptable for inclusion in the Stewardship portfolio.

3.5.3 Research (EIRIS)

Stewardship's ethical research is provided by EIRIS. EIRIS is a registered charity whose purpose is to help people invest according to their principles. Specifically

> 'to provide information that helps investors apply ethical criteria to investment; to help people to identify and choose between different types of investment on ethical, as distinct from financial grounds; to promote a wider understanding of, and debate on, corporate responsibility.' (EIRIS, 1996a:3)

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[12] This flexibility does not apply to those ethical issues where Stewardship has a policy of absolute exclusion.

EIRIS now has about 1,000 individual and institutional members. The EIRIS charity owns EIRIS Services Ltd which provides commercial services to individuals and institutions. 90% of EIRIS's revenue arises from the research services it provides to the ethical unit trusts (Jepson, 1995:55). The core of EIRIS's services is based on its database of 1,100 companies. These companies are drawn mainly from those listed on the FT-SE A All-Share Index (excluding investment trusts). EIRIS maintains information on each company about its performance on a range of more than 300 positive and negative criteria. On the basis of this it is able to provide lists of companies which pass numerous combinations of criteria. For example, the database could provide a list of companies which have not had contracts with the Ministry of Defence worth more than £5m in any one of the last three years, while also deriving not more than £10m of their annual turnover from the production or sale of tobacco or tobacco products. The database can be used to generate a list of companies which are acceptable according to particular ethical criteria. It can also be used to screen a client's existing portfolio of investments to weed out those companies which contravene selected ethical criteria. The database also enables EIRIS to provide detailed fact sheets on the status of an individual company with respect to a range of criteria. By applying the database in these ways EIRIS provides the services which are its principal sources of revenue. EIRIS now provides a high quality research service to 21 out of the 30 ethical funds.

The way this works in practice is that in the first instance each fund must complete either the 'Basic Questionnaire' or the 'Specialised Questionnaire' which EIRIS produces. Both questionnaires list a range of criteria areas (e.g. alcohol, armaments). These areas contain a list of specific criteria (e.g. 'company groups that derive any turnover from the production and sale of alcoholic drinks'). The basic questionnaire covers fewer areas, and offers fewer criteria to choose from than the specialised one. The fund manager uses these questionnaires to choose which ethical criteria to employ as a basis for excluding companies. Once these criteria are selected, EIRIS uses them to screen its database of companies. The companies that fail to pass all of the chosen criteria are excluded, leaving an 'acceptable list' of companies. From this acceptable list, of companies the investment manager of the ethical fund selects a portfolio of investments on ordinary financial grounds. Once the fund has invested in companies, EIRIS is able to offer a subsequent 'portfolio screening' service, which periodically compares the companies in a fund's portfolio against the ethical criteria it has selected, informing the fund manager if any of its companies have changed their ethical status (e.g. because they acquired an ethically dubious subsidiary).

EIRIS's service does not include telling funds which ethical criteria to choose, or how to invest the fund wisely on financial grounds. EIRIS says that it:

> 'does not make moral judgements about the activities it researches; its expertise is in researching the issues. Nor does it give advice on the financial suitability of any investment or manage investments itself.' (EIRIS, 1996a:7)

This means that it is up to the individual investor, or investment fund manager to determine what criteria are the most ethically appropriate ones to adopt. You decide which criteria are appropriate to your ethics, and EIRIS will find the companies consistent with your chosen criteria. Of course, the particular range of ethical criteria EIRIS offers has a strong influence on the practical shape of ethical investment. If EIRIS does not offer criteria on a particular ethical area, it is exceptionally difficult to adopt an ethical policy on it. This is because it would be difficult for a fund to screen its investments without EIRIS's help.[13] This fact influences the way ethical issues are dealt with by funds, and constrains the range of ethical policies they adopt.

As has already been said, Stewardship was EIRIS's first and remains its largest client. None of the other funds has the closeness of relationship that EIRIS has with Stewardship. Trevor Jepson, the first Chair of EIRIS was also on the Stewardship's Committee of Reference. Marlene Winfield of the Committee of Reference, is also a member of the management council of EIRIS. EIRIS always sends a representative to the Committee of Reference meetings, and undertakes special research on particular issues when mandated by the Committee to do so. In fact, it may be fair to say that many of the criteria used by EIRIS were developed first in collaboration with Stewardship. The close working relationship with EIRIS is one reason why Stewardship has not opted to hire its own in-house ethical or environmental researchers, unlike Jupiter Ecology and NPI Global Care. Another reason which Frank Blighe gives for this is that 'to some extent by doing our own research there's always the danger of being put in a slightly compromising position, there are conflicts of interest involved, so we would rather rely

[13] Of course, as I will argue later in this thesis, ethical policies do not have to involve *screening*. If, instead, the ethical policy simply requires constructive dialogue with companies on that issue, then it might be possible to extend the ethical policy beyond the frame provided by EIRIS.

on the totally independent research.’ An example of the possible conflict of interest is that if you are doing your own research and your investment manager finds a company which he thinks will perform well financially, there will be pressure to compromise the objectivity of research in order to pass the company as ethical.

3.5.4 Secretariat

The Committee is served by a secretary, Roger Whiffin, who is also Deputy Company Secretary for Friends’ Provident Life Office, and he is assisted by Diana Monger, also of the company secretary’s office. The Friends Provident Secretariat produces the minutes of the Committee of Reference meetings, and circulates the agendas and other relevant materials such as the portfolio screen, company reports, and issue-based reports produced by EIRIS. The Secretariat also co-ordinates all correspondence between investors and the Committee.

3.5.5 Fund management

Stewardship’s funds are managed by a team of four fund managers from FP Asset Managers Limited, headed by Richard Lowman, Director, UK Equities. He has been managing the Stewardship funds since their launch in 1984. He sees his responsibility in exclusively financial terms. His role is to invest the funds available in the companies that the Committee of Reference consider acceptable. While Richard Lowman is the senior investment manager of the Stewardship funds, Richard Singleton, who has special responsibility for managing the Stewardship Income Trust, is the manager most involved with the ethical aspects of Stewardship. He attends all meetings of the Committee of Reference and Investment Sub-Committee. Richard Singleton is responsible for writing to, talking to, and meeting with companies about ethical matters on Stewardship’s behalf.[14] He is also the main source of detailed information for the press about Stewardship’s investment policy - including its ethical elements.

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[14] However, EIRIS also does a considerable amount of letter writing to companies in order to give the Committee of Reference the information they need.

3.5.6 Marketing department

The Stewardship brand is managed by Frank Blighe, with the assistance of Phil White. Frank Blighe's time is primarily devoted to Stewardship, but he also has responsibility for Friends Provident's many other unit trusts and PEPs. Phil White, however, works exclusively on marketing Stewardship. The marketing team is responsible for presenting Stewardship to the public and in particular for producing the Stewardship marketing literature. The marketing department publishes a number of documents concerning the Stewardship funds. However, from an ethical point of view there are two documents of principal interest: *The Stewardship Unit Trusts*, and *The Stewardship Investment Criteria*. The first of these documents briefly introduces the concept and history of Stewardship, and describes the three funds. The second goes into more detail about the ethical criteria Stewardship uses, and provides biographical background about the members of the Committee of Reference.[15]

As an experiment, in June 1996, the marketing department also published a newsletter for Stewardship. The first issue gave some summaries of press stories on ethical investment, and internal news about the foundation of the Joanna Lumley Research Fellowship, and about Stewardship's financial performance. It also contained some biographical material about the Committee of Reference members, and how the Committee screens companies. The first newsletter also had a small amount of comment by Charles Jacob, and offered brief sketches of what was good about three of the companies in Stewardship's portfolio. The publication of the newsletter was well received by unit holders and further issues will be published, the second having been published at the end of 1996.

Given that these are the main sources of information available to the public concerning Stewardship's ethical policy, this makes the members of the marketing department important participants in the Stewardship process. Frank Blighe regularly attends meetings of the Committee of Reference and the Investment Sub-Committee. The marketing department has effective control over how Stewardship is presented. They have an important role in recommending, for example, what charges to make to investors and what commissions to pass on to independent financial advisers (IFAs), what new Stewardship products to launch, and they produce the words and images used

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[15] See below, p.95ff., for further discussion of these documents.

in the advertising. The marketing department is also the initial contact for the press. However, the marketing department normally seeks the Committee of Reference's comments on the wording and presentation of much of its output, although, in the past, this was perhaps not as much as the Committee would have liked. Since Frank Blighe assumed the role of Stewardship Market Development Manager in 1994 this has largely been resolved.

3.5.7 Sales force/IFAs

The financial products sold by Friends Provident are sold in five ways - through independent financial advisers, including a small number of specialist ethical or green IFAs; through Friends Provident First Call, the Office's direct selling company; through Friends Provident tied agents; through direct mailshots; and by telesales, through a new sales medium called The Blue Line. Around half of Stewardship business comes through IFAs. Some 2,000 IFAs have sold Stewardship business in its 12 years, which is between 10% and 20% of all IFAs in the UK. Many of the other ethical funds are not sold by such a wide range of IFAs. Their sales are, instead, concentrated in the two dozen or so specialist ethical IFAs. One reason Frank Blighe gives for Stewardship's wider uptake among general IFAs is the considerable financial success of Stewardship in its early years, which put it in the top decile of ordinary unit trusts. A second reason is that Friends Provident offers an ethical pension plan, which most of the other ethical funds do not. A large proportion of IFAs use Friends Provident for other business, so it may be an obvious choice when they come across an ethical investment need. Specialist investment providers are used by a much narrower range of advisers.

Most IFAs make their money from commissions paid when they sell a policy. There is considerable competition between financial services companies to make their products attractive to IFAs. Paying a good commission is one way to do this. Friends Provident Stewardship increased its commission on the Stewardship unit trusts from 1 August 1996 from 3% to 4% of the initial capital amount invested. On the same date, Stewardship increased its initial charges for the first time since launch from about 5% to 5.75%, against the industry trend of reducing initial charges. This was to ensure that the Trust expenses were covered and to respond to competition from other ethical funds which offered IFAs different commissions to that offered by Stewardship.

3.5.8 Investors

The marketing department of Friends Provident estimates that there are as many as 100,000 people investing in the various Stewardship funds. There are around 25,000 investors in the unit trusts alone. This means that Stewardship possibly accounts for two thirds of all the retail ethical investors in the UK. A 1995 EIRIS survey of Stewardship unit holders reveals that unit holders are not committed to the same degree to all Stewardship issues, only some are considered to be an area of major concern by the majority.[16] Table 2. summarises answers to the question. 'For each of the following areas [issues], please indicate your level of concern in making investment decisions: major, minor, no concern.'

Table 2. Issues	**Major Concern (%)**	**Minor Concern (%)**	**No Concern (%)**	**No Answer (%)**
Military suppliers	78	12	4	6
Environmental impact	75	20	0	5
Operations in oppressive regimes	71	21	1	7
Employment conditions	56	31	4	8
Nuclear power	55	26	12	8
Operations in Third World	52	32	4	12
Animal welfare	39	42	10	9
Alcohol, tobacco, gambling	39	34	18	9
Operations in South Africa	17	33	35	15
Corporate Governance	14	41	17	27
Consumer issues	9	53	19	18

Compared to previous surveys, the highest growth in concern is environmental impact, and there has been a dramatic drop in concern over South Africa. Table 3 shows the things which unit holders considered to be most important features of Stewardship.

Table 3. Issue	**Very Important (%)**	**Quite Important (%)**	**Not Important (%)**	**No answer (%)**
Clear statement of what fund avoids and what it seeks to invest in.	87	9	1	4

[16] The survey was sent to 970 Stewardship unit holders, 252 of which replied.

Clear strategy to exert ethical influence on companies	68	23	2	7
Clear statement of process used to evaluate the companies	64	29	3	4
Strict avoidance of companies of greatest concern	60	31	1	8
Committee of people you trust to make individual decisions & oversee fund	57	32	3	8
Large part of the portfolio invested in companies with positive features	55	35	2	8
Good track record of financial performance	46	45	3	6
Regular reporting of decisions taken and reasons for them	11	51	11	10
Meetings of unit holders to discuss the fund.	17	42	35	12

Investors have no formal mechanisms for influencing the future of Stewardship. There is no meeting of unit holders and until recently no newsletter, and no formal mechanisms for unit holders to make the Committee of Reference accountable to their wishes. Nor, arguably, should there be, if one takes the view that investors are buying a financial product, not joining an association. Investors however do correspond with Stewardship, and their correspondence is handled by Charles Medawar of the Committee of Reference and Roger Whiffin, the secretary. This correspondence is taken seriously by the Committee, and overall has a very significant impact on the Committee's work. For example, recently the Committee received representation from an investor about the benefits of eco-tourism. This led to considerable correspondence with a major tour operator; reconsideration of the investment position; and now the development of new criteria.

3.6 Participants in other ethical funds

In the previous section I listed: the Committee of Reference, the Investment Sub-Committee, Research (EIRIS), Secretariat, Fund Management, Marketing Department, Sales/Force IFAs, and Investors as participants in the Stewardship process. How does this range of participants vary across the ethical investment sector? The principal variations are seen in just two areas: the committees of reference or as they are more commonly known, 'advisory committees' and the research used by the funds. As Table 4. shows, only 17 ethical funds have advisory committees. Those funds that do make use of advisory committees do not do so in quite the same way, or to the same degree as Stewardship. Lord Clinton-Davies, Chair of the advisory committee to the CIS Environ fund suggests three roles for his committee,

> ‘to supervise the fund managers and make sure that they carry out the ethical and environmental claims made for the fund; to act as an ombudsman reflecting the concerns of individuals shareholders, and to be an ultimate adviser when the fund manages are genuinely unsure, which in real life is not infrequent.’ (Sparkes, 1995:45)

These roles are included in the work of the Stewardship Committee of Reference. However the Stewardship Committee’s work goes beyond this. For example, according to EIRIS (1996a:70) no other advisory committee is required to approve all potential investment *in advance* in the way the Stewardship Committee does by producing its ‘acceptable list’.

Table 4.[17] **Fund**	**Uses EIRIS**	**In house full-time research**	**Has advisory committee**
Abbey Life Ethical Trust	Yes	No	**Yes**
Abtrust Ethical Fund	**Yes**	No	No
Acorn Ethical Unit Trust	No	No	No
Allchurches Amity Funds	No	No	**Yes**
Barchester Best of Green Life Fund	**Yes**	No	No
Barchester Best of Green Pension Fund	**Yes**	No	No
CIS Environ Trust	No	No	**Yes**
Clerical Medical Evergreen Trust	**Yes**	No	No
Co-operative Bank Ethical Unit Trust	No data	No data	No data
Credit Suisse Fellowship Trust	**Yes**	No	**Yes**
CU Environmental Trust	No	No	No
Eagle Star Environmental Opportunities Trust	No	No	No
Equitable Ethical Trust	No	No	No
Ethical Investment Fund	**Yes**	No	**Yes**
Framlington Health Fund	No	No	No
Friendly Endeavour Broker Bond	No data	No data	No data

[17] Adapted from EIRIS data (EIRIS, 1996a:70).

Table 4.[17] **Fund**	**Uses EIRIS**	**In house full-time research**	**Has advisory committee**
Friends Provident Ethical Investment Trust	**Yes**	No	**Yes**
Friends Provident Stewardship Income Trust	**Yes**	No	**Yes**
Friends Provident Stewardship Pension Fund	**Yes**	No	**Yes**
Friends Provident Stewardship Unit Trust	**Yes**	No	**Yes**
HFS Green Chip Fund	**Yes**	No	No
HTR Ethical Fund[18]	**Yes**	No	No
Jupiter Ecology Fund	No	**Yes**	**Yes**
Jupiter International Green Investment Trust	No	**Yes**	**Yes**
Merchant Investors Assurance Ethical Fund	No data	No data	No data
NPI Global Care Income Unit Trust	**Yes**	**Yes**	**Yes**
NPI Global Care Unit Trust	**Yes**	**Yes**	**Yes**
NPI Pension Global Care	**Yes**	**Yes**	**Yes**
NPI Pension Global Care Managed Fund	**Yes**	**Yes**	**Yes**
Scottish Equitable Ethical Unit Trust	**Yes**	No	No
Sovereign Ethical Fund	**Yes**	No	**Yes**
Sun Life Global Portfolio Ecological Fund	No	No	No
TSB Environmental Investor Fund	**Yes**	No	**Yes**
United Charities Ethical Trust	No data	No data	No data

However, all advisory committees have the power of veto over investment in particular companies. In few cases do advisory committees meet as frequently as the Stewardship Committee of Reference. Also because most funds apply criteria ‘mechanically’, the role of the committees in interpreting the ethical policy, and in weighing up the merits and demerits of companies tends to be much less than that of Stewardship. However, these committees can be valuable. In those funds that do not have advisory committees, ethical policies are adopted and administered by the fund managers. This means that ethical investors simply have to trust that their fund managers are doing what they say they are. It is likely that such trust will be frequently tested, when the financial objectives of the fund come into conflict with its ethical policy. Advisory committees

[18] Also known as Henderson Ethical Fund.

can at least act as an independent check on funds. In one instance this independence has been dramatically demonstrated. In 1989, the advisory committee of one fund, the Ethical Investment Fund, resigned *en masse* because, according to Steve Burkeman, one committee member, ‘we felt we were not able to do the job unitholders were being told we were doing.’ (quoted in Sparkes, 1995:47)

In all, 19 funds make use of the EIRIS research service and use the EIRIS questionnaire process, and portfolio screens. As a result there is considerable overlap between the ethical criteria offered by these funds, as their criteria will generally be limited to those provided by EIRIS. One consequence of this is that as far as the rigorous and comprehensive application of criteria is concerned, all these funds can claim to have the same quality of research. EIRIS’s fee structure for funds is proportional to the size of their assets. This means that a fund with only a few million pounds of assets can afford to purchase the same basic screening research as Friends Provident Stewardship, which is 100 times larger. Of course the application of criteria is not the only issue. As we shall see in the next chapter, there are many other ways to extend the sophistication of an ethical fund. One important modification that should be mentioned here is that two ethical funds managers, Jupiter and NPI, have opted to employ a full-time in-house research team. As it happens the three full-time researchers in the NPI team, headed by Tessa Tennant, were also responsible for the establishment of the Jupiter Ecology Fund, and moved to NPI in 1994, being replaced at Jupiter with a new team headed by Emma Howard Boyd. While in certain respects an in-house research team may not be able to achieve the sheer quantity of universal and objective research about companies that EIRIS can, these in-house teams claim to be able to provide their funds with a more qualitatively informed picture of companies. NPI uses EIRIS as well as its own research. These research teams regularly meet with companies and raise ethical issues with their managements. They have also completed detailed sector surveys, such as *How Green are your Grocers? A Survey of Social Issues in the Food Retail Sector* (NPI, 1996b). The NPI research team has also committed itself to contributing to the development of policy debate in corporate ethics.

What of the funds that do not use EIRIS and do not have a research team? These funds make use of a range of other sources of information. For example CIS Environ has its research provided by Manchester Business School Business Information Service. However, for some funds which do not use EIRIS it is unclear how their research is sourced. It is possible that the bulk of research is mainly undertaken by fund managers themselves, who may or may not be able to do so effectively.

3.7 Conclusion

In this chapter, I have offered an account of the emergence of the Stewardship idea, the development of the individual Stewardship funds, and their place within Friends Provident. I have also introduced the main participants in the Stewardship process. I have offered some brief comparisons between Stewardship and the rest of the ethical funds business.

Finally, before we move on to a consideration of how these participants work together to produce and maintain the Stewardship ethical funds, I said in Chapter 1 that I would support my claim that ethical investment can be regarded as a community. An important part of my methodological approach is that I am interpreting the 'shared understandings' (Walzer, 1983) of a particular community, and contributing to argument within a 'tradition of practice' (MacIntrye, 1984). There are a large number of people involved in the provision of ethical investment: fund managers, marketing managers, independent financial advisors, advisor committee members, researchers and commentators. These people are for the most part attached to particular firms. As such they form part of the community of their individual companies, and meet each other and work together regularly in the course of business. But there is also contact between individuals of different ethical investment companies. Frequently this is for narrow business purposes. However, through the UK Social Investment Forum, and other institutions, these individuals meet regularly and discuss the nature and future of the ethical investment business. Frequently they work together as a 'community' in the pursuit of collective goals. Currently, for example, a collective attempt is being made to persuade the Personal Investment Authority to require independent financial advisors to ask their clients whether they have ethical concerns, and would like to consider ethical investments. If they are successful, this will dramatically increase the visibility of ethical investment.

While ethical investment may be a community only in a rather thin sense, it is more clear that ethical investment constitutes a 'tradition of practice' (MacIntyre, 1994:206). The basic practice of ethical investment is considerably similar across many of the ethical funds. All ethical funds use some form of screening to exclude companies engaged in certain kinds of activities, and all claim to select companies on some positive basis. Most of the funds share similar criteria, and those that use EIRIS share identical criteria. In addition most of those that use EIRIS also have very similar methods for screening. While there are important differences between the funds, as we shall see in the next chapter, ethical funds can very easily be seen as participating in the same ‘tradition of practice.’

4. The Process of Ethical Investment

4.1 Introduction

This chapter contains an account of how the various parts of the Stewardship team - the Committee of Reference, the investment managers, and the marketing department - work together to make an ordinary unit trust into an ethical unit trust. In an important sense these procedures constitute the tradition of practice of ethical investment, they also exemplify what is ethical about ethical funds. An grasp of these procedures offers, better than any definition, an understanding of just what ethical investment is. It also forms the basis for the argumentative engagement with the tradition of practice of ethical investment which occupies the second half of this thesis. As in the previous chapter, I focus on Friends Provident Stewardship. As I said before, this is appropriate because Stewardship is the first and foremost family of funds in the UK. However, there are various respects in which other ethical funds differ in important ways from Stewardship. I will indicate these differences at the end of this chapter.

4.2 Stewardship's investment policy

All unit trusts have an investment policy which guides and limits the choices made by the fund manager as he or she manages the portfolio. This policy is related to the purpose of the fund. Some funds are devoted to maximising capital growth, others aim at producing a good annual income, some try for a mixture of the two. Alternatively the policy may relate to the geographical spread of the companies invested in. Some funds invest in UK equities, others in the stockmarkets of other countries, or regions - North America, Europe, emerging markets, etc. Some funds have a policy of investing widely across the stock market, other funds invest in particular industry sectors such as high technology stocks, or property companies, companies that do well in recessions, etc. The Stewardship funds are no different in this respect. The policy of the main Stewardship Unit Trust is to concentrate on UK companies, and to achieve long term capital growth with an increasing dividend income. The general policy of the Income Trust is also to concentrate on UK companies, but to provide an above average and increasing income with the prospect of some capital growth. The general policy of the North American Stewardship Trust is to produce long term capital growth, but it does so by investing in North American companies. The Stewardship funds do not have a policy to limit their investment to a particular industry sector, but instead they have an ethical policy which limits their portfolio on various ethical and environmental grounds. This is what makes them different from ordinary unit trusts. However, the limitations imposed by the ethical policy on the number of companies that can be invested in are not much different in effect from the limitations imposed by the more conventional kinds of specialist investment policies.

4.2.1 'Investment Selection Criteria'

Stewardship's ethical investment policy is formally specified in a document called 'The Investment Policy Criteria applied by The Committee of Reference in advising Friends' Provident Unit Trust Managers Ltd.' (IPC Document, 1996). The complete text of this document is not published and not made available to outsiders.[1] Excerpts of it are sometimes made available to unit holders in correspondence to illustrate a particular point. The document currently has two parts, a two page introductory section with 3 parts, and the main body of criteria divided into 29 sections, running to some 11 pages.

Section 1 of the introductory part is a summary of the trusts investment policy. This states:

> The aim of the "Stewardship" Trusts is to invest in carefully selected companies whose products, services and operations make a positive contribution to society generally. The Committee of Reference and the Managers of the Stewardship Trusts seek to identify companies which demonstrate a socially responsible attitude in all aspects of their business, notably including consumer and labour relations and care of the environment. The Trusts will, so far as practicable, avoid investments in companies involved in the supply or production of armaments; or which cause environmental damage or pollution; operate in countries under oppressive regimes; exploit animals; or which are involved in the production of alcohol, tobacco or pornography; or involved in gambling.' (IPC Document:i)

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[1] The document was made available to me, subject to the confidentiality agreement mentioned above.

This is an important statement because section three of the first part of the IPC Document states that 'The Committee is obliged to interpret and give effect to the advertised investment policy' (IPC Document:ii). Marlene Winfield of the Committee of Reference explains that the most important part of this statement is the first sentence which commits Stewardship to the aim of investing in carefully selected companies whose products, services and operations make a positive contribution to society. The rest of the statement tells how that over-riding objective will be met, offering examples which are of concern to the Committee. For the most part these examples have remained constant throughout the life of Stewardship. However, the Committee recognises that occasionally there are grounds for change. The clearest example of this is the case of South Africa. Stewardship used to have a policy of excluding companies with operations in South Africa. With the collapse of apartheid, the Committee decided to cease the exclusion of such companies. Changes might arise for other reasons, for example, sometimes new information becomes available, as it has in the case of water pollution; new problems emerge, for example, the growing concerns about biocides; and new positive initiatives, such as the emergence of environmental certification schemes.

Section 2 of the Introduction contains some brief notes about the role of the Committee (amounting to 2/3 of one page). This states that the Friends Provident managers are by law required to be responsible for the selection of investments 'Therefore, the Committee's role is to try to help the Managers to fulfil with sensitivity the advertised investment policy, so that investors and prospective investors can feel confident that it is interpreted and implemented in appropriate ways.' (IPC Document:1)

This section says that

> 'The Committee sees its role as a positive one, always considering investments from the stance of the advertised investment policy to analyse the long-term benefit which particular companies bring to the community. The difficulties of fulfilling this positive role should be fully recognised, for example:
>
> There are real problems involved in obtaining and analysing relevant information about the detailed activities and performance of a number of companies; and different investors have many different interests and concerns, so problems can often arise in assessing the relative importance of different investment criteria.' (IPC Document:1)

Section 3 lists the main headings into which Stewardship's policy is divided. The major content of the IPC Document is a large section entitled 'The Stewardship Unit Trust's Investment Selection Criteria.' This consists of half a page of explanatory notes followed by 11 pages of detailed information about the criteria used by the Committee to screen companies for investment.[2]

The full IPC Document criteria are rather more detailed than those listed in the published material. For example, concerning the issue of water pollution, the published material says:

> **'Environmental destruction.**
>
> This includes activities considered to degrade the environment, such as unacceptable levels of water pollution, destruction of natural woodlands or forests, and the manufacture or use of pesticides or ozone depleting chemicals.' (Stewardship, 1996)

Whereas the full IPC criterion is:

> **'Water Discharges**
>
> - The Trusts would definitely not invest in company groups which had breached their discharge consents for more than 35 times a year;
> - the Trusts would not normally invest in company groups which had breached their discharge consents for more than 10 times per year;
> - the Trusts would preferable not invest in company groups which had breached their discharge consents for more than 5 times per year;
> - the Trusts would not normally invest in company groups which had exceeded a discharge consent on the same parameter three or more times at any one sample point in the last year covered.' (IPC Document:10)

Of the individual criteria categories mentioned above, most are dealt with by a short paragraph of text, with some (including animal testing, military sales, oppressive regimes, tropical hardwood, pesticides, and third world marketing) getting from half a page to one page of commentary.

[2] Here I use the number of pages as an indicator of the amount of information contained in the document. This is of limited value as a measure of the *quality* of the information, however it does offer some indication of the level of detail at which criteria are specified.

4.2.2 Nature of Stewardship criteria

One important general feature of Stewardship criteria is that they apply not simply to individual companies, but to company groups. This in fact applies to all EIRIS criteria (and to other ethical unit trusts which use EIRIS). This seems to be based on the reasonable idea that a parent company must take responsibility for the practice of its subsidiary and associate companies, but it does occasionally mean that a company which is itself exemplary, may find itself excluded because it has a subsidiary or associate company which, on Stewardship criteria, has a poor ethical record. Another feature of Stewardship criteria is that a strong distinction is made between positive and negative criteria. Negative criteria are employed to rule out companies considered to be doing harm to the world or its people, while the positive criteria are used to include companies which make a significant positive contribution to society. When it comes to specifying these criteria, the IPC Document covers negative screening criteria in rather more detail than positive. This balance of detail is also reflected in EIRIS's criteria questionnaires.

It is also worth emphasising that the Stewardship criteria are standards used for screening companies, and generally not ethical positions in themselves. However, at least some of these criteria may be considered to imply ethical positions. For example, on the issue of pornography the published criterion says:

> Stewardship seeks to distinguish between, on the one hand, published materials of real aesthetic merit which reflect and celebrate the physical and sexual nature of men and women, and on the other hand, clearly offensive portrayals of physical and sexual relationships in which personal caring and human dignity are either absent or insignificant. (Stewardship, 1996)

This investment policy begins to imply an ethical position. Rather than simply saying that Stewardship will not invest in companies involved in pornography, it seeks to define what is at issue ethically in the production of images with sexual content.[3] This being said, the purpose of the IPC Document is not to set out moral positions, but to state clear criteria in the form: 'Stewardship will not normally invest in companies which do X'. While the Committee does not tend to publish or write down moral positions, they are frequently articulated by Committee members in their meetings.

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[3] At the time of writing the Committee is seeking to improve their criteria on pornography so that it encompasses images with violent content.

Indeed many members of the Committee have very strong moral principles, in some cases deriving from their religious convictions. For example, Stewardship's unequivocal avoidance of companies involved in armaments is, at least for some members of the Committee, supported by the Quaker Peace Testimony.

On many ethical issues the criteria commit Stewardship to excluding companies which fail to meet the criteria without exception. Stewardship would never, for example, invest in a company group which was involved directly in the manufacture of weapons systems. However on many issues Stewardship is prepared to make exceptions. Stewardship's founding principle is that it should strive to invest in companies which *on balance* make a positive contribution to society. 'On balance' means that frequently Stewardship will invest in a company group which does some minor harm, because it does considerable good which the Committee regards as outweighing that harm. Part of the reason for this approach is the judgement that there is no such thing as a *perfectly ethical* company. Investment in every company must therefore be based on the acceptance of some imperfections. There are various ways in which the criteria reflect Stewardship's recognition of the need to weigh up the positive against the negative. The main way is that a wide range of criteria are not presented as absolute, but are qualified. Typically the IPC Document says that Stewardship would 'not normally' invest in companies involved in certain activities considered unethical; or it would 'preferably not' invest in certain kinds of companies; or it would only invest in companies engaged in certain kinds of activity 'only in special circumstances' or 'only in the most exceptional circumstances.'[4] Perhaps the majority of the Stewardship criteria are qualified in this way. The terms 'not normally', and 'preferably not' have a specialised meaning as far as the Stewardship criteria are concerned. 'Not normally' was the original qualifying term used in the 1980s, 'preferably not' was introduced later. 'Not normally' refers to certain kinds of issue which, while of concern, can be over-ridden either by specific caveats outlined in the criteria itself, or by countervailing positive achievements. In such situations the IPC Document stipulates that the Investment Sub-Committee's reasoning for a 'not normally' being over-ridden should be minuted. One

[4] There is one case (the issue of corporate political donations) in which a further kind of qualification is employed, which is where the Committee does not have a criteria as such, but will take the issue into consideration when deciding whether to invest in the company. The issue of companies making political donations is the only case of this.

example of ‘not normally’ is that Stewardship would not normally invest in companies whose ‘advertising is clearly deceitful, offensive or offends public good taste.’ ‘Preferably not’ differs from ‘not normally’ in that it specifies some generic conditions when ‘preferably not’ criteria can be over-ridden. These are when the company concerned has either: positive features in other areas; is ‘best of the bunch’; or is ‘moving in the right direction’ (IPC Document:3). It also includes issues which are treated as ‘monitor situations’. A monitor situation warns of a relatively mild ethical problem with a company which requires special attention from EIRIS to examine the issue in its research reports and portfolio screens.

Another way exceptions are made is based on quantity. On some issues companies are excluded from Stewardship’s portfolio whatever the scale of their involvement (e.g. companies which manufacture weapons systems). On other issues companies are excluded only if the amount of business attributable to that activity is greater than a certain proportion. There are a variety of different ways in which this threshold proportion is measured - sometimes it is 10% of the company’s turnover (e.g. alcohol and tobacco sales), sometimes it is if the offensive activity is the company’s ‘main business’ (e.g. livestock breeding), and sometimes it is an absolute figure - a turnover of greater than £1m (e.g. gambling).

These quantitative qualifications can be applied mechanically. Such quantitative exceptions are common amongst ethical unit trusts. Indeed many of the standard criteria which EIRIS uses have quantitative qualifications. The rationale for such exceptions is that company groups may be engaged in some activities regarded as unethical but these activities make up only a very small portion of their total activities, and may be counterbalanced by the larger positive contribution of such companies. Whatever the ethical questions about such a compromise, it has considerable practical value in that it widens the universe of companies available for investment. Such quantitative exceptions are easy to integrate into the EIRIS database procedures, and so can be applied without the attention of the Committee of Reference. The same is not true of the more qualitative qualifications, such as criteria which ‘normally’ apply. These criteria are not easy to apply mechanically, but instead depend on more subjective judgements about what counts as, for example, an exceptional circumstance; about how strong positive attributes have to be in order to over-ride ‘preferably not’ and ‘not normally’; what counts as the ‘best of the bunch’, and what improvement counts as ‘moving (fast enough) in the right direction'. These decisions are the time consuming work of the Committee of Reference and Investment Sub-Committee. The application of the IPC Document requires considerable interpretation and judgement from the Committee. As the marketing literature says, the Committee of Reference

> 'wrestles long and hard over the criteria and the identification of appropriate companies in which to invest. This is a challenging task, often requiring careful judgement about the correct balance between the positive and negative criteria relevant to any particular company.' (Stewardship, 1996a:4)

One consequence of this interpretative process is that the ethical policy of Stewardship is significantly more than the contents of the IPC Document. On many matters of judgement the Committee has, over time, produced precedents, and settled on various agreements about what these various qualifications mean. Much of Stewardship's policy then is not 'statute law' contained in the IPC Document, but 'case law' held in the minutes of the meetings of the Committee of Reference and Investment Sub-Committee, and in the memories of the members of the Committee.

4.2.3 Communication of the ethical policy

The ethical investment policy is communicated by the marketing department principally through their six page *The Stewardship Investment Criteria*. This includes a general statement of the ethical policy which states that Stewardship 'seeks to invest in companies which make a positive contribution to society, and avoid those which harm the world, its people or its wildlife' (Stewardship, 1996b:2). This is specified in more detail by lists of various criteria categories. The positive criteria are listed as:

- 'supplying the basic necessities of life
- providing high quality products and services which are of long term benefit to the community
- conservation of energy or natural resources
- environmental improvements and pollution control
- good relations with customers and suppliers
- high employee welfare standards
- training and education
- strong community involvement
- a good equal opportunities record
- openness about their activities.' (Stewardship, 1996a:4)

The negative criteria are:

- 'environmental destruction
- unnecessary exploitation of animals
- trade with oppressive regimes

- pornography
- weapons manufacture
- exploitation of third world countries
- tobacco or alcohol production
- nuclear power
- gambling
- offensive advertising.' (Stewardship, 1996a:4)

In addition the *Stewardship Investment Criteria* document provides roughly 50 words on each of the broad topics, for example, under the heading 'environmental destruction' it says:

> This includes activities considered to degrade the environment, such as unacceptable levels of water pollution, destruction of natural woodlands or forests, and the manufacture or use of pesticides or ozone depleting chemicals. (Stewardship, 1996b:4).

This information gives rather more detail about Stewardship's ethical policy than is published by most ethical funds. However, it is not intended that this document should give a full account of what Stewardship's policy is on each particular issue. In general, ethical funds encourage companies to increase their levels of disclosure of information to the public. Why does Stewardship not publish its ethical policy in full? Those involved in Stewardship offer several arguments against doing so. Firstly, it is suggested that to publish the investment selection criteria document would be misleading. As we have seen, the actual application of the ethical policy is based on interpretation by the Committee of Reference, and is not fully explained by the IPC Document alone. Secondly, the Stewardship investment policy is intellectual property resulting from many years of work, largely paid for by Friends Provident, and so it is argued that to make it available to Stewardship's competitor funds would be unreasonable. Thirdly, on many of the ethical issues there are people who will disagree strongly with the position the Stewardship Committee of Reference has taken. For example, there are many animal welfare activists who take a much more extreme position than Stewardship takes on animal issues. It is feared that publishing the full criteria would invite considerable debate from members of the public which the Committee of Reference is not well equipped to handle, and which may lead to misleading and inconsistent press coverage of Stewardship. Finally, criteria are evolving, and it is suggested that it would be confusing to unit holders to send out revisions.

While Stewardship currently does not publish its detailed ethical policy, it will make available more details about their policy on particular issues to individual investors on request. This is helpful. And the new Stewardship newsletter contains brief case studies indicating why Stewardship chooses to invest in particular companies. As these case studies accumulate, and if they offer detailed examples of the Committee's reasoning, this will serve to communicate the spirit of the ethical policy, without falling foul of all the objections above. The Committee of Reference also intends to produce and publish more detailed accounts of its position on particular issues. As I have already reported, the first such statement was on the subject of animal rights. This is a considerable step forward, as the statement conveys much information about the complexity of the issue, and the position that the Committee has taken. It is worth noting that while Stewardship does not publish its ethical policy in detail, EIRIS publishes its *Money and Ethics* guide (EIRIS, 1996a) which contains a small amount of information on the Stewardship ethical policy which is not mentioned in Stewardship's own published material. More significantly, the guide also provides figures for the percentage of Stewardship's portfolio which passes EIRIS's own criteria (many of which are published in the guide). With careful interpretation, the EIRIS guide therefore serves as a rough indicator to Stewardship's ethical policy.[5]

4.3 Production of the ethical policy

The Stewardship ethical policy is produced and controlled by the Committee of Reference. The current policy, described above, is the result of a gradual evolution from an initial document produced in 1983 which was shorter and listed fewer criteria. It has gradually grown. Many sections have been changed, some quite radically. The most notable changes concern the adoption of a number of environmental criteria in 1986 and 1987, and the change of circumstances in South Africa in the 1990s. In the latter case, Stewardship used to have a detailed policy of exclusion of companies with involvement in South Africa, but now is prepared to invest in such companies subject to its other

[5] EIRIS's guide (1996a) is only a rough indicator because it measures the fund's performance according to EIRIS's own criteria, and not those the funds use themselves. One limitation of this approach is that it does not reflect the case-by-case judgements made by the Committee of Reference. This means that Stewardship receives rather little credit in the guide for its sophisticated approach.

criteria. (Although it does pay special attention to levels of pay and disclosure by companies operating in South Africa.)

The work of developing the ethical policy is focused around meetings of the Committee of Reference. One part of each meeting is devoted to the consideration of particular issues. For example, at the March 1996 meeting the Committee considered changing the current Stewardship policy on pesticides and greenhouse gases and considered the possibility of considerably extending the range of positive environmental criteria, and adding some positive criteria on South Africa. In each case, discussion was based on a short report produced by EIRIS on the subject. Usually these reports arise from a suggestion by EIRIS to which the Committee responds. In the December 1995 meeting, the Committee prioritised a set of criteria topics which it wished to discuss. EIRIS was instructed to prepare reports on these topics - including those on greenhouse gases and positive South Africa criteria. Alternatively, EIRIS reports arise in response to a particular contingency - the pesticides report arose in response to a letter from a unit holder who asked the Committee to consider investing in a well known chemist (see below). The reports are a few A4 pages in length, and are circulated to the Committee in advance of the meeting for individual consideration. Each of the reports for the March meeting included:

- a note of the current Stewardship criteria, where appropriate,
- a brief survey of some of the key issues in question,
- a selection of indicators or benchmarks which the Committee may consider as possible new or alternative criteria,
- some definitions,
- and a short list of questions for the Committee to discuss and try to resolve at the meeting.

In addition, the report on South Africa also included some results from a survey of 970 Stewardship unit and policy holder's attitudes to various issues.[6] While these reports are

[6] Of the 252 replies received, only 17% said that South Africa was a major concern, thus giving it the rank of 9th out of 11 issues. However, there was strong endorsement among the respondents for supporting companies which are 'investing to rebuild South Africa,' 'training and promoting black employees or supporting black business,' and providing a high level of disclosure on its South African

brief, they provide a useful summary of many of the questions and concerns of unit holders. The EIRIS reports and the portfolio screens it provides, constitute a document that often runs in excess of 100 pages. Copies of this document are circulated to those attending the meeting, and given detailed consideration by the Committee members.

4.3.1 Committee of reference discussion of pesticides criteria

In the March 1996 meeting of the Committee, the first EIRIS report to be considered by the Committee concerned pesticides. This particular report was commissioned by the Investment Sub-Committee, as a result of a letter from a Stewardship unit holder. The letter asked the Committee to consider adding the well known chemist to the Stewardship portfolio. This request prompted a re-examination of the reasons why the chemist was currently not considered an acceptable Stewardship investment. In this case, one of the criteria which the company failed to pass concerned a fly killer which it retails and which contains Dichlorvos, a ‘Red List’ chemical.[7] The Committee had already corresponded on the insecticide in question with the Director of Investor Relations. He had told the Committee that the Red List applied to substances likely to be released into the water system, but fly killers were not very likely to do this and so arguably the Red List was not a very sensible standard to apply. The Committee, however, had in the past taken a broader stance to Red List chemicals, excluding companies which made products which contained them, whether they were likely to get into the water system or not. The Investment Sub-Committee therefore requested that EIRIS investigate this matter, and review the Stewardship criteria.

The EIRIS report lists two of the chemist’s products which contain Dichlorvos - the fly killer mentioned above, and a moth killer. It noted the company’s position together with some arguments against the use of Dichlorvos. Firstly that it is an acute hazard to birds and benign insects such as bees; that a number of poisonings have been reported from agricultural and public use; that there are alternatives to Dichlorvos in fly killers; that in the US Dichlorvos is to be banned after January 1 2001. EIRIS then quotes a series of

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business. 72% of respondents agreed that their ‘concern had changed from whether a company is investing in South Africa to what it does there’.

[7] The Red List is a list of substances that the Department of the Environment considers to be particularly dangerous to the aquatic environment. (EIRIS, 1996b:49).

press reports critical of Dichlorvos. It then offers a series of quotes from *This Poisoned Earth: the Truth About Pesticides* by Nigel Dudley which give an alarming picture of the risk posed by pesticides. Following this, the EIRIS report lists the current Stewardship criteria on pesticides; three alternative indicators from its own list of criteria on pesticides; and a short discussion which, among other things, notes some evidence that suggests that pesticides are one of the more significant concerns of EIRIS's private clients.[8] EIRIS's report on pesticides for the Committee is slightly unusual in that it focuses as much on the use of a particular chemical by a particular company, as on the general issues.

As it turned out, in the Committee's discussion there was little detailed consideration of Dichlorvos. The discussion of the pesticides criteria took place at a rather more general level. There were six existing criteria on pesticides which state that the Friends Provident Trusts would not normally invest in the companies which manufacture pesticides and pesticide ingredients; the formulation or marketing of pesticides known to cause problems, to exceed their limits in the water, to have been known to kill birds or mammals, to be commonly misused, or to cause harm to humans; and company groups which had been prosecuted by the Health and Safety Executive or National Rivers Authority. There was agreement that these pesticides criteria could be improved. For example, the first (of six) criteria which was used states that the Trusts would not normally invest in company groups that: 'manufactured pesticides (including any company group that manufactured the chemicals that made up, or went into the formulation of, a pesticide)' (IPC Document 1995). The problem with this is that it contains an ambiguity: many of the ingredients of pesticides are themselves not harmful at all or, at least, not particularly harmful. However, this criterion does not appear to distinguish between harmful ingredients and harmless ones. Another question that was discussed was whether the criteria were used to exclude environmentally friendly or organic pesticides. EIRIS was able to assure the Committee that this was not the case. An even more general question was the issue of whether there was ever a *positive* case for using pesticides. Charles Jacob pointed out that in many areas of the Third World the use of pesticides was of considerable positive benefit in limiting the damage done by

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[8] In addition to providing a screening service to the ethical unit trusts, EIRIS also offers a service to private individuals who wish to screen their own portfolios. According to EIRIS's report, pesticides criteria are among the most common concerns among this group of 167 private clients.

pests such as locusts, and restricting diseases such as malaria. This issue in particular illustrates the scale of some of the problems with which the Committee has to 'wrestle long and hard.' The Committee has to decide between excluding companies which manufacture pesticides because pesticides can be harmful to the environment, and supporting companies which manufacture pesticides because pesticides can be of great benefit to human health and agriculture. There was, at least at this Committee meeting, no time to resolve this dilemma. Discussion concluded with the invitation to EIRIS to offer some new criteria, which were accepted with some modifications at a subsequent Committee of Reference meeting. The new criteria are sharper than the old ones, but they still do not address the central dilemma surrounding the environmental costs, and the health benefits of pesticides.

Of course the case by case method that the Committee uses to address difficult dilemmas means that this problem will be addressed in future discussion of individual companies. As I said previously, the ethical policy of Stewardship is rather more than the IPC Document, but it is also based on the accumulated 'case law' of the decisions the Committee makes. This means that the ethical policy evolves not just at the main Committee of Reference, but also at the Investment Sub-Committee, as it considers individual companies ('cases'), and sets precedents about how the IPC Document should be interpreted.

In addition to the formal Committee meetings, policy is also sometimes made at occasional private meetings of the Committee. One such meeting took place in the week before the March 1996 Committee of Reference meeting. This meeting was the culmination of two years of intensive discussion on animal testing which failed to achieve consensus. The need for consensus came to a head when an ethical IFA who has clients with strong views on animal testing issues asked for clarification on Stewardship's animal testing policy. This private meeting led to the publication of the Committee's 'Statement on Animal Testing' (see below, p.175).

4.3.2 Source of authority for ethical investment policy

As we have seen, the Committee of Reference is practically responsible for the ethical policy. With the help of EIRIS, it develops and chooses the criteria which are to be used to place limits on investment. But whose ethical views does the policy seek to represent? There are several possibilities: the views of the Committee of Reference members, the views of the unit holders, the views of the general public, the views of Friends Provident? It appears that it may be a combination. The individual members of the Committee of Reference each have views on various ethical matters, and they agree upon criteria based on these views. On some issues the Committee is unanimous, while on others there is some disagreement about the ethical position the Committee should take. In the latter case the Committee is usually able to come up with a compromise around which a consensus can be built. The Committee does not tend to operate by majority, but by consensus. There is in fact only one occasion in the Committee's history where a vote has been sought on an ethical issue. This was on the question of whether Friends Provident should be asked to develop an alternative fund with a very tight restriction on animal rights issues. The Committee voted five votes to one against this proposal.

While formal decisions about Stewardship's ethical policy are taken only by the Committee, in practice there are a number of informal influences on these decisions. For example, the investment managers have an effect on the direction of Stewardship policy. Occasionally the investment managers will put the case for a more relaxed stance on ethical issues, particularly those which might lead to the acceptability of 'market leaders.' This would allow them to diversify and strengthen their portfolio at various stages in the economic cycle. Conversely, they also make arguments for resisting further ethical limitations on the range of acceptable companies. Here is an example of one such intervention. In the Investment Sub-Committee meeting in May 1996, a fund manager intervened on the issue of South African employment policies. He argued that there were a number of large blue chip UK companies which were excluded from the Stewardship portfolio because they failed on the South African employment criteria. He noted that because Stewardship had a strong weighting towards smaller companies, it would tend to underperform when the smaller companies sector underperfomed. He argued that this underperformance could be avoided if the fund managers were given permission to buy the shares of some of the larger companies. Of course this is a purely financial reason for changing the ethical policy, not an ethical one. However, he also offered an ethical argument to the effect that it was perhaps invidious to have a policy on the employment practices of multinationals in South Africa, while not adopting similar employment policies for multinationals operating in other developing countries. The response of the Committee was that South Africa was a special case and that 'reparations' needed to be made for the years of apartheid. However, the Committee did agree to look into the matter further. Later in the same meeting the fund manager commented that relaxing the criteria on pesticides would enable Stewardship to invest in some useful stocks in the health sector. In neither case was his intervention decisive. While the Committee of Reference listened carefully to his detailed observations, it did not agree. In these cases the fund manager acts as an advocate for the financial interests of the Stewardship fund, and the Committee has the discretion to reject these interests on account of their ethical commitments.

In addition to those attending the meetings who influence the compromises that result in the Stewardship ethical policy, there are, metaphorically speaking, a few ‘empty chairs’ around the Committee of Reference table. One ‘chair’ is filled by the opinions of general ethical investors. Some indication of these opinions is derived from questionnaire research by EIRIS of its own members. While such questionnaires impose limitations on the quality of information that can be gathered, they offer a useful source of information. When there appears to be particular concern on an issue, the Committee will often respond. A second and more significant ‘empty chair’ is occupied by the Stewardship unit holders. Charles Medawar thinks that an important practical test for deciding whether to change a criterion is whether such a change could be justified in good conscience to the unit holders. He says that one way he thinks about this is by asking ‘What would unit holders think if they had all these facts available to them?’ Any change the Committee makes to its ethical policy risks bringing the policy into conflict with the personal ethical views of current investors. One important need for such a test is that for many Stewardship investors termination of their Stewardship pension policy, say, would involve significant financial penalties. The general approach which Charles Medawar recommends for reducing this risk is a ‘ratchet’ approach. The criteria may get tighter, but not looser. This recommendation has not always been followed. For example, it is possible that the animal testing criteria could be regarded as having been slightly relaxed over time because of the realisation that the old policy had rather extreme implications. The problem with the ratchet approach is that people change their minds on ethical issues. Over time some issues cease to be significant concerns, and others emerge to replace them. Applied strictly, the ratchet approach might mean that one should never relax an ethical criterion, even when few people seem concerned about it. In fact, as Marlene Winfield comments, the ratchet metaphor is too simple. The Committee frequently seeks to improve criteria so that they better reflect their assessment of the issues and of the concerns of unit holders. The most obvious example of this is the case of South Africa discussed above.

Another problem the Committee has in trying to manage the ethical policy so as not to bring it into conflict with the beliefs of the unit holders, is that it is difficult to get representative and detailed information about the views of the latter. The Committee's main sources of information about the unit holders views are threefold: the letters written by unit holders, questionnaire surveys on the views of unit holders, and the views of IFAs who specialise in ethical investment. The first certainly offers a good indication of the views of the unit holders who write to the Committee. But there are reasons for thinking that the views of those who write to the Committee might not be representative of unit holders as a whole. The second does not suffer from this problem: Stewardship's recent questionnaire survey received over 5,000 responses, and data from it can more reasonably be claimed to be representative. However, as the Stewardship process demonstrates, ethical issues are complex and have many dimensions, it is exceptionally difficult to try to gain detailed information about complex views from self-completion questionnaires. The third source, ethical IFAs, certainly provides useful information, if for no other reason than IFAs regularly talk to unit holders. However IFAs have their own financial interests and ethical convictions which may colour their reports of the thinking of unit holders. The Committee, therefore, is constrained in its information for judging what the unit holders are thinking.

4.4 Applying the ethical policy

The purpose of the ethical policy is primarily to select those companies which are acceptable for investment. There are two aspects of this. Firstly, to exclude those companies which fail to meet ethical criteria and, secondly, to identify those companies which have special positive attributes. As I said in the section on criteria above, most of the Friends Provident ethical criteria have indefinite quantitative or qualitative elements. This means that they cannot be applied automatically - for example, EIRIS can not simply take the Friends Provident criteria and apply them mechanically to produce an acceptable list of companies. Additional interpretation by the Committee is necessary to produce the acceptable list. This is done at each meeting of the Investment Sub-Committee and occasionally at meetings of the main Committee of Reference.

One reason the Committee might examine a particular company is because it has been highlighted by the EIRIS 'portfolio screen.' This screen is produced by using the EIRIS database to apply the Stewardship criteria to the companies in its current portfolio. For each Committee of Reference meeting, EIRIS produces a portfolio screen which reveals if any company in the Stewardship portfolio has changed its ethical status. This might happen if a company starts up a new business operation in an unethical area, or more usually if a company acquires another. The portfolio screen is delivered by EIRIS in the form of a table, with the companies listed in rows and the ethical criteria categories in columns. If a company in the portfolio transgresses in a particular category, an asterisk appears in that column. Sometimes the asterisk appears in a category requiring absolute exclusion in which case there is no further discussion. But frequently the asterisk appears in one of the columns with a criterion in which the Committee allows exceptions to be made. Such cases do not lead to automatic exclusion but require the Committee to decide how serious the failing is, and whether the company's positive contribution is sufficiently good to outweigh the negative aspect.

Another slightly different reason for reconsidering a company is that several companies in the portfolio are described as 'monitor situations' on the portfolio screen. EIRIS pays special attention to these companies, and if in the particular areas to be monitored a change is noticed, this may lead to new discussion of the company. The other main reason for discussion of a particular company is that it is the Committee's procedure to review all companies in the Stewardship portfolios on a rolling basis. All companies are considered at least once every three years.

4.4.1 The selection of companies

While the main Committee of Reference does look at companies which have changed their status since the last Investment Sub-Committee meeting, most of the work of selecting companies is done by the Investment Sub-Committee. Discussion of each company by the Investment Sub-Committee is facilitated by detailed company reports produced by EIRIS. Each contains information about contact with the company, the Committee of Reference's rating of the company's acceptability, and the bulk of the report is a listing of those areas of the company's activities which fall short of the negative criteria or exceed its positive criteria. There are several different steps in the Investment Sub-Committee process. If a given company fails to meet one of the strict, objectively defined, ‘definitely not’ negative criteria it is invariably classed as unacceptable. If such a company is one of those which is currently in the portfolio and has changed its status, then instruction will be given by the Committee to the fund managers to dispose of it within six months. On occasion a case is made, usually by the fund manager, that there may be special circumstances. For example, the company may have recently acquired a company with a subsidiary which produces alcohol, but has committed itself to disposing of the subsidiary. Under these circumstances, the order to divest awaits clarification of that circumstance.

It is relatively easy for the Investment Sub-Committee to make a decision about companies which fail to meet strict ‘definitely not’ negative criteria. It is harder to do so with the qualified negative criteria (‘not normally’, ‘preferably not’, etc.). What are the circumstances under which these negative criteria are over-ridden? There are three examples shown in the IPC Document.

- if a company’s activities make a significant positive contribution
- if a company is the best of the bunch
- if a company is improving in the area of concern

Implicit in the criteria one can perhaps add:

- if a company’s unethical activities are an insignificant part of its business

There are good reasons for making use of each of these grounds. Stewardship has always had the aim of investing in companies which make a positive contribution to society, rather than the negative aim of seeking to avoid every company with the slightest flaw. Indeed such a negative policy may yield a very small portfolio indeed! Consequently, the Committee makes frequent use of these qualifications to its ‘not normally’ and ‘preferably not’ criteria. Perhaps a fifth of the companies in the Stewardship portfolio are considered acceptable by the Committee of Reference on the grounds listed above. This makes Stewardship’s approach more subtle than that used by many ethical funds. Rather than simply drawing up a list of negative criteria and excluding companies which fail to achieve them, it seeks on many issues to make an overall judgement of that company’s contribution. If an excellent company is let down by one or two modest failings, then it seems reasonable to support it with investment. This is certainly less puritanical than the practice of excluding any company, however good, once it is ethically ‘tainted’ to the slightest degree. The decision about when the good a company does outweighs the harm it does is largely a matter of the Committee’s judgement. The decision rests partly on what the criteria say, partly on precedents set by the Committee on previous similar cases, and partly on fresh judgement. While there are a set of positive criteria, there is no formal set of rules which say what counts as a sufficient positive contribution, or how to decide which is best of the bunch; whether a company is improving sufficiently, and quickly enough, or to define what counts as insignificant corporate involvement in an unethical area. The advantage of this case-by-case approach is that it allows the Committee to be flexible, but it does raise some questions about whether, with so many different variables, an informal and subjective procedure of this kind can be administered consistently and fairly over time.

4.4.2 Grading acceptable companies

Companies that pass the various negative criteria will be deemed acceptable by the Investment Sub-Committee. However, in addition to merely deciding whether a company is acceptable or not, the Investment Sub-Committee divides acceptable companies into three further categories:

- Category A - companies which amply fulfil the positive criteria of the trust.
- Category B - companies in the middle ground, which ‘could be regarded as worthwhile’ (Committee of Reference, Minutes, 12 June, 1985)
- Category C - ‘companies which were not offensive to the Investment Selection Criteria yet did not fulfil the positive criteria, in other words their activities did not offend against the “negative” criteria’. (Committee of Reference, Minutes, 12 June, 1985)

Each of the members of the Committee of Reference who attend the Investment Sub-Committee reads the EIRIS reports on each company which are circulated in advance of the meeting, and allocates their own categorisation to the company - A, B, C or Unacceptable. Then at the appropriate point in the Investment Sub-Committee meeting, each company is rated; if there is no disagreement, and if there are no comments from the other, non-voting attendees of the Investment Sub-Committee, then this rating - A, B or C - is accorded to the company. If, as is often the case, there is some dissent, a discussion will ensue. Often this will be quickly resolved, for example, one Committee member might concede that his or her rating was somewhat provisional and, in retrospect, sees no reason not to alter it in line with the majority view. However, there are also a number of issues on which there is disagreement which is not quickly resolved. More lengthy discussion then ensues.

For example, the Investment Sub-Committee in its routine company review procedure discussed the question of whether Stewardship should consider a major dairy company as an acceptable investment. Previously there had been some question about the acceptability of the company because it operated three slaughterhouse businesses worth around £100m. Stewardship has the following policy on this subject:

> 'Only in the most exceptional circumstances would the Trusts invest in company groups...whose main business involved...operating abattoirs or butchers, or other activities related to the production or processing of meat or meat products.' (IPC Document, 1995).

According to this criterion there are two possible reasons why, despite its interest in slaughterhouses, the dairy company might be acceptable as a candidate for investment. Firstly, because while the company's £100m abattoir business is a large business by any standards, it is not its main business, and in fact it constitutes less than 10% of the company's total business. Secondly, the company may be an exceptional circumstance, in which case it may be excused its involvement. In this case both lines of argument were made by the members of the Committee. One member's opening position was that the company's involvement in abattoirs was too large for it to be an acceptable investment for Stewardship. A second member argued against this that its 'main business' was the production and delivery of milk which was a basic necessity. In addition he argued that the company still did doorstep deliveries which were a valuable service to the community. The first member remained unconvinced, arguing that he would feel uncomfortable saying to unit holders that the circumstances were exceptional enough to justify investment. However, it was pointed out that while the company's involvement in slaughterhouses was substantial, it was not the company's main business, so the criterion did not apply in any case. In the end three of the members of the Committee of Reference agreed that the company was an appropriate investment, while the first member dug his heels in and took the rare step of abstaining. The company therefore joined the Stewardship acceptable list, classed as a Category C company. The discussion lasted some 20 minutes.

At the end of the selection process, Stewardship has in its possession a list of FT-SE A All Share Index companies rated either A, B, C or Unacceptable. This list comprises some 50% of the 895 companies in the Index. It is then the turn of the investment managers to take this list and from it select a portfolio of investments.

4.4.3 Investing the fund

At any one time the Stewardship Unit Trust tends to invest in about 200 companies of the 450 or so considered acceptable by the Committee of Reference. The other smaller trusts have smaller portfolios. The primary goal of the two main Stewardship funds is capital growth and, because of the ethical criteria used by Stewardship, the available universe of companies is considerably skewed towards smaller companies - broadly speaking, the larger the company is, the more likely it is to have some element which contravenes a negative ethical criterion. This means that the Stewardship investment strategy has no choice but to also be skewed towards smaller companies. Richard Lowman argues that the performance of small companies is tied more closely to the economic cycle than that of large companies. The proportion of the fund devoted to smaller companies grows with the economy, and when a downturn is expected the balance swings back to larger companies which ride out recessions better. On average 20% of the funds are invested in companies in the top 200 of the FT-SE A All Share Index, and 80% in the rest of the market. This can shrink to less than 10% and over 90%, and rise to 40% and 60%. The two main Stewardship funds - the UK growth Unit Trust and the Pension Fund are managed in almost exactly the same way, and their portfolios are almost identical. Lowman believes that the main Stewardship funds have, in financial terms, performed very creditably over the period of their existence. In only four years in the late 1980s and early 1990s has their performance been below the median of the basket of similar funds. In most years performance has been above average, and in several years in the top quartile of similar funds. Lowman thinks that the best performance measure for the 80% of the fund invested in smaller companies is the Hoare Govett Smaller Companies Index. He takes pride in the fact that the 80% of Stewardship invested in smaller companies often outperforms this index.

The process of buying and selling companies is done on a rolling basis: new stocks are bought as old stocks are sold. In many cases, the two large Stewardship funds own as much as 8% of some of the smaller companies they invest in. This means that trading in their shares is not an easy and immediate matter. Like an oil tanker, the funds cannot do an about turn instantaneously. They have to gradually move out of one company and into the next. If the fund managers were forced to sell their shares in one of their smaller holdings all at once, the company's share prices would decrease, and so would the value of the Stewardship shares it was trying to sell. This oil-tanker problem has an important consequence for the implementation of the ethical policy. If a company in the Stewardship portfolio fails, because of a change in circumstances, to meet the ethical criteria, it may not be possible to sell the shares immediately. Sales must be made gradually over a period of months. As I noted above, the Committee of Reference usually gives the fund managers up to six months to dispose of such shares. However, in practice, the investment managers usually seek to dispose of them before the next Unit Trust 'Manager's Report.' This document lists the companies in which the funds invest. If a company already in the portfolio committed some gross and public act which contravened the Stewardship ethical criteria, then it would be embarrassing and perhaps damaging if, some months later, the manager's report revealed that Stewardship was still holding shares in that company. While this gradual disposal approach is clearly sensible from a financial point of view (and it does give one last opportunity for the company to 'mend its ways'), it does mean that on some occasions Stewardship may be investing in companies which fail to meet its ethical criteria. But it is hard to see any alternative to this course of action that is without significant financial penalties.

Another consequence of this issue is that Richard Lowman does not see his role as an ethical one. He simply takes the list of acceptable companies, and chooses those stocks which he considers to be good buys at any one time. He does not seek to apply additional ethical bias, such as the Committee of Reference's ABC ethical rating system. He already faces the challenge of producing above average capital growth from a limited segment of the stock market, and does not feel that it would be reasonable to further limit himself by, for example, biasing his investment choices to, say, companies which the Committee designates as Category A over Category B or C. As of March 1996, the Stewardship's portfolio contained the following categories.

Table 5. Ethical Category.	**Number of companies in the investment Portfolio in each category (1).**	**Number of companies on the Acceptable List in**	**(1) as a percentage of (2)**

		each category (2).	
A	38	70	54
B	101	226	45
C	67	152	44

This shows that, taken together, the category A and category B companies outnumber those that are merely acceptable. However, it also supports Richard Lowman's claim that he does not apply further ethical constraints to his investment strategy beyond those that produce the acceptable list. The proportion of category A, B and C companies in the Stewardship portfolio is similar to that in the acceptable list. There is an apparent bias towards A, however, this is statistically insignificant (on a standard test). However, if a modest bias towards A is maintained over time, it would be significant and so lend support to the argument that ethical companies are successful companies: Richard Lowman is selecting from among the acceptable list on purely financial grounds, and on these grounds alone ends up with a portfolio with a bias towards the companies which the Committee of Reference considers to be the best ethically, rather than towards those companies which are merely acceptable, the 'C's!

4.4.4 Active engagement

One final aspect of the Stewardship process, which is not given much attention in the published literature, is the idea that Stewardship should use its influence to persuade companies to change their policies. This happens both informally, when the investment manager, usually Richard Singleton, visits companies in the course of routine financial assessment, and more formally when contact is made on the explicit instructions of the Committee of Reference. For example, if the Committee is unhappy with a particular company, it may ask him to write to the company expressing its concerns. Richard Singleton also has the autonomy to raise ethical issues with companies on his own initiative and frequently does. This role means that out of all the Stewardship employees, it seems likely that Richard Singleton has the most detailed knowledge of the ethical stance taken by the Committee of Reference, and probably has a more detailed knowledge than anyone of how this applies to the companies invested in. It is worth noting, however, that Richard Singleton joined Friends Provident as a general investment analyst with no special interest, knowledge or responsibility for ethics. However, he has now been working with the Stewardship funds for a decade or more, and so has gained considerable practical experience of the issues. In fact there can be few (if any) investment managers in the UK with longer experience of managing an ethical fund.

There are a number of different reasons why the Committee of Reference might ask Richard Singleton to contact a company. Here are some examples:

- A company in Stewardship's investment portfolio changes its circumstances, and as a result falls short of a particular Stewardship criterion and is therefore marked for exclusion.
- A company in Stewardship's portfolio which is failing to make satisfactory progress in a particular area of concern to the Committee.
- A company not on the acceptable list which is in many respects excellent, but which fails on a single issue. For example, as mentioned above, Stewardship contacted a well known chemist with regard to a fly killer which it sells and which contains a Red List pesticide.
- An industry sector from which companies are systematically excluded because of some collective problem.

The initial contact is usually in the form of a statement of Stewardship's conception of the problem and a request for the company's response. Richard Singleton sends about 40 letters each year, and makes another 70 contacts with companies in all. Stewardship has quite considerable holdings in a few of its smaller companies. This means that its voice is sometimes quite persuasive. This would be particularly true if the company believed there to be a chance that Stewardship would withdraw its investment. If Stewardship were to do this quickly it could have a strong short term downward impact on the share price of a small company. However, for the reasons outlined above, Stewardship is unlikely to pursue such a quick sale because it would harm the value of its own investment. Richard Singleton prefers a quiet, behind-the-scenes approach which he believes to be effective. There are occasional exceptions to this, for example, when Stewardship voted its shareholding in favour of a shareholder proposal to elect a consumer representative to the board of Yorkshire Water. While the vote was defeated, the board later appointed a director for consumer affairs.

4.5 Comparisons with other ethical funds

How does the Stewardship process compare with that offered by other ethical funds? In many respects most funds have similar screening arrangements. One respect in which this is true is that the ethical funds which use EIRIS have many individual criteria which are very similar, and often identical to those offered by Stewardship. However, other ethical funds frequently do not cover all the areas which Stewardship does. In particular the environmental funds do not cover the same range of ethical issues. On the other hand, in some cases other ethical funds cover areas which Stewardship does not.

One principal difference between Stewardship's investment policy and that of other funds is the fact that the Stewardship policy cannot be applied mechanically. Many funds adopt a set of criteria from an EIRIS Specialised Questionnaire, and then invest their funds in the resulting list of acceptable companies, periodically reviewing their investments after asking EIRIS to screen their portfolio. This is a largely mechanical or automatic process. It does not need detailed consideration or judgements about individual companies. The Stewardship investment policy contains many criteria which are qualified in ways which prevent them from being applied mechanically. The Stewardship Committee of Reference therefore has to interpret the investment policy, and apply it to individual companies. Perhaps the central distinction, is that on many issues, Stewardship attempts to weigh up the good a company does against the harm it does. Mechanical funds are not in a position do this. Not all funds follow a mechanical approach, a number - including those with their own in-house researchers - also seek to make more balanced judgements about the acceptability of companies.

Another difference concerns the way in which the criteria are produced. As we have seen, the Stewardship investment policy is produced by the Committee of Reference on the basis of considerable deliberation. The particular criteria are chosen at least partly on the basis of ethical judgements made by the Committee of Reference. This is not the case for many of the other ethical funds. Many funds - particularly, perhaps, those which do not have advisory committees - choose their ethical criteria on the basis of market research about what ethical investors are concerned about. Ethical funds, like other unit trusts, exist to serve a market, so it is not unreasonable for them to adopt the criteria that the market demands. Nevertheless this is an important distinction. In Chapter 7 I discuss what I refer to as the distinction between ‘deliberative funds’ such as Stewardship and these ‘investor-led’ funds. As we shall see, there are a number of ethical implications arising from this distinction.

Generally the quality of the information in the brochures used to promote other ethical funds is lower than that produced by Stewardship. Some funds do little more than list a collection of ethical areas which they will avoid (e.g. ‘alcohol, tobacco, gambling’), without specifying in any detail what criteria they will be using on these issues. Other funds however are rather more specific than Stewardship about the exact criteria they use. For example Scottish Equitable publishes a list which comes quite close to stating the actual criteria that the fund employs to select its acceptabel list. A handful of funds provide a relatively high level of qualitative of information, because they produce newsletters. In the case of Jupiter Ecology, NPI Global Care and TSB Environmental Funds, these are quite detailed and informative.

When it comes to active engagement, the bulk of ethical funds do very little at all. In a survey of UK ethical funds, Schoenenberger found that out of 14 who responded, only 4 had regular written dialogue with companies (1993:34). Indeed, according to EIRIS, when ethical funds divest from a company on ethical grounds, less than half of the funds even inform the company concerned that they are divesting because of their ethical concerns about it (1996a:70). There are some important exceptions. The NPI Global Care and Jupiter Ecology funds are both explicitly committed to active engagement, and regularly write to and meet with companies about matters of ethical concern. One tool that both of these funds claim is particularly useful is the ‘sector survey’. This procedure allows these funds to develop detailed knowledge about the key issues affecting a particular sector, and to get an idea of the standards of best and worst practice in that sector. These studies provide a very useful basis for comparing companies with their immediate competitors, and persuading them to change. (I discuss the activities of these two funds further in Chapter 6).

This attempt to make comparisons has been rather brief. It is based on a small number of interviews and discussions with managers of nine other ethical funds, as well as other secondary sources. Ideally, I would like to have produced a fuller study based on case studies of various other funds at the same level as Friends Provident Stewardship.

However, achieving this level of detail has been a very time consuming process, which has limited the scope of my comparative work. Of course the fact that the five Stewardship funds account for over 50% of the total ethical investment market means that my one case study has covered a significant proportion of the overall ethical investment business.

4.6 Conclusion

In this chapter I have offered an account of ethical investment as it is practised by Friends Provident Stewardship. Two earlier drafts of the bulk of this chapter have been commented on at length by various members of staff at Friends Provident, and by the members of the Stewardship Committee of Reference. It is published subject to a confidentiality agreement and with their consent. I am therefore confident that it gives an accurate and detailed picture of the practice of ethical investment. And I have put Stewardship's practice into a wider context of the tradition of practice of ethical funds as a whole. As I said in Chapter 1, my ethical method is to engage argumentatively with the tradition of practice of ethical investment. In this chapter I have offered an account of this tradition of practice. This provides the base-line for the development of my argument in the rest of this thesis.

5. Solving the 'investment ethics' problem

5.1 Introduction

This chapter moves forward from a description of procedures of ethical funds to the first steps in an assessment of their achievements. I will claim that ethical funds have achieved a considerable amount in a short space of time. The principal achievements are that they have surmounted regulatory obstacles; established a large number of institutions of varying sizes; opened stockmarket investment to a wider audience, developed a research institution and a body of research knowledge; developed 300 criteria, which they apply rigorously; and raised awareness of ethical and environmental issues in companies, and amongst the public at large. However, from the point of view of this thesis, their principal achievement has been to provide an effective solution to the investment ethics problem which I have claimed is one of the primary goods aimed at by ethical investment. So far I have stated the investment ethics problem, but I have not offered any explicit evidence that it is an important problem for ethical investment. In this chapter I will offer some evidence that the investment ethics problem is an important 'shared understanding' for the ethical investment community.

While a central purpose of this chapter is to state the accomplishment of ethical funds, there are one or two qualifications that need to be made about these achievements. These concern the inescapability of compromise in ethical investment, and the limitations to the information made available by ethical funds. This chapter will discuss these qualifications. These qualifications notwithstanding, it will in general conclude that ethical investment has achieved a considerable amount in a short space of time, and does offer a solution to the investment ethics problem.

5.2 The achievements of ethical investment

As we have seen in Chapter 3, the initial application to establish a Stewardship unit trust was rejected by regulators at the Department of Trade. It was thought that ethical funds could not serve conscience and profit at the same time. Ethical investment's first achievement was to convince the government to change its mind and allow ethical unit trusts to exist. The second achievement of ethical funds is to have established a number of *institutions*. Setting up unit trusts is not easy or cheap. It is a considerable achievement to have persuaded some 15 major financial institutions to invest considerable resources in launching ethical funds. Collectively the 30 ethical funds, and a similar number of specialist ethical independent financial advisors add up to a sizeable infrastructure for providing services to an estimated 150,000 investors, and for developing and meeting further demand for ethical investment products. It is remarkable that it is now possible to buy just about every kind of financial product - from pensions, to life assurance, to PEPs, and endowment mortgages in an ethical form. Of course many of these achievements are due as much to the pursuit of profit by these financial institutions, as they are to ethics. But unless one takes an extremely demanding Kantian view of ethics, this profit motive should not be held against the ethical achievement.

A more substantively ethical achievement of ethical investment is the development of a substantial and sophisticated ethical screening system. This system requires a very substantial body of high quality information. It requires a wide ranging and intelligent set of screening criteria, and an efficient and continually up-dated system for applying the screening criteria to the information. EIRIS provides all these things. It does research on 1,100 UK companies, and can produce comprehensive fact sheets on each of them. It employees 7 full-time researchers, and it offers 300 different criteria to choose from. EIRIS was initially financed by charitable grants, but much of its development (and 90% of its current running costs (Jepson, 1995:55), was financed by fees paid by ethical funds for screening services. As long as ethical investment remains popular with the investing public, the ethical funds will continue to be able to finance the development of increasingly detailed and broad research into the ethical and environmental practice of companies. It is crucial to the provision of an ethical screening service that when a fund says it will not invest in companies which, for example, manufacture arms, it has considerable confidence that it does not invest in such companies. EIRIS can justifiably claim to provide this confidence. It is no easy task. Modern companies are very large - often employing hundreds of thousands of people in many countries. There are often tangled webs of ownership between holding companies, subsidiaries, and other kinds of associate companies. It is a considerable achievement to be able to justifiably claim to screen out all companies with operations in a single ethically questionable area. EIRIS do this for many ethical areas.

In addition to these general achievements, ethical funds can claim to have raised awareness of the ethical and environmental aspects of corporate practice, within companies, within the investment community, among investors and amongst the public at large. As we shall see in subsequent chapters, ethical funds have helped put ethical and environmental issues much more firmly on the corporate agenda than they were in the 1970s.

5.3 Shared understandings about the Investment Ethics Problem

In Chapter 1, I said that one of the primary goods which the ethical investment tradition aims to pursue is a solution to what I have called the investment ethics problem. This good is constituted by two different 'shared understandings,' a conception of the problem, and a conception of the way in which ethical investment can solve it.

5.3.1 The investment ethics problem

The conceptualisation of the problem is as follows. According to investors, funds, and commentators alike, by investing in a company which acts unethically, one is 'supporting' that company and, in doing so, one is behaving unethically. There are a number of examples of this kind of attitude. In their marketing literature, Friends Provident Stewardship claims that the investments of many people involve them in an inconsistent moral position. People say that they 'care about the problems of the world' on the one hand, but fail to 'invest in companies which make a positive contribution to society rather than those which harm the world or its people.' (Stewardship 1995:1) This means that:

> 'Through their investments, many people may inadvertently support practices which they would find objectionable: pacifists may support the arms trade, conservationists may contribute to environmental destruction, religious people may support oppression and exploitation, non-smokers may help the tobacco industry, and vegetarians may invest in factory farming.' (Stewardship, 1995:1)

Similarly, Henderson Ethical, a smaller, newer ethical fund argues that

> Like any sensible investor, [ethical investors] want a good return on their money. But what they do not want is to have their money invested in any company, activity or regime of which they disapprove. Whether their objections are on moral, political, social or environmental grounds, they know that by investing in something they

> deplore, they are actually helping to support it and sustain it. (HTR Ethical Fund brochure, 1995:1)

These accounts of why it might be unethical to invest in a company which is pursuing unethical practices rest on the idea that by investing in a company you are supporting it, contributing to the harm it does, sustaining it, or otherwise helping it and that this is unethical.

Some have suggested an even more direct relationship between the harm done by companies and the act of investing. One fund claimed that:

> Many investors are causing, albeit unwittingly, serious damage to our planet by investing in companies that are harming the environment. (Merlin Ecology Fund brochure, 1988:1)

And Bishop Harries of Oxford, well known in ethical investment in the UK for his campaign to get the Church Commissioners to take ethical investment more seriously, has also argued this way.

> If you have watched your mother die painfully of cancer and are totally opposed to smoking, [with the advent of ethical investment] it is now possible to invest your money in a way which does not kill other people in the same way. (Richard Harries, Bishop of Oxford, in Sparkes, 1995:ix)

The implication of this last claim is that by investing in a tobacco company, one is investing in a way which kills people. And the previous quote claims a direct causal relationship between investing and harming the environment. This causal relationship implies a very serious ethical problem for investors. If these kinds of argument are right, then it would seem that investing in the stockmarket is, morally speaking, a very risky thing to do. If one is to take the claims of Richard Harries literally then by investing in the stock market one risks being, in a moral sense if not a legal one, an accomplice to murder, or at least manslaughter. Even if one does not take Harries' remarks literally, the other points, if right, seem to require that stockmarket investors give the ethics of their potential company investments very serious consideration. We will consider whether this kind of view is compelling in Chapter 8.

The 'support' conception of the investment ethics problem is not confined to ethical investors. One prominent academic business ethicist, in his chapter on ethical investment, also affirms this conception of the problem. De George (1990) claims that it is unethical to invest in an unethical operation. For example it is unethical to invest in a cocaine ring or 'If Murder Inc. were quietly seeking investors, investing in that enterprise would be unethical.' (De George, 1990:174) If a company is established in order to pursue an immoral end, then it is immoral to support its activities by investment in its stock. Ordinary corporations are not generally set up in order to pursue immoral ends, however. Yet, de George argues,

> 'by analogy we can argue that even if a company is established for a legitimate end, if it in fact has a policy of engaging in unethical practices, then no one can morally support its activities through the purchase of its stock.' (1990:174)

Since its beginnings in the UK, the investment ethics problem, conceived more or less in this form, has been a central 'shared understanding' of the ethical investment community.

While the conception of the investment ethics problem as an ethical dilemma arising from the fact that one may be 'supporting' companies engaged in unethical practices is widespread, it would be wrong to imply that this is the only conception of the investment ethics problem held by ethical investors. For example, one ethical investor I interviewed, when asked what was wrong with investing in a company with unethical practices, said:

> I was supporting them [companies] in that I was going to get dividend payments from them, you know the better they performed the more I would get from them and of course the better they performed, say for example Tarmac [a construction company], the more roads they were building through nice places like Twyford Down.[1]

What was unethical for this investor, was partly that he was supporting the company, but also that he was profiting form the harm done by the company, and he made this relationship rather direct, the more harm the company did, the more he would profit. And in addition to specific concepts such as 'support' and 'profit' I think it is fair to say that there are also rather vaguer conceptions that the problem is not associated merely with a particular kind of relationship companies, but *any* kind of relationship. If a company engaged ethically questionable practices, then at least some appear to feel that

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[1] Interview with the author.

any kind of involvement is undesirable. At least some ethical investors want to be ethically ‘clean’. They do not want their money ‘tainted’ in any way. While this rather vaguer interpretation of the shared understandings is found within the tradition of ethical investment and, as we shall see in Chapter 8 requires consideration, I maintain that the central understanding of the investment ethics problem is based on the idea of support. The idea that by investing in companies with unethical practices one is supporting (or profiting from) those companies and those practices, and the idea that this is unethical is deeply ingrained within ethical investment. It appears widely within the marketing literature, and was stated by many of the investors I interviewed.

One reason why it is useful to conceptualise the investment ethics problem as a ‘shared understanding’ and locate it within the context of ‘methodological communitarianism’ is the idea that the shared understandings about the investment ethics problem do not float free of the practice of ethical investment, but are at least partly dependent on ethical investment. While it is likely that the conception of the investment ethics problem pre-existed ethical investment, and may be widespread in people who have not even heard about ethical investment, it is possible that part of the achievement of ethical investment in the last 12 years has been to establish the idea in the public mind that there is an ethical ‘problem’ about investing in the stockmarket. In order to encourage people to take ethical investment seriously, and to consider investing in it, first investors have to be persuaded that there is a problem about the kind of investments that they have traditionally made use of. Ethical investment funds - and the ethical investment community in general - have therefore sought to popularise their conception of the investment ethics issue as a problem for investors. In fact the form of the problem that they have sought to use is a rather particular one which, as we shall see in Chapter 8, is not the only one available. The particular conception of the investment ethics problem that is shared by the investment ethics community is therefore not simply something that ethical investment has responded to but that it actively promotes and sustains - sometimes by using the rather extreme rhetoric of the kind we have seen above.

5.3.2 The conception of the solution to the investment ethics problem

Of course there would be no point in promoting this conception of the problem if ethical funds did not also offer a solution to it. I have tried to offer an account of the solution to the problem found within the ethical investment tradition in Chapter 4. The solution is to use screening procedures to avoid investments on companies which are engaged in unethical practices, and to invest instead in ethically exemplary companies. There are different conceptions about what this entails. For example their are different ideas about whether companies engaged in unethical practices should be avoided absolutely, or whether a small amount of unethical activity might be tolerated; and different ideas about whether the good a company does can be regarded as outweighing the harm it does. However, the practice of ethical funds demonstrate that their basic conception of the solution to the investment ethics problem is negative screening and positive selection. This solution is broadly consistent with the 'support' conception of the investment ethics problem. By avoiding companies engaged in unethical practices, one is avoiding supporting those companies, profiting from them, or more generally being involved with them. (Indeed, by positively investing in good ones, one is achieving even more than one needs to, in order to simply solve the investment ethics problem.)

Do ethical funds effectively implement this solution? Generally, it is reasonable to argue that they do. As we saw in Chapter 4, ethical funds offer a range of criteria which identify various unethical aspects of corporate practice; through EIRIS, they have a research service which is able to screen companies on each of these issues, producing a list of acceptable companies; ethical funds then invest in these companies, and where possible in companies which are not merely acceptable but exemplary. This is a solution to the investment ethics problem, because it allows investors to be reasonably certain that they are not investing in companies with grossly unethical practices. To able to offer this solution consistently over time to such a large number of people, across such a wide range of financial products, is the considerable achievement of ethical funds in their first 12 years.

5.4 Constraints on screening as a solution to the Investment Ethics Problem

The considerable achievements of ethical investment should be recognised. However, there are certain issues concerning their achievements with respect to the investment ethics problem which need to be examined. In particular I want to see what, if any, difficulties an investor may encounter in using ethical funds to solve the investment ethics problem. While ethical funds provide an effective procedure for solving the problem, an individual investor may encounter a few difficulties using ethical funds for this purpose. To illustrate this, I propose to consider an imaginary ethical investor who has a clear idea of what kinds of corporate activities are unethical. Let's call her the 'expert ethical investor'. (In the next section we will consider some problems for investors who have not formed a clear idea of the ethics of corporate practice which, we will call 'uncertain investors'). In order to solve the investment ethics problem, an expert ethical investor must find a fund which has an investment policy which is similar to her conception of what is unethical about corporate practice. As we shall see in the next two sections, an expert ethical investor might encounter two kinds of difficulty in finding such a fund. Firstly, she might find it hard to find a fund which matches her understanding of the ethics of corporate practice, and secondly, even when such funds exist, she might find it hard to get enough information about ethical funds to make a sensible decision.

5.4.1 The need for compromise

To completely solve the investment ethics problem for just one investor, a fund does not simply have to match an investor's ethical principles on one issue, but on all relevant issues. Given that people's conceptions of the ethics of corporate practice vary, and given that ethical funds can only offer a limited and fixed package of ethical exclusions, ethical funds will only be able to completely solve the investment ethics problem for a limited subset of investors. For example, an ethical fund might have absolute ethical exclusions on arms, tobacco and alcohol, and partial ethical exclusions on meat production and pollution. This will solve the investment ethics problem for people with similar ethical priorities, but it will not for an investor who may be prepared to tolerate some degree of investment in alcohol and tobacco, but is profoundly opposed to meat production. In such a case, the fund is not offering a pattern of exclusions which matches the investor's conception of the ethics of corporate practice. There are a large number of ethical areas - EIRIS lists 18 (EIRIS, 1996a) - which offer a potentially huge range of combinations of ethical view points. Any two investors may agree on tobacco, alcohol, and arms, but disagree on meat, or agree on tobacco, alcohol and meat, but disagree on arms, etc.

Of course particular points of view may cluster together. Anand and Cowton (1992) have shown that there may be some statistical clustering of investors' ethical conceptions into particular groups. However this effect will only reduce the number of combinations somewhat, but still leave a considerable number of different individual investors' conceptions of the problems of corporate ethics. It is rather unlikely that the ethical funds can match this diversity of ethical opinion. There are only 30 ethical funds so investors are limited to choosing between 30 packages of ethical exclusions.

In fact may ethical funds have adopted rather similar sets of exclusions and so the ethical packages of many funds are alike. This is partly because many of the ethical funds to choose their screening criteria from the same list provided by EIRIS. Some critics have argued that the choice of criteria offered by ethical funds is from a rather narrow ethical point of view. For example, Entine claims that ethical funds promote 'narrow social agendas' (1995:3). Mueller (1991:113) has described ethical investment as, at least in part, sectarian. Although he notes that ethical investment is not religious in the narrowest of senses,

> 'many of its proponents have close ties to organized religion, and practically all of them share certain normative standards that are at variances with those to the wider society, especially those of the investment community.' (Mueller, 1991:113)

Entine illustrates his point by contrasting the values promoted by US ethical funds, with the values adopted by a South African trades union ethical fund.

> 'In 1991, black trade unions in South Africa surveyed members on how to invest their $175m pension fund. Rather than relying on "ethical" categories popular in North American and the UK, the group came up with its own guidelines for The Community Growth Fund (CGF). Litmus-test social issues such as idealistic mission statements, animal testing, liquor and beer sales were dispensed with; CGF's most important criteria are product quality, jobs, working conditions, benefits, safety, and equal opportunity.' (1996:19).

The basic argument here is that UK ethical funds might be regarded as meeting the ethical needs of only a narrow subset of the UK investing public. Their ethical policies are not, perhaps, representative of 'mainstream' values but only of particular sub-groups. This is not a failing in itself. But it does limit the number of ethical positions that will be satisfied by the packages offered by ethical funds.

All this means that in practice ethical funds only offer complete solutions to the investment ethics problem to people with a fairly small range of views on the ethics of corporate practice. This alone does not reverse my claim that ethical funds do not solve the investment ethics problem. It merely means that only in rare instances will the solution be *complete.* In practice many expert ethical investors will simply have to make compromises on one or more of their principles.

Compromises can be in two directions. One can accept a fund that offers a *weaker* ethical policy than your principles require, or accept a fund that offers a *stronger* ethical policy than your principles require. The first kind of compromise is obviously unsatisfactory, though it may prove acceptable to investors. Before considering it in more detail, it is worth briefly considering whether the second kind of compromise is acceptable. Is it bad if a fund is *too tough?* For example, if one is concerned about the manufacture of landmines, or the arming of oppressive regimes, but quite happy for arms companies to manufacture weapons for the British Army and UN peacekeepers, is one really making a compromise if one chooses a fund which avoids investment in *all* arms companies even if they are not engaged in the manufacture of landmines or other specific activities which you oppose? One might argue, as Anderson et al. (1996) do, that such 'toughness' is unfair to the companies concerned. But there is no moral compulsion to support *every* company that is consistent with your principles. So perhaps this unfairness is tolerable. Another kind of objection is that by avoiding all arms companies you are denying yourself the opportunity to engage with the arms industry in order to persuade it to adopt more sensible policies on selling arms to oppressive regimes, and to stop them making land mines. This seems to be a reasonable point. It may mean that by solving the investment ethics problem one is limiting ones ability to address the wider corporate harm problem. We will return to this issue in Chapter 8.

There are several advantages for ethical funds in adopting tough ethical criteria. If it is easier for investors to compromise towards overly tough criteria than it is for them to compromise towards insufficiently tough ones, then by adopting tougher criteria, one opens up a wider field of investors. There is also perhaps a marketing advantage to be had from having tough criteria. There is some anecdotal evidence to suggest that investors are attracted by funds with the tightest criteria, because they see them as the 'most' ethical. This is not necessarily the case. From the point of view of the investment ethics problem, the most ethical fund might be the one that avoids only those companies which it considers to be acting unethically, no more, no less. Being tougher than you need to be is no virtue. But perception may be what is important in the market place, and the perception of ethical investors may favour tough funds.

While expert ethical investors might be forced to compromise because ethical funds are too tough for them, they may also have to compromise because the funds are not tough enough, and so do not offer a complete solution to the investment ethics problem for them. One issue that I have already discussed is that ethical funds offer packages of exclusions which may not fully cover the exclusions an individual investor would require to solve their investment ethics problem. Another similar reason why compromise might become necessary is that most of the ethical funds do not exclude *all* companies engaged in the unethical activities mentioned in their ethical policies. Frequently funds make qualifications to their criteria. These make exceptions for companies whose involvement in activity, which is regarded as unethical, falls below a certain threshold. The threshold can be an absolute value of, say, turnover. For example, one ethical fund will not invest in any company which derives more than £1m from gambling. Alternatively, and more commonly, the threshold can be a proportion of the company's business. For instance one fund allows itself to invest in companies in various areas regarded as unethical as long as they do not derive more than 1% of their turnover from such areas. In other cases funds allow companies in to their portfolio as long as their involvement in an unethical practice is less than 10% of that company's turnover. And on some issues, funds stipulate that they can invest in a company so long as the unethical practice is not the companies 'main business'. There are plausible pragmatic reasons for making these exceptions. However, they can weaken the solution the fund can offer to an individual investor to the investment ethics problem. If you are a committed vegetarian and you feel that by investing in a company you are supporting it, you may consider that nothing less than total exclusion of meat producing companies is acceptable. You may feel that it would be wrong to invest in a fund that only excludes companies whose 'major business' is meat production because such a fund may well invest in many substantial meat production businesses.

It is certainly true that the practice of making exceptions on the basis of proportions of turnover can lead to some strange anomalies. For example, lets take a criterion which excludes all companies which derive more than 10% of their turnover from the sale of tobacco. This criterion would mean that a small newsagent chain, which sells £10m of tobacco goods, out of a total turnover of £50m would be excluded because it derives 20% of its turnover from tobacco. A large supermarket chain, on the other hand, which sells £150m of tobacco products out of a total turnover of £2bn would be acceptable because it derives only 7.5% of its turnover from tobacco. The supermarket is acceptable, even though it sells 15 times as much tobacco as the newsagent, which is unacceptable.

Another kind of exception ethical funds make which might limit their appeal to investors seeking a solution to the investment ethics problem, is that some funds allow the good a company does to outweigh the bad. That is, if a company is unethical in one respect, but particularly good in another respect, then they will allow the company to enter the portfolio. As we saw, Friends Provident Stewardship, does this, and for good reasons. The example of this which we discussed in Chapter 3 (see p.107) was a diary company which amongst other things delivers milk to people's doors. The home delivery of milk is regarded as being a positive contribution to society. However, this company also owns subsidiaries which run abattoirs and account for less than 5% of its business. For those opposed to animal farming, this will count against the company. A fund that allows the good to outweigh the bad may argue that this food company is on balance a good company, and so deserves to be invested in. If you are a principled vegetarian, however, you may feel that to invest in the company would be to support its abattoir business, and so would be inconsistent with your principles. This may be particularly true when you learn than the company is a big company, and the 5% of turnover provided by the abattoir subsidiaries could be more than £100m.

There are other more trivial reasons why an expert investor with her own schedule of ethical positions might find herself compromising by investing in ethical funds. At least some ethical funds do not immediately dispose of companies in their portfolio if, by change of circumstance, they come to fail to meet the funds ethical criteria. When for example, a company in an ethical fund's portfolio acquires another company as a subsidiary, and that new subsidiary, say, produces armaments, then the company may move from being acceptable to being unacceptable for the fund. However, the fund may not immediately sell it. Indeed the fund will not necessarily know about it immediately. Funds review their portfolios on a reasonably regular basis, so this factor will not apply for long. However it is true that for months at a time a given fund may possibly be holding one or more companies which falls short of its criteria. Furthermore, even when the ethical fund learns that it has such a company in its portfolio, it will not sell instantly. As we have seen (see p.109ff.), ethical funds may wait for a period of several months before selling an ethically questionable stock. Firstly, they must decide whether divestment is the best path. The fund may, for example, seek to determine whether the parent company plans to cease, or sell off, the arms manufacturing operations of the subsidiary, thereby obviating the need to divest. And secondly, if the path of divestment is chosen, the fund manager will need time to divest gradually at the optimal time, in order to realise the best price for the shares. These practices are sensible. However, they do mean that at any one time an ethical fund may be investing in at least a few companies which contravene its ethical polices. If one or more of these companies are acting in a way that conflicts with the investor's principles, then that fund will not be offering a perfect solution to the investment ethics problem. If, on the other hand, funds adopted the policy of selling unacceptable shares immediately, investors would have to compromise on their financial performance.

The fact that expert ethical investors may often be forced to compromise their principles to some extent was not denied by those I spoke to about this issue in the ethical investment business. One of whom argued that the idea that ethical funds can offer a complete solution to the investment ethics problem is unrealistic. The point, he said, is that ethical funds allow investors to bring their investments *closer* to solving the investment ethics problem, than they would have been if they were invested in an ordinary unit trust, for example. Very many ethical investors seem happy to make these compromises. However, according to one of the leading ethical specialist IFAs, occasionally potential investors are unwilling to make these compromises and they therefore find they are unable to invest in equity investments at all.

5.4.2 The disclosure issue

Above I said that the expert ethical investor might encounter two kinds of difficulty in finding an ethical fund which solved the investment ethics problem for her. Firstly, she might find it hard to find a fund which matches her understanding of corporate ethics, and secondly, even when such funds exist, she might find it hard to get enough information about ethical funds to make a sensible decision. In the previous section, I argued that it may well be very difficult to find an ethical fund which excludes exactly those areas which one would like to exclude. In this section I will argue that it can be quite difficult to find out exactly what kinds of corporate activities ethical funds consider to be grounds for avoidance. Expert ethical investors need detailed information about the ethical criteria and positions of ethical funds. They need this so they can work out whether the ethical policy produced by the fund is consistent with their conception of what is unethical about corporate practice.

Funds are often not very good at publishing detailed information about their criteria either. Often their published material seems to provide an insufficient basis on which to make a good judgement about whether investing in the fund would be consistent with one's principles or not. Funds divide into two groups as far as disclosure is concerned: a small minority which seem to publish something close to the actual criteria they use for screening, and those which do not publish their exact criteria but instead either simply name the areas in which they have exclusionary criteria, and summarise or paraphrase these criteria.

Here is an example of the contrast:

The Scottish Equitable Ethical Unit Trust's published material states clearly that it will not consider as suitable for investment companies 'for which brewing, distillation or sale of alcoholic drinks accounts for more than 10% of its total business' (EIRIS, 1996a:96). Several other funds, on the other hand, simply list 'alcohol' as a an 'area of concern.' (EIRIS, 1996a).

Publishing something close to actual criteria is rather more useful to expert ethical investors than publishing a paraphrase or a summary. With funds that simply name ethical areas, or offer brief summaries of their ethical positions it is impossible to work out exactly what the fund's polices mean. This can be important. If your ethical position is that all production or sale of alcohol is wrong, then you cannot be sure that a fund which lists 'alcohol' as a negative criteria will be avoiding all such companies. As it happens, in some cases by listing alcohol the funds are referring primarily to the *production* of alcohol and not its *sale*. By investing in such a fund the investor may therefore be 'supporting' companies which derive turnover from the *sale* of alcohol.

However, even funds which publish actual criteria may not go far enough from the point of view of enabling investors to establish whether the fund would be consistent with their personal principles. The problem is that it is not clear what the words and concepts used in the short statements of criteria actually meant in practice. For example, when Credit Suisse Fellowship says that it will not invest in:

> Companies which have been involved in the sale of production of weapons systems and producers of strategic goods or services for military users.(EIRIS, 1996a:80)

What is meant by ‘weapons systems’? Ethical funds generally do not provide any explanatory notes on their criteria. The absence of detailed notes means that there is a lack of precision about just what each criterion actually stands for, and so leaves scope for investors to be mistaken. In fact EIRIS does provide to its members a ‘Guide to EIRIS Research: Definitions’ (EIRIS, 1996b), which explains in some detail what the terms used in all its criteria mean. This means that if a would-be investor becomes a member of EIRIS and asks for this document they will be able to get a very clear idea of the criteria of those funds which use EIRIS’s research services. So for example if you have this document, then you can make the reasonable assumption that, as Credit Suisse is using EIRIS criteria, it will follow EIRIS’s definitions of ‘weapons systems’ which states:

> ‘weapons and platforms for weapons. By weapons we mean products sold for military users that are designed to kill, maim, or destroy. This can include ships, tanks, armoured vehicles, aircraft, guns, grenades, bombs, mines, munitions, and ammunition. Under production of weapons systems we include the refitting of such systems. By platforms for weapons we mean ships, planes or other vehicles from which weapons can be deployed whether or not the prime function of the vehicle is that of a fighting weapon. This would include a supply ship which has missiles and guns aboard for defence as well as a landing craft or small boat which has weaponry fitted. (EIRIS, 1996b:26-27.)

This definition itself introduces new words that could also themselves be defined, but the definitions must come to an end somewhere, and this paragraph gives us a very clear idea of what EIRIS means by weapons systems. In its Guide, EIRIS also defines ‘sale or production of...for military users’, ‘goods or services for military users’ and ‘strategic goods or services’. Given that EIRIS publishes these definitions, it would not seem very onerous to expect funds to provide a little more information about what their criteria mean.

One rather extreme example of the problem arising from not defining ones terms, is provide by the Allchurches Amity Fund. This fund’s policy states that it ‘avoids investment in those companies whose practices may be considered detrimental in building a safe and prosperous society, such as companies materially involved in the alcohol, tobacco and gambling industries and those who produce magazines or video tapes of an explicit nature’ (EIRIS, 1996a:75). However, according to EIRIS data the Allchurches fund invests money in companies involved in the sale of alcohol, including at least one company that is in the top ten retailers of alcoholic drinks in the UK (EIRIS, 1996a:19). It also invests in at least one company that derives more than £100m of its turnover from the production or sale of tobacco products, and at least one company that derives more than £10m from the production of tobacco (EIRIS, 1996a:51). It also invests in at least one company which either publishes, prints or wholesales magazines that fall within the Campaign Against Pornography and Censorship's proposed legal definition of pornography, or newspapers that contain 'page 3' photographs; as well as at least one company which provides adult entertainment services' (EIRIS, 1996a:43). However, on EIRIS data, Allchurches does avoid all companies involved in gambling. These apparent contradictions reveal that published ethical policies are not always as clear as they might be. It should be noted that Allchurches does not use EIRIS's research, it is likely that is therefore not typical of ethical funds as a whole, most of which do use EIRIS, and are unlikely to demonstrate such sharp apparent inconsistencies.

While there are some limitations to the amount of material published by ethical funds, since 1996, ethical investors have been offered another source of information on the investments of funds. The EIRIS *Money and Ethics* (1996a) guide provides detailed criteria by criteria studies of all the ethical funds, showing the extent to which the ethical funds' portfolios conform to EIRIS's own criteria. So, for example, the guide will be able to tell you which funds are avoiding investments in companies which have been involved in the sale or production of non-civilian goods or services for weapon systems. It can do the same on each of more than 150 individual criteria. This is a very useful guide to the portfolios of ethical funds. However, it has limitations as a guide to the ethical fund's policies. For instance, it only covers those holdings of ethical funds which are in the UK, so it is not 100% reliable for international funds. It also is a snapshot of current portfolios, not a statement of the policies of funds. It is possible that ethical funds which the guide shows to be avoiding investment in companies making goods for weapons systems are doing so by accident and not as the result of policy. Unless the fund's own policy commits it to doing so, the fact that such a fund avoids such companies today, does not necessarily imply that it will do so tomorrow. This having been said, the guide is a very useful resource.

In conclusion, if ethical funds are to serve as solutions to the investment ethics problem, it is important that investors are able to get detailed information about the investment policies of the funds. At present there are some limitations on the ability of investors to do this. To improve things, funds need to publish the actual criteria they use for screening, together with notes which explain these criteria in detail, and the procedures which they use to apply them. This conclusion chimes with Russell Sparkes', that one area in which ethical funds could 'do better' is the area of transparency and greater disclosure (Sparkes, 1995:47).

5.4.3 The needs of uncertain investors

So far we have been considering problems that 'expert ethical investors' might encounter in using ethical funds as a means of solving the investment ethics problem. But is it likely that most people have worked out a full set of ethical positions on all of the many issues of corporate practice? Probably not. As we shall see in Chapter 7, this task poses a considerable challenge to the ethical funds themselves. Most investors may simply lack the time, information and expertise to do this considerable ethical work. Certainly I have found little evidence that most ethical investors have a set of principles on the details of corporate practice. It is possible then, that many investors are not 'experts' in this sense. They have not decided exactly what is unethical about companies. This makes it rather hard for them to solve the investment ethics problem. If you do not know what it is which is unethical about corporate practice, how do you decide which companies to avoid investing in? One response is to turn over the task of making ethical judgements to the ethical funds. Investors who do this need the fund to make wise ethical judgements on their behalf. What counts as a wise judgement? Different people with different ethical perspectives may disagree on what constitutes good judgement. If you have strong anti-abortion feelings, you may be wary of investing money in healthcare companies, for example, but if you are not particularly worried by the abortion issue, these might be among the most ethical of investments. So part of what counts as a 'wise' choice is the ethical perspective taken by the fund. Another aspect of what counts as a wise choice is the issue of whether a fund has adopted procedures for decision making which are good enough. We will discuss this issue at length in Chapter 7. Ultimately the best way to decide whether an ethical fund makes what you would regard as wise ethical judgements is to look at the ethical positions that it takes to decide whether they seem convincing or authoritative, or at least whether they inspire trust. Unfortunately, as we will see, the ethical funds do not tend to publish ethical positions. So the only way for undecided investors to make a reasonable choice is to look for information about whether the fund has an advisory committee, how often it meets, whether it employs in-house researchers, and whether it publishes an informative newsletter. Also, IFAs specialising in the ethical funds have considerable inside knowledge of the funds, and so can offer their judgement.

5.5 Conclusion

We can conclude from these discussions that, for those investors with clear principles of their own, ethical funds are effective at enabling them to achieve a solution to the investment ethics problem. However, it is likely that any given investor will have to make some degree of compromise. The job of making a good choice between funds is made harder by weaknesses in the way funds disseminate information about their investment policies. Uncertain investors have a different kind of problem. Such investors need to trust an ethical fund to make wise judgements of their behalf. As we shall see in Chapter 7, it is not always easy to establish an indubitable basis for such trust.

It would be unfortunate in focusing on the weakness of the ethical funds in these ways to leave an overall negative impression. There is little doubt that in spite of these short comings, an average investor is likely to come rather closer to solving the investment ethics problem by investing in an ethical fund than she is if she invested in, say, an ordinary unit trust. Ethical funds have achieved much in a short time, and do offer a sensible solution to the investment ethics problem.

6. Ethical funds and the 'corporate harm' problem

6.1 Introduction

In the Introduction I claimed that ethical funds offered a fairly effective solution to the investment ethics problem. I offered evidence in support of this claim, and a few qualifications in Chapter 5. However, in the Introduction I also said that the other primary good that ethical investment sought to achieve was to address the corporate harm problem. I also claimed that ethical funds are not currently very effective at achieving this goal. In this chapter, I offer evidence for this claim. I begin by offering evidence that ethical funds do indeed wish to address this corporate harm problem. Then I describe the means which they employ to address it, which I shall refer to as 'market signalling', and 'active engagement' respectively. I then consider the efficacy of these means.

6.1.1 Addressing the corporate harm problem as a primary purpose of ethical investment

One important 'shared understanding' concerning ethical investment is that a central goal of ethical funds is to use their influence to promote more ethical and environmentally sustainable corporate practice. What is the evidence for saying this? The principal founder of ethical investment in the UK, Charles Jacob, says that 'influencing companies' is one of two goals of ethical investment (The other is investing in companies which make a positive contribution, which is one way of solving the investment ethics problem.)[1] A number of ethical investors I talked to said that their belief that ethical investment can effectively address the corporate harm problem is an important part of their motivation for investing in ethical funds. In a recent survey 68% of Friends Provident Stewardship investors said that 'Clear strategy to exert ethical influence on companies' was 'very important.' This was the second highest ranked item (see table on p.81)

[1] Interview with the author.

The goal of addressing the corporate harm problem is also found in the marketing literature of ethical funds. An NPI Global Care leaflet states,

> 'Investment will also be made in companies which the Managers believe could, with encouragement, make a greater contribution to these [ethical and environmental] objectives. The trust aims to achieve positive change across industry.' (NPI, 1995a)'

And the leaflet also asks, 'Do we use our influence to encourage companies to change?' and replies:

> 'Encouraging change through dialogue is one of the aims of the Global Care family of funds...Meetings and visits are used to encourage companies to raise social and environmental standards...With active encouragement from shareholders, we believe companies can improve their response to environmental and ethical concerns.' (NPI, 1995a:13).

Jupiter Ecology states that

> 'An important element of JERU's [Jupiter Ecology Research Unit's] dialogue with companies is the promotion of improved environmental performance. In particular the Research Unit urges companies to integrate environmental issues into every day business management and to increase environmental disclosure.' (JERU, 1996)

In 1992, the Social Investment Forum (SIF) in the US proposed a resolution for the UN Conference on Environment and Development in Rio de Janeiro, which stated that 'financiers are the pump primers of the global economy - they can withdraw funds or give their full support to any enterprise. They can therefore uniquely and powerfully influence the course of industrial development so that it is compatible with the sustainable development agenda.' (SIF, 1992)

It should be clear from this that ethical investors do seek to address the corporate harm problem. Of course investors are not the only people who have a role to play in addressing this problem. The most forceful limits on the ethical behaviour of companies are probably set by the law and by government appointed regulators. Companies are also influenced by the informal norms of acceptable business practice which exist within their industry and amongst the public at large. And they are influenced more directly by their stakeholders - customers, employees, and suppliers. But there is no more important stakeholder than the shareholders. Investors are the principal suppliers of capital to companies, they finance the development of business enterprise. For many company directors, the pursuit of 'shareholder value' is the principal purpose of business enterprise.[2] The directors can be forgiven for seeking to please the shareholders, because the law gives shareholders, and shareholders alone, the power to appoint and dismiss the board of directors. In fact, this power can be regarded as making shareholders the ultimate source of control for companies (Goyder, 1987:35). SIF may well be right, then, in claiming that investors are 'uniquely and powerfully placed to influence the course of industrial development.' (SIF, 1992).

However, there have been criticisms of the ability of ethical funds to effectively address the corporate harm problem. In particular it has been argued that the screening approach (which is the central method used by the UK ethical funds) has little contribution to make to influencing corporate practice. As Miller (1991) has said 'The main arguments against SRI are that: one cannot hope to change the ways of a major institution simply by buying or selling its shares.' (Miller, 1991:7). Dowie (1993) also argues that the screening approach to ethical investment does not persuade companies to change. He claims that there is not a single documented case of a management changing its social policy in response to divestment of shares in a company (Dowie, 1993:55). Indeed, many of the ethical investment professionals and a number of economists I have spoken to are dubious about the impact of screening on share prices. In this chapter I seek to assess these criticisms.

6.1.2 Means of addressing the corporate harm problem

There are two ways that ethical funds claim that they might be able to influence companies to adopt more ethical and more environmentally sustainable policies. One is through market signalling, the other is through what has been called 'positive action' (Domini and Kinder, 1986), or 'active engagement', and which is in many ways a form of shareholder action.

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[2] Whether the pursuit of shareholder value should be the goal of business enterprise is open to dispute. See Goyder (1987), Drucker (1991a), Sorell and Hendry (1994) and Sternberg (1994) for examples. It is also questionable whether companies do, as a matter of descriptive fact, pursue shareholder value as their principal goal. However, the fact that many directors at least pay lip-service to this goal is important for my point here.

The market signalling approach is based on the following claims. If ethical funds divest, or avoid shares in companies with unethical practices they will force down the company's share price. And because companies care about their share prices this will induce them to change their practices. Conversely by supporting exemplary companies, ethical funds will push the share prices of these companies above the equilibrium market rate. This will incentivise companies to excel. The general idea is that ethical investors can send ethical signals via the stockmarket. As Sorell and Hendry have noted (1995:134), in this respect ethical investment is similar to 'ethical consumerism'. Ethical consumers, like ethical investors, hope that by adopting ethical purchasing behaviour they can send ethical signals to companies and persuade them to change. Avoiding shares of companies with unethical practices is also in some ways similar to the idea of consumer boycotts. Indeed it is possible that the idea that boycotting shares might be effective may arise from the perceived success of consumer boycotts.[3]

I will argue that the market signalling approach is not an effective as a way to persuade companies to improve their practices. One reason for this is that ethical funds are too small to be noticeable. But even if ethical funds were rather larger they may not have a long term effect because any short term downward pressure on share prices would be counteracted by routine activity by ordinary financially motivated investors on the market. Ethical investment would have to be much, much larger than it is for it to have a noticeable downward effect on companies in general.

These arguments also apply to attempts by ethical funds to push up the share prices of exemplary companies. However, I will argue that ethical investment funds might be able to sustain a small premium on the shares of smaller companies which they proactively invest in, because the markets for shares in these companies are illiquid, and so may outweigh the effects of ordinary financially motivated investors. This will provide an incentive to smaller companies to court the ethical investment funds, and may have a positive effect. However, this is far from the popular idea that the ethical investment business, by boycotting the shares of large multinationals, might force them to change their policies. This is unlikely to happen on the basis of ethical investment's effect on the markets. Finally, I will offer several ways in which ethical funds can influence

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[3] For a detailed account of consumer boycotts, and an assessment of their efficacy see N. Craig Smith (1990).

practice which do not make use of market signalling directly, but may offer an indirect means.

The engagement approach is based on the idea that ethical funds should seek to persuade companies either by force of argument or by pressure tactics to adopt more enlightened policies. There is a range of techniques available to investors who seek to engage with companies in order to persuade them to change, from letter writing, and meetings with management, to providing advice, and comparing companies within particular sectors, to asking questions and proposing resolutions at company AGMs, to campaigning publicly for better practice. I will argue that currently in the UK, compared to screening, engagement is underdeveloped as an approach. However, there are some early signs that engagement can be effective. In the US, ethical funds, pension funds and other activist bodies have demonstrated that engagement can be extremely effective as a means of addressing the corporate harm problem. I will argue that ethical investment is not as effective as it might be in the UK for several reasons: difference in regulatory regimes, lack of a strategic approach, lack of resources, lack of targeting of poorly performing companies.

I conclude that market signalling is in general ineffective, but that, on evidence from the US, active engagement is a promising means for persuading companies to change, but this method has not so far been used concertedly in the UK. Because neither of the main mechanisms which may be used by ethical funds to exert influence on companies are currently substantially effective, I am forced to the negative conclusion that, currently in Britain, ethical funds do not offer a very effective means of addressing the corporate harm problem. However, arguably it is still early days for ethical investment in the UK, and as I indicate in the final chapters of this thesis, there is much that can be done to improve performance.

6.2 Efficacy of market signalling[4]

Let us consider the idea that ethical funds can change corporate practice using market signalling. As Peter Webster, director of EIRIS, has put it:

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[4] My argument in this section has been considerably improved as a result of conversations with Dr. Adrian Winnett, an economist at Bath University.

> If large numbers of investors decide not to buy a share '*at any price*' [because it is considered unethical] this alters the balance of buyers and sellers. Company groups may well be influenced by the resulting changes in the value put on their shares. (EIRIS, 1991:7)

The basic idea here is that if ethical investors boycott particular shares, they will, because of the law of supply and demand, drive down the price of those shares. It is not clear how widely this conception is shared within the ethical investment community. Peter Webster, as the executive director EIRIS since its inception is a very significant figure within the ethical investment community. He has offered versions of this argument on a number of occasions (EIRIS, 1992:7; EIRIS, 1993:7). Several of the ethical investment professionals I spoke to offered an account similar to the one just given. However, a similar number of other ethical investment professionals rejected this approach. Who is right? Given that a key goal of corporations is to maximise long term shareholder value,[5] a downward movement in the company's share price should be of considerable concern to its directors. In addition, a lower share price increases the cost of raising capital for the company, which will also not be desirable. If ethical funds can convince company directors that by avoiding investment in that company's shares they can significantly lower its share price, then company directors will have a strong incentive to take the necessary steps to stop this happening. Under such circumstances ethical funds using the negative screening approach would carry a big stick and be considerably powerful. But do ethical funds have the power to move share prices? The simplest example is a case where an ethical funds sell their shares in a single company.

6.2.1 Divestment from a single company

Periodically EIRIS produces a 'portfolio screen' for its ethical fund clients. This screen identifies companies in the fund's portfolio which have changed their ethical status in the previous period. A typical example would be a company which had been acceptable to fund, but which has recently bought a subsidiary company which contravenes the fund's criteria. It is likely that in such a case the fund is likely to give instructions for the company's sale. Would such a disposal force the share price downwards? This depends on three things, the size of the company, the size of the ethical fund's holding, and the liquidity of the market for company's shares. The holdings ethical funds have in large

[5] See note. 2

companies are tiny. Even Stewardship's holding in a FT Index top 100 company never exceeds 1%. While the liquidity of these companies' shares is variable, it is likely that it would be able to absorb the sale of such a small holding without any noticeable effect on the share price. It is unlikely, therefore, that at their present scale ethical funds can depreciate the share prices of large companies by selling their shares.

The situation is different for smaller companies. The holdings of some of the larger ethical funds in some of these smaller companies runs to a few percent. The liquidity in the market for the shares of these companies is lower. It is quite likely that were one of the larger ethical funds to sell its stake in one of these companies all at once in a short period, the market would not be able to absorb the sale without a dip in the share price. In theory then, ethical funds could force a depreciation in the share prices of smaller companies in the short term.

Would such an effect be lasting? Companies, according to standard financial markets theory (Howells and Bain, 1995), are judged on the basis of their 'fundamentals' - analysts' estimates of the company's underlying value in terms of discounted predicted future profitability, and hence dividend yield. These estimates will not change simply because an ethical fund, however large, has sold its investment in the company. Consequently, if an ethical fund is successful in pushing down the share price of a small company, and if the fundamentals have not changed, then ordinary financially motivated investors in the market will consider the company to be trading at a discount, and over time buy the stock, returning it to its equilibrium share price (Folger and Nutt, 1975:159; Dowie, 1993). Of course, a short term depreciation in the share price, may well be uncomfortable for the directors.

However, while in theory ethical funds could inflict this discomfort, in practice, they have strong reasons not to do so. If an ethical fund sought to sell its holdings suddenly in a way that caused short term depreciation of the company's share price, the most significant financial casualty of the falling price would be the fund itself. In an illiquid market, the only way it would be able to sell its shares quickly would be to accept a lower price for them. This could cost the fund significant sums. If it made a routine practice of quick sales, this would undermine its financial performance. Consequently ethical funds have a strong financial incentive to find a way to sell their shares in such a way that *minimises* the downward pressure on the company's share price. Consequently, for example, Friends Provident Stewardship does not require its investment managers to sell the shares of companies which contravene its criteria immediately, but over a six month period - giving them a chance to minimise the effect on the fund's financial performance. A skilled fund manager will be able to divest himself of a particular stock over time without having any effect on the share price at all. The larger the share an ethical fund holds in the company, the more likely the fund is to be able to hurt the company's share price, but the stronger the financial pressure on the fund not to hurt the company's share price.

6.2.2 General avoidance

While ethical funds frequently sell the shares in companies on financial grounds, the general way in which their activity is regarded as being able to depreciate share prices, is through their general policy of avoidance. Friends Provident says that its 'acceptable list' of companies comprises some 40% of the stockmarket. Consequently it is staying out of the market for 60% of the shares on the stockmarket. Can an ethical policy of withdrawing from the market in the shares of 'unacceptable' companies have a downward effect on share prices? In fact the issues are similar to the above argument. The principal issue is the proportion of the total market represented by those funds. Ethical funds all together have £1.3bn of assets under management, one might add another £10bn of screened funds managed by churches and charities giving a total of around £11bn. This is approximately 0.5% of the total size of the stockmarket. Such a small percentage will have an unnoticeable effect on share prices. Any negligible short term impact will be negated by ordinary financially motivated investors comparing share prices to fundamentals. In fact this percentage is diluted further by the fact that ethical funds do not all have the same ethical screening criteria. While some funds might stay out of the market for brewery shares, others might participate in this market.

What if ethical funds grew much larger? What if, in a few years time, they comprise 5% of the total market? Such a level of avoidance may well affect the share prices of companies. But, for big companies with liquid markets for their shares, the effect would be short term and arbitraged away by ordinary financially motivated investors. However, in the case of small companies whose shares are traded in a relatively illiquid market, buyers are comparatively scarce, and it is possible that such effects may persist.

However it is unlikely that ethical funds will grow to such a significant percentage of the overall market in the foreseeable future. While the asset value of ethical funds cannot be expected to appreciate at a faster rate than the market as a whole, ethical funds may be able to attract new capital at a faster rate than the market as a whole. This, at least in theory, could allow them to grow to 5% of the market. In today's terms that represents £100bn. This is larger than the size of the whole unit trust industry in 1990. Even if ethical funds were amazingly successful at attracting new funds, it may be decades before they could command a 5% share of the market. At least not by attracting new investors alone.

One way in which they might be able to grow faster is if *pension funds* start to adopt ethical screening strategies in large numbers. Indeed Friends Provident asset management arm has signed up five local authority pension funds on contracts to manage a small proportion of their funds using a variant of the Stewardship model. If more local authority pension funds follow this route, and entrust more money to ethical management, the funds under ethical management could achieve a 5% threshold a little more quickly. However, there are still concerns that pension fund law does not allow pension funds to adopt ethical screening policies, on the grounds that pension fund trustees have the fiduciary duty to maximise the financial interests of their beneficiaries. But, recent legal cases have concluded that trustees may not pursue the financial interests of their beneficiaries in contradiction to their other direct interests. For example, the trustees of a cancer research charity could be in breach of their responsibilities if they invested in a tobacco manufacturer. But the beneficiaries of pension funds do not have such direct common interests across the range of issues pursued by ethical funds. While some pension fund members may be opposed to arms manufacture, the majority of them may not be. So it may be hard for trustees to adopt an ethical screen on armaments on the basis of beneficiaries' interests. The fact that ethical funds can argue that their performance is in fact better than average changes this case somewhat. If ethical funds perform well, they could be invested in on financial grounds, with the added ethical benefits arising incidentally. If an environmental investment policy produces greater long term returns as Nottinghamshire's local authority fund argued (at a 1996 United Nations Environment Programme conference on ethical investment and local authorities), then investing ethically may well be acceptable on *financial* grounds.

One factor that would come into play were ethical funds to become a truly mainstream activity is that the particular ethical exclusions currently used are unlikely to find widespread support.[6] For example, while a small minority of the British public might consider the manufacture of alcohol to be unethical, it is likely that the majority would not do so. Similarly, while a minority might oppose all manufacture of armaments, the majority may find it acceptable, subject to certain exclusions concerning particularly offensive weapons such a landmines, and trade with oppressive regimes. The larger ethical funds grow, the more diverse the ethical opinions held within them. This may dilute the effect of ethical funds. Indeed it may mean that different ethical funds are often on opposite sides of the same issue. Some funds might seek to support initiatives which protect the rights of gay people in the workplace, whilst others might avoid such companies. There are some issues on which it might be possible to build a broad based consensus. In particular one might consider environmental issues less likely to lead to opposing ethical funds than the more contentious ethical issues.

The strongest case that tends to be made for the impact of screening in the market place is the example of South Africa. At the height of the campaign against apartheid a very large number of investment institutions divested themselves of shares in companies involved in South Africa. As a result of this and more public shareholder and consumer campaigns, a large number of companies withdrew from South Africa. Subsequently, as the world knows, apartheid collapsed. This may appear to be an excellent example of how screening can work. However, it is very hard to establish the part screening played either in persuading companies to withdraw, or on the collapse of apartheid. It is possible for example, that the most powerful reasons why companies divested from South Africa, was because *consumers* boycotted companies, not investors. Without taking sides in this argument, it is possibly true that even if the South Africa investment boycott was effective, is a truly exceptional event in the history of ethical screening. No other screen has ever gained anything like the level of support that South Africa has.

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[6] This relates to the suggestion made in Chapter 5 that ethical funds currently have a rather narrow conception of the ethics of corporate practice, see p.123ff..

6.2.3 The Impact of positive selection

The attempt to use the market for a company's shares to influence its behaviour can work in both directions - seeking to hurt companies by avoiding their shares, and seeking to help them by preferentially buying their shares. There is considerable focus in the marketing literature of ethical funds on positive investment. Indeed, from its beginnings to the present, positive investment has been the publicly stated purpose of the Stewardship funds. The idea of supporting good companies does not offer a direct mechanism to persuade companies with poor ethical performance to adopt better practices. However, in theory it might be expected to make some contribution. If by proactively investing in exemplary companies ethical funds are able to put a premium on their share price, companies and their directors will be pleased, and will find it easier to raise further capital. In which case there will be an incentive for companies with poor ethical performance to meet the criteria which would make them eligible for such proactive investment. In practice there are several problems with this idea, many of which are similar to those facing the avoidance approach to market signalling.

The effect of ethical funds' positive criteria is to concentrate their investment in companies which, on their criteria, have above average ethical performance. Because of the small size of ethical funds this will not have any dramatic effect on the share prices of larger companies for the reasons offered above. However, again, in the case of small companies there may be some effect. A large ethical fund buying and holding a significant share in a small company on ethical grounds could raise the share price for that company. However, ordinary financially motivated investors in the market may, on the basis of fundamentals, then consider that share over-valued and so may sell it, taking a profit, and reducing the price of the stock to its equilibrium level. If the market for that share is illiquid, then it is possible that the premium might persist. One senior figure in the ethical investment industry believes that this is sometimes the case for some of the smaller companies in which the larger ethical funds invest. If this is correct then there will be some incentive available to smaller companies to make themselves acceptable to ethical funds.

There is some anecdotal evidence that some smaller companies go to some lengths to present themselves as attractive candidates for ethical funds. I discussed this issue with the financial director of a small company in the public transport sector. He said that he was very keen to persuade ethical funds to invest in his company, and he went to some lengths to persuade them that his company was ethically acceptable. However, while clearly the company considered it worth some effort to court ethical investors, it is doubtful how much the company in question actually changed its practices in order to make it acceptable to ethical funds. Indeed the company is known for its highly aggressive approach to competition.

One issue which limits the effectiveness of this possible premium effect is that it is only available to companies that already come reasonably close to meeting the criteria of ethical funds. A company with significant Ministry of Defence contracts is unlikely to receive significant investment from ethical funds unless it ceases these contracts. However the cost of doing so is likely to considerably outweigh the possible benefits to its share price from being attractive to ethical funds.

6.2.4 Other effects of the existence of ethical funds

We must conclude that for large companies, the effect of ethical funds on share prices is negligible. For smaller companies with illiquid markets for their shares its effect may be noticeable over the short term, but is likely to be eroded in the long term. Incentive effects arising from persistent premiums on smaller companies may have some effect, but they will be limited. An important point to consider is that most of the harm done by companies is done by large companies, companies whose share prices are unlikely to be hurt or helped by ethical funds' market activity. Consequently claims that market signalling can have a significant impact for changing corporate practice are implausible. Indeed this conclusion is accepted by many, but by no means all, practitioners of ethical investment.

While ethical funds might not be able to harness the market to put pressure on companies to improve, there are other indirect ways in which screening might have an impact. The screening process encourages disclosure, and raises awareness of issues; the existence of screened funds puts ethical issues on the investment agenda; ethical funds may educate markets on hidden performance issues, such as environmental liabilities.

6.2.4.1 Indirect consequences of screening

In the process of screening, companies are sent extensive questionnaires by EIRIS (and by a few other funds independently). These questionnaires encourage the disclosure of corporate activities beyond that required by law. Over the last few years the response rate to EIRIS questionnaires has been around 40%. If the process of filling in questionnaires does encourage higher levels of disclosure, there may be benefits. The more the public know about companies, the harder it will be for companies to conceal their wrong doing, and the more questions the public can ask of them. Furthermore the particular questions which EIRIS asks in the questionnaires reveal which issues ethical investors are concerned about, and companies can use this as an indicator of their ethical performance.

6.2.4.2 Sabotaging share issues

Dowie (1993) is generally sceptical about the long term impact of ethical funds using the market signalling. However, Dowie (1993) argues that the one way that ethical funds could hurt a company financially is by sabotaging share issues:

> ‘if enough irate stockholders suddenly dumped their shares on the market at once, they could temporarily drive down the prices of a stock and affect the amount a company was able to raise in a pending underwriting, the major mechanism by which external capital is actually injected into most public corporations.’ (Dowie, 1993:55)

Dowie is writing in an American context, but it is possible here, that ethical investors could sabotage rights issues in this way. However, as Dowie suggests, ethical funds have not used this tactic, and it would be extremely costly for them to do so for the reasons I have already outlined.

6.2.4.3 The effect of mere existence of ethical funds

The mere existence of a substantial ethical fund industry shows the financial community that there is reasonably substantial interest in ethical issues. A £1.3bn ethical retail investment business is harder to ignore than a few individuals and institutions who privately practice an ethical policy, which was the situation in the early eighties. Retail ethical funds put ethical issues into the minds of fund managers, financial advisors, the financial press, and ultimately investors, in a powerful and practical way. This undoubtedly has had an influence on the culture of the investment industry, and ultimately on corporate practice. However, given the fact that most funds do not take public positions on most issues, let alone actively seek to promote issues on the public agenda, this effect is considerably more limited than it might be. I return to this issue in Chapter 7.

6.2.4.4 Leading market opinion on benefits and liabilities

As regulatory regimes tighten on environmental issues, many companies may find themselves with very substantial liabilities, for example, for cleaning up land they polluted many years before. These liabilities may not be currently factored into analysts' estimates of the value of companies. This may also apply to ethical issues which can undermine a company's reputation. For example, Shell's activities in Ogoniland, and the Brent Spar episode may turn out to be a long term liability to its reputation, and to its business. Ethical and environmental funds are specialists at identifying such liabilities before they receive widespread attention. Ethical funds may therefore educate the market on these issues. If they can do this, they can possibly influence the assessment of fundamentals that I discussed earlier. This could affect share prices significantly. In discussion with ethical funds managers I found some anecdotal evidence that analysts do look to green funds for information in this way.

The other side of this coin is that ethical funds could offer a way of picking high performance companies. An important idea promoted by some in the ethical investment industry is that ethical business is good business; that companies with good ethical and environmental policies will perform better in the long term than those with poor policies. If this is turns out to be true, then ethical funds will not only be a good ethical bet, but they will also be a good financial bet. One new fund which is very committed to this line is the 'Tomorrow's Company Fund' mentioned in Chapter 2. This fund does not want to be considered an ethical fund, and yet the idea of 'Tomorrow's Company' is thoroughly ethical. Tomorrow's Company believes that companies should include their stakeholders in their core decision making, and that this is the way to more fulfilling and successful business (Tomorrow's Company, 1995). Studies done by Klienwort Benson before the fund was launched, based on retrospective performance of companies selected on Tomorrow's Company criteria, show that they outperformed the market significantly over an 10 year period. If ethical funds offer a way of picking winners, then they could considerably influence City opinion, and in so doing dramatically influence the assessment of the fundamentals of companies in a positive direction.

These side effects of ethical investment could in the long term be very important. However, they are currently rather accidental. A much more deliberate effort could be made by funds to heighten the awareness in the City of potential ethical and environmental liabilities and benefits. This, however, would require the kind of public adoption and explanation of ethical positions, which I will argue is important in Chapter 7.

6.3 The efficacy of active engagement

While direct use of market signalling is not likely to be a very effective means for ethical funds to influence corporate practice, they are not the only means available to such funds. The attraction of market signalling is that it offers a way of communicating with companies in a language that they understand. It also requires little extra effort on behalf of ethical funds. On this model, ethical funds, simply by screening their investments (which they do anyway in order to address the investment ethics problem) can signal to companies through their share prices which activities they consider to be undesirable, and which desirable. Unfortunately, as I have suggested, these signals are likely to be drowned in the general noise of the market. But sending signals through the market place is a rather indirect and haphazard way of communicating, so why not tell the companies directly what you consider to be unacceptable or desirable corporate practice? Several funds in the UK, and more in the US, have adopted this 'active engagement' approach.

In this section I will illustrate the effectiveness of this approach by discussing some initiatives in the US. I will then assess the achievement of UK funds. Broadly I argue that this approach has tended to be a marginal part of ethical investment in the UK. It is early days yet, and improvements are being made all the time, however, I argue that ethical funds could be substantially more effective than they currently are. I conclude by claiming that the engagement approach has largely been 'bolted on' as an extra to the screening approach, and that this greatly limits the potential for engagement to be an effective method for addressing the corporate harm problem.

6.3.1 Active engagement in the US

In the US, active engagement, or shareholder activism, has become a routine part of investment activity within certain sectors of the investment market. Since the early 1980s a wide coalition of 275 Protestant, Catholic, and Jewish institutional investors have been engaged in shareholder activism through the Interfaith Center on Corporate Responsibility (ICCR), directed by Tim Smith. The first church-sponsored shareholder resolution was filed by the Episcopal Church in 1971 with General Motors on their involvement in South Africa (Smith, T. 1992). Over the next 25 years church investors have placed many hundred resolutions at AGMs. In the 1980s they were also joined by many of the largest pension funds such as TIAA-CREF, and the pension funds of New York City and State and the state pension funds of California, Wisconsin and Minnesota (Smith, T. 1992:109). Some of these pension funds have tens of billions of dollars of assets. Institutional activism in the US is now supported by the Council of Institutional Investors, which in 1993 represented 80 institutional investors with $600bn in assets (Smith, M. 1996:231). One particularly important example is CalPERS (California Public Employees' Retirement System). Between 1988 and 1993, 36 firms were requested by CalPERS to make changes in their governance structure. CalPERS repeated these requests several times during this period, and by 1993, 72% of the firms had adopted the changes proposed by CalPERS, or made changes that satisfied CalPERS. (Smith, M. 1996: 228). CalPERS is the largest public pension fund in the US, and the second largest pension fund over all, with approaching $100bn in assets in 1995. It is widely seen as a leader amongst institutional activists (Smith, M. 1996:230).

CalPERS' activism has been focused on governance issues. Its motivation for pursuing governance reform is not simply ethical, but also self-interested. It aims to use shareholder activism to improve the long term value of the companies it invests in, by such changes as removing 'poison pill' devices, requiring confidential shareholder voting systems, preventing 'greenmail' payments, creating shareholder advisory committees, changing the composition of the board of directors, and restructuring executive compensation (Smith, M. 1996:231-232). CalPERS focuses its activism on companies with a high level of institutional ownership, and in which it is one of the largest shareholders. (Smith, M. 1996:231). Smith concludes that CalPERS has been successful at pursuing its goal of increased long term value.

'Overall, the evidence indicates that shareholder activism is largely successful in changing governance structure and, when successful, results in a statistically significant increase in shareholder wealth.' (Smith, M. 1996:251).

Smith estimates that the benefit of activism to CalPERS has been $19m over the 1987-93 period, and the cost $0.5m per year.

However, shareholder activism as a whole moves far beyond governance issues to a range of social and environmental issues. Indeed, over the last 15 years some 300 social and environmental resolutions have brought before company AGMs each year by institutional activists. In 1994, ICCR alone sponsored 202 social resolutions, on 138 companies. According to Tim Smith (1992), in the early 1970s social shareholder resolutions were considered successful if they achieved 3% of the vote, in the 1990s many social resolutions achieve between 10% and 25% votes, while governance votes have approached 50% approval. However, many social resolutions have been effective without actually being voted on at the AGM. In the 1980s between a quarter and one third of shareholder resolutions were withdrawn as a result of negotiated agreements with companies (Smith, T. 1992:109).

One recent example of effective ethical shareholder activism is the attempt to persuade the US's third-largest billboard company, 3M Media, a subsidiary of 3M, not to provide billboard advertising space to tobacco companies. Following a sustained campaign by ICCR, which involved the submission of four different shareholder resolutions in 1995, 3M has agreed to phase out tobacco advertising by the end of 1998 (Business Ethics Magazine, July/August 1996). However, perhaps the largest co-ordinated shareholder activist campaign in recent years has been the attempt to persuade companies to sign up to the CERES Principles.

6.3.2 The CERES Principles

In June 1988, the Social Investment Forum[7] held a meeting which decided that a long term priority of the social investment movement is the environment, but that little activism was occurring in this area (Bavaria, 1992:138). SIF consequently resolved to

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[7] The Social Investment Forum (SIF) is the trade body of ethical investment in the US. It is the inspiration for the UK Social Investment Forum referred to in Chapter 3.

set up a sub-group to pursue environmental objectives. This sub-group, which began meeting in 1989, came to be known as the Coalition for Environmentally Responsible Economies (CERES). The coalition included both representatives of the social investment community, and of various environmental pressure groups, such as the Sierra Club, the National Audubon Society, and the United Nations Environment Programme. The first task CERES set itself was to adopt 'a set of environmental principles for corporations that would serve as both a baseline for performance measurement and management standards' (Bavaria, 1992:139). The resulting Principles were launched in September 1989. In March of that year, the Exxon Valdez ran aground off the coast of Alaska, releasing more than 10m gallons of oil, and attracting the attention of the world's media. Consequently, these principles were initially known as the 'Valdez Principles'. As soon as the Principles were launched, CERES began to talk to companies. The Principles were sent by CERES to 3,000 companies, and the organisation began work on a guide to help companies understand the ideas behind CERES. The main CERES objective was to persuade companies to sign up to the Principles. To this end, in 1989 20 shareholder resolutions were filed by church investors working with ICCR, and also by CalPERS and the New York City Retirement System, to ask companies to disclose their compliance with the Principles. The resolutions received an average vote of 12.5%. (Bavaria, 1992:141). Between 1991 and 1994 an average of 40 resolutions a year were filed on the Principles (Hoffman, 1996:52). Each year some resolutions were withdrawn because the company concerned agreed to negotiate with CERES. By 1995, over 50 companies had endorsed the CERES principles, most of them companies with well known environmental concerns or commitments - such as Ben and Jerry's and the Body Shop. However, some very large companies have also been persuaded to sign, including General Motors, Sun Oil and Polaroid.

However, as Hoffman (1996) argues, CERES' effectiveness has not simply been confined to those organisations who have signed up to the principles. He describes the case of the Amoco Corporation as an example. In the early 1990s CERES repeatedly proposed resolutions that Amoco should adopt the Principles. In 1990 nine religious institutional investors wrote to Amoco suggesting filing a resolution on CERES for the AGM. Amoco negotiated with these investors, who subsequently withdrew their proposed resolution, and in return Amoco promised to publish an environmental progress report, which was a requirement of one of the CERES Principles (Hoffman, 1996:55). Subsequently, Amoco also set up a board-level environment, health and safety committee, another CERES requirement. It is not easy to say whether this came as a direct response to CERES pressure. As Hoffman says, Amoco executives are

> ‘cautious to grant the [CERES] organization that much credit. According to one senior EH&S [environment, health and safety] manager, CERES precipitated but did not create the idea of forming a board-level committee, the process had already begun.’ (1996:55).

While Amoco issued a number of statements stating its commitment to protecting the environment, according to Hoffman, the company was reluctant to adopt external principles, or make itself accountable to CERES, which was after all a self-appointed group (1996:56). The company therefore decided to adopt a proactive response, by seeking to redraft its environmental policy and develop its own ‘Amoco Principles’ on the environment. Hoffman argues that this meant a shift in the environmental policy from being compliance oriented to being proactive (1996:57). In subsequent years Amoco has gone on to work with a variety of other companies in the development of environmental reporting standards, in part, Hoffman argues, to avoid further pressure from CERES. This culminated in 1993 in the launching of the Public Environmental Reporting Initiative which was also supported by Dow, BP, Northern Telecom, Phillips, Polaroid and Rockwell.

While CERES may not have achieved the obvious goal of persuading a large proportion of corporate America to sign up to its Principles, this was never its only purpose. As Joan Bavaria, co-chair of CERES, says ‘What we’re after is culture change and forging relationships. Our goal is not to become an institution but to be part of the process.’ (Hoffman, 1996:60). It is likely that, albeit indirectly, CERES has had a significant effect on the culture of environmental practice of a wide range of large corporations in the US and Europe. While it was not solely responsible for changes in environmental policy, it served as an important catalyst. Hoffman claims that ‘CERES’s influence in the business environment cannot be disputed...the changing landscape of corporate environmentalism bears CERES’s mark. In consequence we can conclude that the large scale, long-term active engagement which CERES embodies can be a effective means of addressing the corporate harm problem.

6.3.3 Active engagement in the UK

The first thing to say about active engagement in the UK is that it is not widely pursued. There are few examples of shareholder activism on social or environmental issues by institutional investors, and there have been few organised attempts at activist campaigns. However, there are a number of relatively isolated examples of activism in the American style. In 1991, the South Yorkshire Pensions Authority, together with local authority pension funds from Derbyshire, Lancashire, Cleveland, Humberside and Lewisham, and one private sector fund, attempted to bring a resolution to the Fisons plc AGM, calling for the company to stop its peat extraction operations in ecologically sensitive areas. The coalition of funds was co-ordinated by PIRC (see Chapter 3). In fact it failed to meet the full requirements for resolution submission, but nevertheless, Stuart Bell of PIRC claims that 'The Fisons case shows it is practical to get companies to respond. In fact investors provided the only effective form of pressure in that case' (Sparkes, 1995:80). There have been a small number of other shareholder campaigns in the UK. For example, Yorkshire Water were eventually persuaded to appoint a director for consumer affairs. There has also been a decade long campaign on RTZ by Partizans (a single company/multiple issue pressure group) on a variety of ethical and environmental issues. This was joined recently by a campaign by Friends of the Earth to persuade RTZ to stop the ilmenite mining development in the Fort Dauphin region of southern Madagascar, because it would severely damage unique littoral forests, and reduce biodiversity. Another example is Greenpeace's attempt to persuade prospective investors in European Vinyls Corporation, a leading manufacturer of PVCs, that the official floatation prospectus did not adequately address the threat to the environment from PVCs, or the potential threat to profits of future environmental legislation to control them. Perhaps the most well known shareholder campaign in the UK was in response to the pay policy of British Gas. When Cedric Brown, Chief Executive of British Gas was awarded a 75% pay rise, many people were incensed. Professor Joe Lamb, a small British Gas shareholder, decided to do something about it. He launched a campaign to change the company's pay policy. By the annual general meeting, he had won the support of 800 other British Gas shareholders, and had tabled a resolution for consideration at the AGM. His resolution was joined by another one from PIRC. The AGM was attended by a record 7,000 shareholders. The PIRC resolution received 20% of the vote. While not enough to force British Gas to change, it was a watershed for a

British shareholder action campaign to secure a support from one fifth of the shareholders in one of Britain's biggest companies.

However, while one or two of the ethical funds have been involved in various ways in these campaigns, most ethical funds do not pursue any kind of engagement with the companies in which they invest. Most ethical funds do talk to companies and have meetings with them. But it is routine for most fund managers (whether ethical or non-ethical) to research companies and meet with them. It is likely that for the majority of ethical funds in the UK, engagement is limited to questions from the fund asking for clarification on company policy, and informing the company of the fund's ethical policy. This activity is unlikely to do much to persuade companies to change their policies. However, I noted in Chapter 4, that three ethical fund managers in the UK do have policies of engaging with companies in order to persuade them to change their policy, namely Friends Provident Stewardship, NPI Global Care, and Jupiter Ecology. Friends Provident Stewardship has over £700m of funds under management. Jupiter Ecology and NPI Global Care have over £100m between them, so these funds account for perhaps 70% of the ethical fund market. These funds have used a number of different procedures to pursue engagement, including writing letters, holding meetings with managers, doing sector surveys and feeding back the results to management, engaging in formal shareholder action at company AGMs, as well as attempting to lead policy in more general ways, by writing articles, briefing the press, giving addresses at conferences, participating in industry wide initiatives.

NPI and Jupiter also carry out sector surveys. One purpose of these surveys is to develop a more detailed understanding of the particular sector, and of the particular issues that operate in that sector. EIRIS criteria tend not to be sector-specific and set absolute standards for, say, pollution across industry as a whole. This is useful for screening purposes, however, it means that the environmental impact of supermarkets is compared with that of chemical companies using the same basis of measurement. Such criteria do not provide a sensible starting point for persuading companies in either industry to improve their practices. However, a sector survey can reveal they key ethical and environmental issues in a particular industry, the current benchmarks and best practice standards operating in the industry, and the individual performance of companies with respect to these ethical and environmental issues and best practice standards. Tessa

Tennant, head of research at the NPI Global Care Fund, believes that this process is extremely important to her fund's constructive dialogue with companies.

> 'We actually want to talk to management, we want to do the sort of analysis that will get industries and companies to take these issues more seriously. [This requires] building our internal research capability...to extend the scope of our dialogue with companies and to open the process up more and more over time. Dialogue without serious homework beforehand is just a waste of time. I mean you'll get fleeced, because companies know their business better than anybody else, so unless you have done a lot of homework you can get caught out very quickly.'[8]

The sector research approach provides a much better informed basis on which to engage with the company than a generalist criteria based approach alone. It measures companies against the standards achieved by their direct competitors, and against the best achievements in their industry. Companies can be told where in particular they are failing in relation to typical industry standards, and in which areas they can do most to improve. If the sector surveys are rigorous, they can provide an authoritative basis for engagement. NPI Global Care, for example, is prepared to back companies which they believe offer examples of best practice in a difficult industry sector.

In addition to these methods of engagement, one fund, NPI Global Care aims to take a leadership role on ethical and environmental issues in corporate practice. To this end, staff from NPI regularly make presentations at conferences, and lend their support to particular initiatives - for example, Tessa Tennant is chair of the UN Environment Programme working group on insurance and the environment. NPI has also recently launched a new fund which explicitly changes the ethical focus from screening to engagement. The NPI Global Care Income Fund retains certain screens on tobacco, arms, and nuclear power, but it also seeks to derive its ethical credentials from its commitment to engagement.

6.3.4 The modest achievements of engagement in the UK

The activities I have described are only practised by a small number of ethical funds. Most ethical funds engage with companies no more actively on ethical issues than ordinary non-ethical funds do. As we saw in the previous section, this does not mean

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[8] Interview with the author.

that such funds make no contribution to addressing the corporate harm problem - their very existence makes a contribution in itself. But how effective are the methods used by the funds that *do* practice engagement at addressing the corporate harm problem?

I have asked the funds that do practice engagement for examples of companies which they have persuaded to change their policies. Unfortunately the funds are not able to produce such lists. However, all of these funds were certain that their efforts at engagement were effective at persuading companies to rethink certain issues. There are a number of reasons for this apparent discrepancy between what the funds believe they achieve, and what they can prove they have achieved.

One reason for this is a problem of measurement. While it might be easy to tell if the market signalling approach is working by seeing if the share price moves up or down, there is no such objective, and single reference point with which measure the effectiveness of active engagement. Ideally, in order to prove engagement is effective as a means of persuasion we need to know that a company has changed its policy in the way recommend by the ethical fund, and that it did so at least partly because the ethical fund persuaded it to do so. This ideal situation rarely applies. Some attempts to change corporate practice have a clear fixed goal whose achievement can be easily measured. For example, in the 1980s the Campaign for Lead Free Air (CLEAR) undertook a campaign with the simple objective of persuading the government to phase out leaded petrol (Wilson, 1984). In January 1982 when the campaign was launched, the UK government claimed that the addition of lead to petrol was not harmful, and opposed any phase out. Less than 2 years after the campaign started, the principal objective had been realised: the government had been persuaded to change its mind. This is a clear measurable success. Ethical funds have not tended to adopt such clear measurable goals. They are not single issue campaigning groups, but deal with companies across a broad range of issues. This diffuses the effect of ethical funds. Consequently, it is rather hard for them to offer clear examples of situations in which they have had an impact.

Another problem is that companies may not want the world to know that they have changed their policy as a result of the intervention of an ethical fund. If they do make a change, it is easy to see that they would want to take all the credit for themselves, and not give the impression that they have been forced into it by outsiders.

It is not unreasonable to accept the claims of those who practice engagement within ethical funds that they have had some effect on companies. However, these practitioners would also accept that their contribution has been rather modest, particularly compared to the success of shareholder activists in the US. In the next chapter I shall discuss some reasons for this modesty. However, here I shall discuss just one claim that is made for the modesty of achievement in the UK.

One reason for this modest achievement is the possibility that the hopes of the ethical investment movement are misconceived, and that investors, in reality have negligible power to address the corporate harm problem. One might argue that minority shareholders have very little power within companies for the following reasons: because they have insufficient access to corporate information; because company law inhibits all but the most determined activism; and because the bulk of shareholders care little about environmental and ethical agendas and cast their votes, routinely, in support of the company board (see Mackenzie, 1993). This gloomy picture has some truth, and there is no question that much could be sensibly done to improve the self-regulatory systems that make management accountable to shareholders in companies. It is probably true that the achievements of active engagement in the US have been facilitated by a more amenable regulatory regime. For example, the UK regime typically requires that resolutions can only be submitted for voting at the AGM if they are supported by at least either 100 shareholders with an average of £100 of stock, or shareholders with 5% of the voting shares of the company (Walmsley, 1990). In the US, that requirement is a holding of $1,000 or 1% of the shares for one year. (United Shareholders Association, 1990). Another reason for the higher levels of resolutions in the US compared to the UK, offered by Stuart Bell of PIRC, is that UK companies are much more accessible to their investors than their US counterparts. It is relatively easy for a shareholder in a UK company to get a response to a request, and even to have a meeting. However, not long ago, even the largest US pension funds found it hard to get adequate response from companies. In the US, the proxy resolution has been one of the only ways to force a company into dialogue. In the UK dialogue can happen without the need to make use of resolutions. If this is true, then the more responsive corporate culture in the UK offers the possibility of even more opportunity for the engagement approach to work than in the US. It would therefore be a mistake to suggest that differences in company law are the only reasons for the comparative ineffectiveness of ethical funds at engagement.

Investor activism in the US is more concerted, more strategic, and better resourced than it has been in the UK. I would therefore suggest that ethical funds, even under existing UK legislation, have it in their power to be considerably more effective at addressing the corporate harm problem than they are now. If they adopted a plan of concerted, clearly thought out, targeted, adequately resourced engagement activity, they may be able to achieve a considerable amount.

In conclusion, the US record of achievement at addressing the corporate harm problem using active engagement is long and impressive, though only a small proportion of the clearest achievements have come from ethical mutual funds. Ethical funds in the UK do not have such a lengthy track record. One reason for this is that most ethical funds limit their ethical activity to screening, and do not have a policy of engagement. For those few funds that have a policy of engagement early signs are promising.

6.4 Conclusion

In this chapter, I have argued that we can only have modest expectations for the market signalling approach to addressing the corporate harm problem, particularly for large companies. I have argued that, on the other hand, engagement is a promising approach to the corporate harm problem. I have argued, however, that it is not widely practised by UK ethical funds, and where it is practised, it frequently comes second to the screening approach. This is not necessarily a criticism. Screening is an important goal of ethical investment. As we saw in Chapter 5, it is a considerable achievement to offer a service which allows 150,000 investors to invest in a way which is compatible with their ethical convictions. However, if my arguments are correct, then those ethical funds which do not practice the engagement approach can claim only a rather modest achievement at addressing the corporate harm problem. Those funds that do practice engagement can claim greater success, but could, I will argue, do considerably more. If I am right that the corporate harm problem is one of the primary goods pursued by ethical investment, this is a serious challenge for ethical funds. In the final two chapters, I will explore some to the way in which ethical funds can become better at addressing the corporate harm problem.

7. The place of deliberation in ethical funds

7.1 Introduction

This chapter offers an assessment of the extent to which ethical funds deliberate on corporate ethical and environmental practice, and the nature of these deliberations. Anderson et al. (1996) have made strong criticisms of the quality of ethical thinking in ethical investment. In this chapter I will assess these criticisms. But there are other more important reasons why we should consider this topic. Firstly, adequate deliberation is an important part of deciding what is ethical and unethical about corporate practice. Establishing positions on the ethics of corporate practice is a vital first step towards addressing the corporate harm and investment ethics problems. Secondly, deliberation is important if one is to produce the persuasive ethical arguments which are needed to engage effectively with companies in order to convince them to change. As we concluded in Chapter 6, such engagement is the most promising means by which ethical funds may address the corporate harm problem. Finally, and more controversially, ethical deliberation is important if ethical funds are to contribute to the development of wider traditions of ethical thinking about business practice that are current in our society. This point draws strongly on the arguments made in Chapter 1 about the particular 'interpretive' approach to business ethics I am taking in this thesis. I will shortly consider these points in more detail, but first, I ought to be a little clearer about what I mean by deliberation.

7.1.1 What does deliberation involve?

There are many ways in which ethical deliberation can be undertaken. One way is to start with a founding principle, or theory, and argue how it should be applied to practical problems. For example, in Chapter 1 we discussed the possibility of using philosophical ethical theories as the basis for ethical criticism of ethical investment. Alternatively one might begin with the teachings of a particular religion, the doctrines of a church, or the dogma of an ideology. Another approach is to start with one's common sense intuitions about what is ethical, and build ethical arguments from them. A more reflective approach, which is in some ways similar to arguing from intuitions, which I also discussed in Chapter 1, is to build ethical arguments from the 'shared understandings' (Walzer, 1983), or 'traditions' (MacIntyre, 1984) of ethical thinking of a particular community. In the case of ethical investment, the relevant traditions might for example, be those of the wider business community, those of business ethics, or more appropriately those of the particular religious or political communities which have been involved in the foundation and development of ethical investment. My discussion in Chapter 1 indicates my preference for this third approach. However, I do not want my arguments in this chapter to require acceptance of this particular approach to ethics. I want to suggest that the common denominator that runs through these approaches to ethical deliberation is the use of *argument*. In each of these approaches to ethics, a reasonable ethical decision will require some sensible procedure of deliberation which involves the making of arguments, the assessment of claims, and the weighing of evidence. I wish to adopt this common denominator as the minimal standard by which to consider ethical investment to be ethical. This standard is a procedural one. It says that in order to pursue ethical investment it is important not simply to assert that a particular corporate practice is harmful, or unethical, but to be able to make a claim that the practice is unethical based on sound, well-grounded arguments of some kind.

What counts as a sound argument? Such a question is partly answered in the significant literature on practical reasoning which has emerged in the last few decades (for example Beardsley 1950; Toulmin, 1958; Geach, 1976; Scriven, 1976; Toulmin et al. 1979; Fisher, 1988; Booth et al. 1995). These works are a good place to start. If we take Toulmin's approach, good argument consists of the making of claims, the supporting of claims with data or evidence, and the supporting of evidence with 'warrants' (1958:97). For example[1]:

A: 'It must have rained last night'. (Claim)

B: 'How do you know?'

A: 'Because the streets are wet.' (Evidence)

B: 'Why does that tell us anything?

A: 'Whenever we see the evidence of wet streets in the morning, we can conclude that it probably rained the night before'. (Warrant).

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[1] This example is based on one offered by Booth, et al. (1995).

A warrant, then, is a general justification that the evidence offers appropriate support to the claim. Typically arguments are not so simple. Claims require a network of supporting sub-claims which will be backed up by further evidence, and further warrants. There are also important general features of what constitutes a good claim, for example, that it is substantive, contestable and explicit; and that the evidence offered is reliable, which as Booth et al. (1995) argue means that it should be 'accurate, precise, sufficient, representative, authoritative, and perspicuous.' (1995:97). For my present purposes, it is not important for me to establish in detail what is required for good ethical argument, only that some deliberation is an important requirement for ethical investment. This I will now try to establish.

7.1.2 Why should ethical funds deliberate?

1. I claimed in Chapter 5 that the 'support' conception of the investment ethics problem that if a company's activities are unethical, then it may be unethical to invest in it. If, as I have argued, a key goal of ethical investment is to solve the investment ethics problem, then an important initial requirement is to establish what kinds of corporate practice are unethical, and consequently which companies it is unethical to invest in. The corporate harm problem is that companies are acting in ways that are harmful or unethical. If one wishes to address this problem, then it is important to have a clear conception about what is harmful, or unethical, about corporate practice, and why it is harmful or unethical. While, as I indicated in the previous section, there are many ways to go about establishing what is unethical about corporate practice, it is important to engage in ethical deliberation of some kind. Of course one can simply make decisions about what is unethical about corporate practice based on one's intuitions, or gut feelings without any reflection at all. However, few would argue that decisions made on gut feelings alone are better than those made with the aid of *both* intuition and deliberation.

2. A second reason why ethical funds needs to deliberate is that if one wishes to engage with companies in order to persuade them to change their policies, one important requirement is the ability to offer good arguments for them to change. One kind of argument that might be offered is an ethical one which says that a certain practice of a particular company is unethical and ought to be changed. Of course companies may not accept the argument that the practice is unethical, but that does not invalidate the attempt to make an ethical argument. Indeed failure to convince the company on the first attempt may call for further, more persuasive, ethical arguments. It is also possible that while companies accept that certain of their practices may be widely considered unethical, they do not accept that they 'ought' to do something about it. If they adopt Friedman's position on the responsibility of companies is limited to the pursuit of profit. However, even in this case, one might see the occasion for further ethical arguments, for example, about why Friedman's approach may be wrong. At the end of the day ethical arguments might not prove effective, and other kinds of argument might be necessary, or even the abandonment of argument for less polite strategies such as launching press campaigns etc. However, it is hard to see that an ethical argument should not have some part to play in the attempt by an *ethical* fund to persuade companies to change.

3. Finally, deliberation by ethical funds may have an important public function as well. As I indicated in Chapter 1, the interpretive approach taken by ethical theorists like MacIntrye, Walzer and others sees ethics as partly a matter of the shared understandings and the evolving traditions of communities. So the ethics of corporate practice depends on the shared understandings and evolving traditions of the business community, and the society in which business operates. Sorell and Hendry's conception of the 'moral climate' or 'climate of expectations' (1994:6) may be another way of talking about at least some of these shared understandings. Ethical investment could have a role in contributing to the modification and shaping of these understandings in the future. If we can imagine the corporate community as a whole as being part of a tradition of thought and practice, then ethical investment might be considered as a new kind of argumentative contribution to the evolving traditions of ethical business thinking. Ethical funds are certainly a rather novel voice in this argument. Ethical funds can - and to some extent already do - make a contribution to the constitutive arguments of the traditions of corporate practice, simply be being there: by refusing to invest in certain companies, getting written about in the press, and occasionally talking to managers. However, it is possible that this contribution could be substantially more significant and constructive if their contribution did not arise simply from their presence, but from their willingness to promote intelligent argument about corporate ethical practice in the public sphere. Many aspects of the traditions and shared understandings about the ethics of corporate practice are very much open to debate both among business managers, and amongst the public at large. On many issues what is right or wrong for a company to do is very unsettled in the public mind. Unfortunately, much of what passes for 'debate' about corporate practice, are public campaigns and counter-campaigns between single issue pressure groups and corporate PR departments. The Greenpeace vs Shell confrontation over Brent Spar is a good example. Certainly these confrontations put important issues on the public agenda, but they tend to fall some way short of the sophisticated moral debates that are required for an intelligent resolution to these difficult issues.[2] Ethical funds, by seeking to make intelligent arguments, could contribute much to raising the quality of debate.

7.1.3 Criticisms of the ethics of ethical funds

Now that I have argued that deliberation and argument are important to ethical investment, I will consider the nature and degree of deliberation actually performed by ethical funds. Initially I will do this by assessing the merits of one of the most substantial critiques of ethical investment to have appeared to date. In 1996, a report was published by the Social Affairs Unit, entitled *What has "Ethical Investment" to do with Ethics?* (Anderson, et al. 1996). The report is strongly critical of current ethical investment practice in the UK. It claims that ethical investment is 'not very good ethics.' Indeed the authors of the report claim that ethical investment does not even deserve the title 'ethical' (Anderson, et al. 1996:4). There are various reasons given for these charges. Anderson and his colleagues claim that ethical investment represents an 'aggressively simplistic' approach to ethics, it makes 'crude distinctions' and is ethically 'incoherent'; that it 'pre-empts moral debate', fails to encourage 'refined ethical judgement,' and 'subverts moral education' (Anderson, et al. 1996).

If these criticisms are right, then it would seem hard to claim that ethical funds can possibly engage in adequate deliberation. In this section I will consider two kinds of criticism that Anderson and his colleagues make. Firstly that ethical investment has little to do with ethics - we can call this the 'no ethics' argument. Secondly that the quality of deliberation used by ethical investment is poor. The Social Affairs Unit report claims that 'ethical funds reach moral conclusions without doing adequate moral analysis' (Anderson, et al. 1996:14). We can call this the 'weak analysis' argument. Each of these

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[2] It is worth emphasising that my discussion of the interpretive approach to ethics in this section is slightly different to that introduced in Chapter 1. There the shared understandings I referred to were mainly the shared understandings and traditions of the ethical investment community, here I am referring to the much wider community of corporate business as a whole.

criticisms, if true, indicates significant problems with the ability of ethical funds to address the investment ethics and corporate harm problems.

While I find fault with both of these arguments, my conclusion in this chapter will be that only a few funds engage in any significant deliberation at all, and those that do face considerable challenges if they are to aspire to the demanding standards set in the preceding paragraphs.

7.2 The 'no ethics' argument

In the introductory section of the Social Affairs Unit report, Digby Anderson asks the rhetorical question 'What has ethical investment to do with ethics?' The answer he gives is 'Not much' (Anderson, et al. 1996:4). In this section I examine the grounds for saying that ethical investment has little to do with ethics. If it has little to do with ethics, then it certainly cannot have the solid basis of ethical deliberation, which I have argued is necessary. One reason why Anderson and his colleagues do not regard ethical investment as having much to do with ethics seems to be that they consider ethical criteria to be chosen by funds, not on ethical grounds, but in order to satisfy the demands of investors. They suggest that ethical investment might be better known as 'investment reflecting investor's opinions' (Anderson, et al. 1996:4). There are good reasons for Anderson and his colleagues to think this. One important goal of ethical funds *is* to reflect investor concerns, and if they did not, they would not have a market. And there are indeed some 'investor-led' funds which do in fact choose their criteria on the basis of investor concerns and not ethical deliberation. However, Anderson and his colleagues seem to claim that *all* ethical funds have 'not much' to do with ethics. There are two kinds of objection to this. The major objection is that there are many ethical funds which choose their criteria on the basis of considerable deliberation, and so have 'much' to do with ethics. The minor objection is that even in the case of investor-led funds there are circumstances under which it is reasonable to consider that investment is undertaken on the basis of ethical deliberation.

7.2.1 The distinction between investor-led and deliberative funds

The first thing I must do to defend these objections is to establish the distinction between investor-led and deliberative funds. Investor-led funds choose their criteria on the basis of market research, in discussion with ethical IFAs, and on the basis of letters from unit holders. Once they have established what investors are concerned about, they choose criteria from EIRIS which they believe will fit these concerns. However, the decision to adopt the criteria is not based on ethical deliberation by the fund manager, it is a decision about what will reflect peoples' concerns. For example, if people are concerned about animal testing, the fund manager may adopt a set of criteria which prohibit investment in companies that undertake animal testing. This decision is based, not on an ethical argument about what is wrong with animal testing, but on the simple fact that people are concerned about the issue.

Friends Provident Stewardship, on the other hand, is a clear example of a deliberative fund. It has chosen its ethical criteria on the basis of lengthy deliberation by its Committee of Reference over a period of 12 years. While the Committee is attentive to the concerns of unit holders, and expects its conclusions to be acceptable to them, Stewardship criteria are chosen on the basis of deliberation, and not on the basis of market research. In addition, Stewardship does not apply its criteria in a purely mechanical way, the Committee attempts to weigh up the positive and negative aspects of each company (see p.104ff.).

It should be noted that it is hard to draw a sharp divide between investor-led and deliberative funds because there are many funds which fall in between. For example there are many funds which have advisory committees which engage in some deliberation about the choice of criteria, and have responsibilities for the oversight of the fund, but do not engage in the lengthy deliberation that Stewardship, for example, does. While it is hard to draw line between the two kinds of fund, the distinction can still do valuable work. It is particularly important when considering the Anderson and his colleagues' 'no ethics' argument. It is unfortunate therefore that the Social Affairs Unit report appears to miss this distinction, and treats ethical funds as if they are all alike.[3]

In order to assess whether Anderson is right in claiming that ethical investment has 'not much' (Anderson, et al. 1996:4) to do with ethics, we need to know what satisfactory standard to use to decide whether ethical investment has enough to do with ethics to deserve the term 'ethical'. Anderson and his colleagues do not explicitly offer such a

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[3] I offer a more detailed account of the failure of the Social Affairs Unit report to pay sufficient attention to this issue below, see p.171.

standard. However, from many of the specific criticisms in the report, I think it is reasonable to claim that one standard which is important for Anderson and his colleagues, is the procedural standard I adopted above, which says that the use of argument is important to the making of ethical claims. This procedural standard will be the standard I use as a minimal measure for evaluating objections to Anderson and his colleagues' 'no ethics' argument.

On this basis, we can make swift work of objecting to Anderson and his colleagues' 'no ethics' criticism for deliberative funds. By definition these funds engage in ethical deliberation, and I think I have shown in Chapter 4 that the level of deliberation in Stewardship is at least sufficient to pass the minimal procedural standard of being regarded as ethical. However, this argument might be too swift for some, so I return to it below on p.171.

7.2.2 Investor-led funds and ethical deliberation

The job of deciding whether Anderson and his colleagues' 'no ethics' criticism applies to the investor-led funds is a lengthier task. Investor-led funds do seem to be just what Anderson has in mind when he says ethical investment should stop using the term 'ethical' and would be 'more accurately labelled "investments reflecting investors' opinions"' (Anderson, et al. 1996:4). Investor-led funds do not offer criteria on the basis of their own ethical deliberations. For example, an investment criterion which commits the fund to avoiding investment in companies which manufacture armaments is not adopted because anyone within the fund has, on the basis of deliberation, come to the ethical judgement that investment in arms companies is wrong. Instead the adoption of an ethical investment criterion is based on such things as research into what potential ethical investors are concerned about, what ethical IFAs think their clients are worried about, and what seems to be demanded in the market place. On the basis of this concern, these funds offer an effective positively and negatively screened investment vehicle. They do not, and generally do not claim to, offer anything more.

The absence of detailed moral deliberation may be seen by some financial institutions as a virtue, because it makes such investor-led ethical funds relatively simple to run, and avoids the demanding and costly necessity of establishing procedures for adequate ethical deliberation. However, this economy, on the face of it, would seem to make ethical funds vulnerable to criticisms like those made by the Anderson and his colleagues. From the point of view of the procedural standard of ethics I have adopted, a set of criteria is no substitute for ethical argument. An investment criterion, for example, ‘We will not invest in companies that manufacture armaments’, is not a moral position. It does not say what is unethical about manufacturing armaments, or even that manufacturing armaments is wrong. If investor-led funds do not engage in deliberation, are Anderson and his colleagues right in their ‘no ethics’ criticism?

7.2.3 Investor deliberation

Actually, the fact that investor-led ethical funds do not undertake ethical deliberation, does not yet prove that ethical investment using investor-led funds is not ethical in a procedural sense. The principal reason why investor-led funds might still reasonably claim to be ethical is that the funds may be invested in on the basis of ethical undertaken *by the investors.* On this model, ethical investors deliberate to decide their ethical positions, they then choose an ethical fund with criteria which are consistent with these principles. Anderson and his colleagues seem to believe that the only way in which an ethical fund can offer investment deserving of the term ethical is for it to undertake ethical deliberation itself. This does not need to be the case. An investor who, after much deliberation, becomes convinced of an argument which says that investing in arms companies is unethical, may choose an investor-led fund which avoids such investment. If this investor’s argument for rejecting investment in arms companies is sound, then it is hard to see how such a case could be ruled out as not having much to do with ethics. If the assets invested with an investor-led fund are invested on the basis of sound arguments accepted by the kind of ‘expert ethical investors’ discussed in Chapter 5, then the fund has enabled investment to take place which is adequate in a procedural sense, even though it has not itself engaged in deliberation.

7.2.4 Insufficiently reflective investors

However, there is an important qualification to this line of argument. What if investors do not engage in adequate ethical deliberation when choosing ethical funds? What if they invest instead on the basis of a vague set of anxieties about the ethics of corporate practice? What if they are confused and look to the ethical funds to engage in ethical deliberation on their behalf? If investors generally do not adopt ethical positions on the basis of sound arguments, then there is problem for investor-led funds. Under these circumstances, at no stage in the investment process is the ethics of corporate practice adequately considered. What happens instead is a hall of mirrors effect. An investor-led fund chooses ethical criteria in order to reflect the issues investors are worried about; investors, on the other hand, are indeed worried about these issues, and so choose to invest in the fund because it reflects their concerns. There is nothing terribly wrong with this in itself. However, at no stage in the process are arguments about the ethics of corporate practice made or defended, and so *under these circumstances* investor-led funds are not offering *ethical* investment in the procedural sense I have identified.

This claim only applies to circumstances when insufficiently reflective ethical investors invest in an investor-led fund. If such circumstances are unlikely to arise, or only arise in a small number of cases, then the problem can be ignored. However, it is at least a possibility that many investors do not engage in detailed deliberation on the ethical issues concerning corporate practice. While investors clearly have concerns about issues like the arms trade, environmental pollution and animal testing, and they may feel that companies engaged in these activities are acting unethically, it is another thing altogether to assemble sound ethical arguments to defend such convictions. The failure to have engaged in the difficult work of constructing sound arguments, in the face of the huge complexities of corporate practice, is not a moral failing on behalf of investors. But for ethical investors to be considered the source of moral deliberation to underwrite the ethical claims of investor-led funds, ‘concern’ is not enough. Without any moral deliberation to decide the merits of each issue, concern alone does not get us very far. Mere concern about a particular activity, does not make that activity wrong. For example, someone might be concerned about animal testing, but that does not mean that all animal testing is wrong, or even that that individual would, after lengthy deliberation, consider that all animal testing is wrong.

If the circumstances I have outlined are common in investor-led funds, then for these funds at least Anderson and his colleagues may be right in their charge that the use of the term ‘ethical’ is perhaps inappropriate. In these circumstances ethical investment does not pass the procedural test that I set out at the beginning of this section. Anderson and his colleagues’ charge that ethical investment is merely investment for ‘fashionable causes’ (1996:4) would also not be unreasonable for such investment, because finding fashionable causes, or popular concerns, is the intentional outcome of the market research approach. (Though, the fact that a cause is fashionable does not make it wrong.)

7.2.5 Alternative ethical measures

The fact that under certain circumstances investor-led funds might not be ethical in a procedural sense does not, however, mean that this kind of investment is either unethical, or ethically inferior to ordinary unscreened investment. Indeed the ethics of an action does not have to be measured by the procedural standard I adopted. Something can be ethical because it is based on good intentions. The intentions of the investors are no less good for the fact that they are, in some cases at least, not supplemented by lengthy and difficult ethical arguments. Of course, good intentions are not always enough for us to judge an action to be ethical.

Another way we judge an action to be ethical is if it has good consequences. The fact that many investors may not have thought things through with sufficient detail does not take away from the fact that their money goes to swell the size of the money invested in ethical funds, and in as much as the existence of ethical investment is good, then their investment has a good consequence. Though, ultimately, the kind of good consequence that is important here, is a reduction in the corporate harm problem. As we saw in the previous chapter, ethical investment as currently practised is unlikely to lead substantially to this consequence in the foreseeable future.

Another thing to be said in defence of investor-led funds is that their criteria, while chosen on the basis of market research, are selected from a list of criteria supplied by EIRIS. While EIRIS itself does not offer advice on ethical issues, many of its criteria are developed with funds which do engage in ethical deliberation. This means that many of the criteria that investor-led funds choose on the basis of market research, are chosen elsewhere on the basis of ethical arguments. In such cases, investor-led funds can at least claim that their criteria are not inconsistent with ethical argument.

7.2.6 Conclusion

The fact that in some circumstances ethical investment by investor-led funds takes place in the absence of ethical deliberation does not necessarily lead to the conclusion that these funds are not ethical. If ethical investors are doing their own ethical thinking, then investor-led ethical investment can reasonably claim to be ethical. However, if ethical investment is to adopt reliable ethical positions concerning corporate practice, if it is to be an effective means for persuading companies to adopt higher standards, and if it is to contribute argumentatively to wider public traditions of thinking about corporate practice, then investor-led funds are not in a very good position. They can, for example, tell companies what their investment criteria are, but they cannot offer considered arguments that say in detail on any particular ethical issue what the company is doing wrong, and how it should put it right. As it happens, few investor-led funds attempt to engage in persuasion with companies. Investor-led funds, by and large are among the group which do not adopt the engagement strategy (see p.111ff.). However, while we must conclude that from this point of view there are considerable limitations to the investor-led approach, many of the largest, most well known ethical funds are deliberative, not investor-led, and so escape this particular criticism.

7.3 The weak analysis argument

While deliberative funds may escape the starkest criticisms of Anderson and his colleagues, some of their other criticisms come closer to the mark. In addition to the general claim that ethical investment does not deserve the name ‘ethical’, the Social Affairs Unit report makes a number of more detailed claims that suggest that ethical funds are making judgements on the basis of inadequate ethical analysis, and that this has unhelpful consequences such as the pre-emption of ethical debate. This section examines the grounds for this charge. As I have already accepted, investor-led funds do not engage in ethical deliberation, and so can rightly be criticised for ‘weak’ analysis.[4] Deliberative funds do engage in deliberation, so this section will focus on the adequacy of analysis used by this group of funds.

Anderson and his colleagues argue that ‘Investing ethically is not a straightforward matter. The issues involved are often disputed, and almost always complex.’ (1996:20), that ‘moral choices involve balance and judgement’ (1996:20), and that they require complex moral arguments to find their proper resolution (1996:14). They do not believe

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[4] It is important to emphasise that while the investor-led funds’ capacity for ethical analysis might be regarded as weak, this does not undermine such funds’ claim to be rigorous in their application of ethical criteria to investment.

that ethical investment comes close to providing these things. Instead they claim that it 'gives a heroes and villains picture of the economic world with some investment portrayed as ethical and others portrayed as not.' (1996:20), that it makes 'crude distinctions' (1996:4), and that it disregards 'difficulties and counter-arguments' (1996:20). The report concludes: 'The overall objection to ethical investment codes is their aggressive simplicity. It is a simplicity which ill fits them for ethical work' (1996:20). Furthermore they argue that the effect of this simplicity is to 'pre-empt,' 'short-circuit,' 'subvert' and otherwise discourage complex moral argument, or the development of sophisticated ethical sensibilities.

7.3.1 The misconception of the Social Affairs Unit

One important objection to the criticisms made by Anderson and his colleagues is that they appear to have made their judgements about the ethical sophistication of ethical funds solely on the basis of the funds' marketing material. The only detailed evidence Anderson and his colleagues offer in support of their claims is contained in a lengthy set of appendices which quote verbatim from the investment policies of ethical funds, published in their marketing material. Many of the criticisms levelled at ethical funds by Anderson and his colleagues seem to treat these lists of criteria as authoritative statements of the fund's ethical position, and as illustrative of the level of complexity of ethical thinking by the fund. This is a mistake, because in fact these lists are not 'ethical investment codes' (Anderson, et al.1996:20), they are not statements of an ethical position, and for the deliberative funds at least, they do not reflect the level of complexity of ethical deliberation of the funds. The brochures in which these lists appear are short marketing documents designed to introduce the investing public to ethical investment in a simple and attractive way. In the case of Friends Provident Stewardship, they are produced by marketing executives rather than by the Stewardship Committee of Reference. They are written with brevity and simplicity in mind, and do not contain an account of the procedures used by the funds. The lists of criteria themselves are not ethical positions at all, they are merely statements of the investment policy of the fund. There is a considerable difference between an investment policy, 'We will not invest in companies that do X' and a moral position 'Companies that do X are acting unethically because of Y'.

So Anderson and his colleagues are wide of the mark when they claim, in their conclusion, that:

> The overall objection to ethical investment codes is their aggressive simplicity. It is a simplicity which ill fits them for ethical work. Moral choices involve balance and judgement. (Anderson, et al. 1996:20)

If you treat the list of negative and positive criteria that appears in the marketing literature used by Friends Provident Stewardship as an ethical code, then it may seem to be an 'aggressively simplistic' one, it may appear to offer mere 'slogans' (1996:20), and to pre-empt 'complex moral arguments in favour of a particular foregone conclusion' (1996:13). It may also appear to avoid balance and judgement. However, this document should not be regarded as revealing the level of Stewardship's ethical deliberation, but rather as a summary of its investment policy.

In fact, as we have seen in Chapter 4, the Stewardship Committee of Reference is constantly seeking to find an acceptable balance based on careful judgement. As we have seen (Chapter 4), the Committee of Reference goes to considerable lengths to make ethical judgements about which companies it would be ethically unacceptable to invest in, and which it would be ethically desirable to invest in. It does this in two ways: by selecting ethical criteria, and by using its judgement to apply those criteria to individual cases. It does the former at frequent and lengthy Committee of Reference meetings, and at special private meetings which occur rather less frequently; it does the latter at quarterly investment Sub-Committee meetings. The discussions are reasonably well informed, often being based on special issue reports provided by EIRIS. They also have a distinctively ethical flavour. On each matter many ethical issues are raised and debated. The discussions are also, to some degree, cumulative, and the Committee has built up a large body of 'case law' on particular companies and particular ethical issues. Another important feature of the Committee of Reference process is that on many issues it seeks precisely the balanced judgements that Anderson and his colleagues demand by trying to weigh up the good that companies do against the harm they do.

I have described these issues at greater length in Chapter 4. I restate them here as a reminder that some of the deliberative ethical funds devote considerable resources and energy to making ethical judgements about their investment practice. It is therefore wrong to write them off as 'aggressively simplistic' or to say that ethical funds do not use 'balance and judgement, or that they make 'crude distinctions.' The members of the

Stewardship Committee of Reference appreciate as much as anybody Anthony O'Hear's point that 'Investing ethically is not a straightforward matter. The issues involved are often disputed, and almost always complex' (1996:20). And the Committee of Reference may well be able to allay his worry that ethical funds make a habit of 'disregarding difficulties and counter-arguments' (1996:20).

Without wishing to labour this point, I will offer two lengthy quotes, which I believe offer a rather conclusive way of illustrating this issue clearly. The first is a quote from Roger Scruton's contribution to the Social Affairs Unit report.

> 'For the most part "ethical" is another name for fashionable causes, and a way of pre-empting complex moral arguments in favour of a particular foregone conclusion. This is a real ethical *question*, for example, about the use of animals in testing pharmaceutical products. Are we to test these products on human beings? Use them without testing? Give up pharmaceutical research altogether? Would those who oppose investment in these areas refuse drugs tested on animals when, without them, they will not recover from serious illness? To assume that this complex ethical issue can be brought to a conclusion, simply by refusing to invest in firms which test drugs on animals, is to adopt a frivolous and self-indulgent response to a real moral problem - and that itself is immoral' (Anderson, et al. 1996:13-14)

In mid-1996, after two years of detailed discussion, the Stewardship Committee of Reference issued a statement on animal testing. It is worth emphasising that this statement was not produced until after the publication of the Social Affairs Unit report, so it was not available to Scruton and his colleagues. It should also be emphasised that this statement was not produced as a response to Scruton's argument, but to a number of queries from Stewardship unit holders and IFAs.

> ...Recently the Committee has also been reviewing the question of investment in companies providing products which involve tests on animals, which is among the most complex and contentious issues the Committee has had to consider. Stewardship's policy is not to invest in companies involved in the unnecessary exploitation of animals. The interpretation of this policy in relation to the issue of animal testing has been the subject of detailed and painstaking review. The Committee is very aware that some members of animal charities or of anti-vivisection organisations, some of whom are holders of Stewardship units, believe that no investment should be made in any company which manufactures or sells

products which have been tested on animals, whatever the nature of the products themselves. The Committee understands those views. Its own discussions on the matter have been long and intensive. The present statement reflects the outcome of those discussions.

3.The Committee will not approve investment in manufacture of cosmetics, soaps and toiletries, unless their products are animal test free. The Committee will not regard products as free of animal testing unless the manufacturer has either not conducted or commissioned any animal tests on the products or their ingredients within the past five years or has stated that, since a particular date, it has not and will not conduct or commission any such tests. The Committee has similar criteria in relation to manufacturers' suppliers.

4.Bearing in mind, however, Stewardship's aim of investing in companies which are of benefit to the community, the Committee believes there will be occasions when investment in companies that are involved in animal testing is justified, especially when testing is required by law and where the company's products would be likely to provide outstanding and exceptional benefits, such as the alleviation of pain or the prevention or cure of serious diseases. The Committee does not believe that Stewardship could properly exclude all possibility of investment in pharmaceutical companies which contribute to the fight against disease, for example in combating AIDS, or providing drugs for cancer sufferers, or the vaccination and other forms of inoculation on which many millions of people in both developing and developed countries depend.

5.At present there is no legal requirement for companies to provide information about their practices with regard to animal testing. It is therefore impossible for the Committee to satisfy itself, in the case of any particular company, that testing on animals is indeed essential, and is kept to a minimum, with avoidance of unnecessary suffering. The Committee will nevertheless do all it can to encourage disclosure, and will favour those companies that provide information both about their own practices and those of their suppliers. The Committee will itself be open about the decisions it makes: whenever an investment in a pharmaceutical company is approved, the Committee will record and make public its reasons.

6.Similar considerations apply to investment in companies that manufacture those veterinary products or food additives which the law requires to be tested on animals. In the case of manufacturers of other products, who themselves undertake or commission the (again sometimes obligatory) use of animal testing, approval for investment will be given only in the most exceptional circumstances. Examples of such products are household or industrial chemicals, including printing inks. If approval is given, the Committee will again record and make public its reasons. It will also seek to influence manufacturers of such products to find alternatives to animal testing and to encourage their suppliers to do the same.

7.With regard to retailing, the Committee will consider investment in a company that sells cosmetics, soaps and toiletries that have been tested on animals only if it also sells an alternative range or products that is animal test free.

8.The Committee will not approve investment in companies that provide animal testing services to other companies.

9.The Committee recognises the question of animal testing as one of great sensitivity and complexity. It is an area where it is extremely difficult to obtain reliable information. Even on the basis of the restricted information that is available, no ethical unit trust can at present realistically claim to be completely animal test free. The Committee will continue to keep the whole question of animal testing under review, and in doing so it will wish to monitor and take account of the views of unitholders. (Excerpt from 'Statement on Animal Testing', Stewardship, 1996c).

This statement explicitly does not offer a final resolution by Stewardship on the issue of animal testing, however, it does show how wide of the mark Scruton's comments are, at least concerning Stewardship (the family of funds which accounts for over 50% of the ethical investment market!). This statement indicates that the Committee of Reference are not 'pre-empting complex moral arguments in favour of a particular foregone conclusion', and it accepts the existence of 'a real ethical *question*, for example, about the use of animals in testing pharmaceutical products.' Indeed the Committee specifically refers to the value of pharmaceutical research in order to combat disease which Scruton mentions. The Committee demonstrates that it does not 'assume that this complex ethical issue can be brought to a conclusion, simply by refusing to invest in firms which test drugs on animals' and so cannot be regarded as adopting a frivolous and self-indulgent response to a real moral problem' (Anderson, et al. 1996:13-14).

As we saw in Chapter 4, Friends Provident Stewardship is not the only fund to have an advisory committee, although few though do as much as Stewardship to discuss the issues. Some funds also have researchers who devote themselves to ethical and environmental issues full time. For funds such as these it is hard to come to any other conclusion than that they do give serious consideration to ethical issues, and so Anderson and his colleagues are, in this respect wrong. There are, however, five important qualifications to my rejection of Anderson and his colleagues' 'weak analysis' argument. Firstly, Anderson and his colleagues have some excuse for conflating the published brochures of the funds with their ethical positions. The brochures are not clear about the limited picture they give of the funds' work. Indeed the brochures of some funds sometimes use language which implies that their criteria are rather more than simple investment policies. The brochures are certainly full of strongly ethical language. In failing to state clearly the distinction between their investment criteria and their ethical positions and procedures, the funds must share the blame for Anderson and his colleagues' misinterpretation. Having said that, it was perhaps not a wise research strategy for Anderson to take marketing material as primary evidence to support claims of the strength which they have sought to make.[5]

Secondly, while Stewardship and a few other funds engage in deliberation, as I have said, the many investor-led ethical funds do not.

Thirdly, while I believe I have shown that Anderson and his colleagues fail to acknowledge the sophistication of ethical analysis undertaken by ethical funds, this does not mean that there are no weaknesses. Several of those I spoke to about this issue within the ethical funds thought that they had a considerable way to go in achieving better, more sophisticated procedures of deliberation.

Fourthly, for ethical thinking to serve as a basis for persuading companies to adopt better ethical and environmental practices, it needs to be of a particular kind. There are grounds for thinking that the kind of thinking engaged in by deliberative ethical funds is not always of the right kind.

Finally, it is possible that however much ethical funds recognise and deliberate about the complexity of ethical issues, the *appearance* they give might be too unsophisticated for them to effectively promote the kind of public debate necessary to persuade companies to change.

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[5] Oddly enough Anderson and his colleagues do appear to realise that their criticisms are not quite directed at the right target, because they complain that the ethical funds do not publish details of their underlying principles: 'It is worse than eccentric to be coy - in much of their public literature - about revealing the principles on which such selections are made. It may even be unethical.' (1996:17) However, in the absence of these principles, they appear happy to treat the marketing material as if it fully reflects the positions of ethical funds.

I will now consider the last three qualifications in more detail.

7.3.2 Weaknesses of ethical argument

The ideas about what counts as good practical argument, which I discussed in the introduction to this chapter, suggest that good arguments require one to make claims, backed by evidence that is warranted. The claims should be substantive, contestable and explicit; and that the evidence should be accurate, precise, sufficient, representative, authoritative, and perspicuous. As I said, I am not concerned to argue that these are necessarily the best conditions for good argument, only that good argument requires something like them.

When considering the weaknesses in the ethical thinking of ethical funds, one has to consider the resource implications of doing the kind of rigorous thinking that is necessary. The first problem is the sheer scale of the task. Ethical funds consider a wide variety of different issues. The range of topics covered by ethical funds given by the EIRIS guide is ‘alcohol, animal testing, gambling, greenhouse gases, health and safety breaches, human rights abuses, intensive farming, military - Ministry of Defence contracts, military - nature of involvement, nuclear power, ozone depletion, pesticides, pornography, roads, South Africa - poor workplace conditions, third world concerns, tobacco, tropical hardwoods, water pollution’ (EIRIS, 1996a:5). Each of these issues has many dimensions, as we saw in Stewardship’s statement on animal testing (see above). There are also many different perspectives, or opinions from which each issue can be considered, many of which are not easily reconcilable. Animal rights arguments, for example, are difficult to reconcile with utilitarian arguments about the benefits of animal testing for human health. Dealing with each of these issues in any detail is a considerable task. Adopting ethical positions based on sound arguments is harder still.

The undertaking of this task is hampered in various respects. The committee members whose responsibility it is to deliberate on these issues also have other practical tasks to do. In addition to seeking sensible ethical positions on various issues, they must also adopt criteria to be used to screen on these issues; they must apply these criteria to the selection of companies for investment; and they must respond to enquiries from unit holders, IFAs, researchers[6] and others. The advisory committees of many ethical funds meet infrequently and for only a few hours at a time, so they can make only a modest impression on these difficult issues. Even the members of the Stewardship Committee of Reference, who have each devoted two or three weeks work each year for a dozen years, are, as we have seen (see p.99ff.), rarely able to cover issues comprehensively.

The two funds which have a full time research staff might be regarded as being in a better position. NPI Global Care, in particular, has a well resourced research team including three full time researchers and some part-time support. These staff have the time to develop considerably detailed knowledge of the issues. And in their area of speciality - corporate environmental policy - they are exceptionally well informed. Perhaps their most significant claim to have developed the kind of rigorous thinking which is necessary is their practice of 'sector surveys'. These surveys do allow them to get fairly close to the bottom of the issues concerned. For example, the 50 page NPI Global Care report *How Green are your Grocers?* (NPI, 1996b) on the supermarket business identifies various key issues concerning the environmental performance of supermarkets. For example, one of the issues they consider is the quality of site management used by supermarkets. They note that petrol stations can be a significant source of groundwater and soil pollution. Many UK supermarkets operate petrol stations, but NPI finds that some are rather better than others at complying with Department of the Environment guidelines. However, while these funds are gradually making progress in various sectors, even here the task is compounded by the fact that these researchers also have research, marketing and management responsibilities.

As I reported in the previous chapter, Tessa Tennant, of NPI Global Care, argues that 'Dialogue without serious homework beforehand is just a waste of time. I mean you'll get fleeced, because companies know their business better than anybody else, so unless you have done a lot of homework you can get caught out very quickly.'[7] Doing your homework requires both a considerable amount of information about companies, and a considerable amount of ethical (or in the case of 'green' funds, environmental) thinking.

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[6] For example, an earlier draft of my case study of Friends Provident Stewardship, which appears in Chapters 3 and 4, was considered in detail and approved by the Stewardship Committee of Reference, at a cost of considerable time to the Committee.

[7] Interview with the author.

Coming to a reasonably adequate ethical position on any one of the many ethical issues concerning corporate practice, is a lengthy and difficult process. Let us take the issue of pornography as an example. Many ethical funds have criteria excluding investment in companies engaged in the production and distribution of pornographic material. What ethical 'homework' would be needed in order to produce an argument about why a chain of newsagents should stop selling pornographic magazines and novels? To come to an adequate ethical position on this would require, among other things, establishing a position on what is wrong with pornography, and why it is wrong, and a workable definition of pornography - what distinguishes a pornographic novel from a work of erotic literature. This is a difficult process. There are many different arguments about what is harmful about pornography, and how it may be distinguished from erotic art, or harmless 'entertainment'. To come to a conclusion would require detailed consideration and evaluation of each, making and testing claims, weighing evidence etc. This would be a very time consuming task. Furthermore, this process is rather complex, so it is hard to see how it could be undertaken without written analysis of the various positions, and the drafting of papers developing a position between the various different perspectives concerned. And once one has come to a conclusion on the issue of pornography, one has still not completed the task because one then needs to decide upon the ethics of producing, and distributing pornographic material which raises issues other than those directly related to the ethics of pornography itself. One might wish to offer, for example, the argument that the distribution of pornographic material is less blameworthy than its production, and certain kinds of production are less blameworthy than others. Finally, in order to put this moral position to the test, one might like to offer it for criticism to the companies to whom it might be applied, to investors, to anti-pornography groups, to libertarians and perhaps to academic ethicists. This may well lead to further deliberation and revision.

Currently no fund comes close to doing 'homework' on ethical issues at this level of detail. Given the scale of the task this can hardly be considered to be a strong criticism. However, according to the claims I made at the beginning of this chapter, if ethical funds are to become more effective at addressing the corporate harm and investment ethics problems, this is a challenge to which they need to respond.

7.3.3 Ethical position statements

One way in which ethical funds could demonstrably rise to this challenge is to develop the capacity to be able to offer investors, companies, and the public at large, detailed written statements of their ethical position on each of the issues on which they have a policy. If these statements are to have the procedural ethical qualities which I discussed at the beginning of this chapter, then they must contain arguments, which, on Toulmin's account (1958), must contain ethical claims on particular issues, based on carefully warranted grounds. Currently, few ethical funds have produced any detailed statements of their positions. Those that have, have done so only occasionally. However, both Friends Provident Stewardship and NPI Global Care are developing the capability to do so on a regular basis. In mid-1996 Stewardship hired someone specifically in order to set down on paper statements of the Committee's position. The 'Statement on Animal Testing', quoted at length above, is the first fruit of this work. The in-house research team at NPI Global Care have also begun to produce position papers on various issues (e.g. NPI, 1996b). These papers are an excellent start. However, without underestimating the difficulty of the task, they tend to be rather brief, and only begin to flesh out the ethical positions that are being adopted. But perhaps beginning this task is precisely what most is needed at this stage. Stewardship's statement on animal testing, though it is brief, already provides a useful basis for taking the argument forward. It raises a number of issues: the difficulty of gathering information on corporate animal testing practice; the lack of a legal requirement for disclosure; the legal requirement of animal testing for certain products; the benefits of products that have been tested on animals; the diversity of products tested on animals; and the availability of test-free products. This document provides a wide range of issues for further discussion and debate. For example, the Stewardship statement says:

> 'the Committee believes there will be occasions when investment in companies that are involved in animal testing is justified, especially when testing is required by law and where the company's products would be likely to provide outstanding and exceptional benefits, such as the alleviation of pain or the prevention or cure of serious diseases. The Committee does not believe that Stewardship could properly exclude all possibility of investment in pharmaceutical companies which contribute to the fight against disease, for example in combating AIDS, or providing drugs for cancer sufferers, or the vaccination and other forms of inoculation on which many

> millions of people in both developing and developed countries depend.' (Stewardship, 1996c).

This states an ethical position: 'there are occasions when investment in companies that are involved in animal testing is justified'. On what grounds do they make this claim? It is not entirely clear, but it seems to have something to do with the claims that sometimes companies which are engaged in animal testing are doing so in order to meet legal requirements, and also that the products produced using animal testing are sometimes exceptionally beneficial. These are interesting, and perhaps persuasive, claims. But for them to be really persuasive, we will need to know why the fact that a potentially unethical practice required by law should count as mitigation; roughly what counts as an 'exceptional benefit' and what the basis for trading off animal suffering for human benefit is. Of course these arguments could go on indefinitely, and I am not suggesting that ethical funds produce a book on each ethical issue. I would argue only that the further ethical funds are prepared to go in this direction, the greater their ability to justify their decisions about what is ethical and unethical about corporate practice, the greater their ability to persuade comapnies to adopt more ethical practices, and the greater their contribution to traditions of ethical thinking about corporate ethical practice.

7.3.4 Obstructions to the development of ethical arguments by ethical funds

There are a number of reasons why it might not be easy for ethical funds to engage in this time-consuming and difficult task of developing ethical arguments to back-up their ethical policies. One is that there is little support available to them for making ethical arguments. While EIRIS provides excellent research services on matters of information about companies, it has a policy of *not* offering advice on what ethical positions to adopt on issues of corporate ethics (EIRIS, 1996a:7). As a general point this means that EIRIS is only a useful resource when it comes to information, and is not useful as a resource for moral argumentation.

Another reason why it might be difficult for some ethical funds to adopt clear ethical positions, is that there is considerable ethical disagreement at the detailed level between ethical funds, and even between their researchers and advisory committees. For example while some members of an advisory committee might have strong religious objections to the production and consumption of alcohol, others may enjoy drinking in moderation; while some people involved in ethical funds are committed to pacifist principles, others may believe that arming the British Army and UN Peacekeepers is acceptable. Adopting an ethical criterion which commits the fund to avoiding alcohol and armaments can serve to mask this ethical disagreement. This is because those who are in favour of alcohol and armies may not favour ethical criteria which exclude this area, but they tend to *tolerate* such criteria. However, in the attempt to produce a well argued ethical position it will not be possible to hide these differences. Adopting an ethical position requires one to say what is wrong, in some detail, with alcohol, and what is wrong with armaments; and what is wrong with manufacturing and selling these things. In specifying such a detailed ethical position it is inevitable that disagreement between members of advisory committees would emerge. A pacifist committee member would have to say that she considers all manufacture of armaments to be unethical, while another committee member may limit her censure to companies which manufacture landmines and other particularly evil weapons, and to those which sell weapons to regimes noted for their human rights abuses. Several of those I spoke to who operate ethical funds consider their fund to take a rather harder line than they would personally on a number of ethical issues. The possibility of such conflicts of opinion offer one reason why ethical funds might be disinclined to seek to develop detailed ethical positions.

Another limitation on the ability of ethical funds to establish sophisticated ethical position statements is that to do so would require considerable resources. In the case of Stewardship, the Committee of Reference already has its work cut out administering and developing the Stewardship screening service. It is common for Committee members to have to consider well over 100 pages of material before each meeting. The considerable amount of extra work required to develop detailed ethical positions could be a full time job, and probably for more than one person.

7.3.5 The wrong kind of thinking

Another problem is that the screening approach focuses thinking on a different kind of ethical problem from that of developing ethical positions. This is the fourth qualification I offered to my rejection of the conclusions of the Social Affairs Unit report. Investment criteria are not ethical positions. They are of the form, ‘We will not invest in companies that do X', and not in the form 'X is wrong because Y.' The virtues of ethical criteria are rather different from those of ethical positions. Good ethical criteria are ones that can be applied fairly to all companies, and must therefore be based on information that is evenly and reliably available on all companies. This means they must be limited to those issues about which regulatory bodies publish comprehensive data - such as the Environment Agency's publication of breaches of water pollution regulations; information that companies are required to publish by law in their annual reports or elsewhere; and information provided by respected third parties. Deciding what criteria to use in order to screen out companies which, for example, make alcoholic drinks, is a very different task from that of deciding what is wrong with the manufacture of such drinks. The former task requires you to adopt criteria which treat alcohol manufacturers even-handedly on an objective basis. It requires little background ethical thinking about what exactly is wrong with alcohol manufacture, just the decision that it is in some sense unacceptable. The latter task requires detailed thinking about these background issues. What in particular is wrong with alcohol? Is all alcohol manufacture wrong, or just the irresponsible marketing of alcoholic drinks? Should the companies that make alcoholic drinks be held morally culpable for the actions of the minority of individuals who drink to excess, and are violent? These background issues are certainly discussed by deliberative ethical funds, however, they do not seem to be a primary practical concern for much of their deliberative time. They are not pursued as concertedly or systematically as they would need to be if they were to lead to well argued position papers across the range of issues concerning corporate ethics. The procedures outlined in Chapter 4 make the Stewardship Committee of Reference extremely good at making careful decisions about what companies are ethical enough to invest in, but do they not contribute to the development of arguments about how and why companies should change.

The fact that ethical funds focus heavily on the selection of criteria rather than the background ethical issues illustrates a general problem with the screening approach adopted by most funds. Intelligent argument about the ethical issues concerning corporate practice requires detailed consideration of complex ethical issues to be in the foreground. Yet the screening process always leaves these issues in the background. However complex and subtle the background issues are, the ethical screening processes must ultimately reduce these down to a simple ethical criterion which mechanically decides whether a given company is ethical enough to avoid exclusion from an ethical portfolio. Obviously the more criteria you have, and the more subtle your criteria are, the more subtle these choices will be, but ultimately the hugely complex ethical judgements surrounding the performance of a large, multinational corporation, manufacturing a hundred products, employing tens of thousands of people in a dozen countries may be reduced to a simple choice of whether it is 'acceptable' or not according to the requirements of a set of fixed ethical criteria. If such a company operated a subsidiary which, say, employed 100 people making ball-bearings for use in tanks, the whole company would simply be excluded by many ethical funds on an arms manufacture criterion. All other ethical deliberation by the ethical funds would cease for that company, as it would not longer be considered eligible for investment. While it is possible to make an argument might be made about why it is unethical to make ball bearings for tanks, the screening response to this problem seems not to do justice to the ethical complexity of companies, and does seem to cut short ethical argument, as Scruton implies (Anderson, 1996:13).

It should be noted that Stewardship, and a few other funds, do adopt a more flexible approach, at least on those issues for which they do not use absolute mechanical screening criteria. Stewardship seeks to examine companies on their own merits by weighing up the good the company does against the harm it does. This is a more subtle process. But, at the end of the day, however sophisticated the balancing of good and bad a company does, the ultimate choice comes down to a binary decision about whether the company is acceptable for investment or whether it is not. This, again, is a function of the screening response to these ethical problems. As we discussed in Chapter 6, screening is not the only response. If the priority of one's investment practice was to *engage* with companies in order to persuade them to change, one would not expend the huge resources of time and effort seeking to judge whether a company as a whole is acceptable for investment, but would instead seek to discover which areas of that company stand in need of reform, and seek to persuade the company to make those reforms.

My point is to argue that the attempt to make screening work diverts the limited resources of advisory committees away from the goal of developing sophisticated ethical arguments on each of the many ethical issues surrounding corporate practice, towards to more ambiguous task of making judgements about which criteria are best, and which companies are acceptable.

7.3.6 The appearance given by ethical funds

The fifth and final qualification to my rejection of the ‘weak analysis’ argument made by Anderson and his colleagues was that however sophisticated their ethical or environmental analysis actually is, the published material produced by ethical funds presents a contrary picture. Anecdotal evidence for this is suggested by the fact that Anderson and his colleagues were able, on the basis of published material, to almost completely miss the sophistication of ethical deliberation adopted by some ethical funds. The public appearance of ethical funds is important to their ability to persuade companies to change, and to contribute to the development of wider traditions of ethical thinking about business. In order to take ethical funds seriously, companies need to appreciate that ethical issues are treated seriously by the funds. The published material sometimes does not help this cause.

Anderson and his colleagues claim that:

> ‘Ethical investment as currently codified gives a heroes and villains picture of the economic world with some investment portrayed as ethical and others portrayed as not. As such it actually subverts moral education and the cultivation of a fine moral sensibility. (Anderson, et al. 1996:20)

On the basis of published material alone, this criticism is plausible. The material published by many ethical funds does seem to indicate that there are certain companies which are ethical and others which are not. If a company gets through a list of screening criteria, then it is ethical and if it does not it isn’t. The published material talks about ‘ethically sound companies’ (Henderson Ethical Fund brochure, 1996) and describes ethically screened investment as offering ‘performance without compromise’ (Abbey Life Ethical Trust brochure, 1994), and it implies that this can be achieved through a screened fund. Arguably, in using such simple rhetoric, ethical funds are presenting the investing public with a picture of ethical investment which indicates that deciding the ethics of corporate practice is as simple as a providing a list of investment criteria. Furthermore, the material may be taken to imply that the particular set of ethical criteria used by ethical funds are uncontroversial, firmly established ethical positions. This is largely not the case. Little attention is given, even in the material, of the deliberative funds, to the complexity of the issues, and to the fact that actually establishing what counts as ethical practice is very hard.

As we have seen, the deliberative funds at least appear to appreciate these complexities. This comes across clearly in Stewardship's statement on animal testing quoted above (see. p. 171). However, this complexity is not well communicated in the published material of ethical funds. It is at least possible that the simplistic message conveyed in published material actually discourages ethical investors and the wider public from thinking for themselves and from engaging with the difficult issues which arise from corporate practice. If, for example, an ethically concerned individual believes the simple message that by investing in an ethical fund he can invest with a 'clear conscience', or that he can have 'profit with principle', then he will no longer be stirred by his conscience to engage in debate about the difficult ethical issues concerned.

In fact there is very little positive evidence that ethical investment encourages complex moral debate about the issues with which it is concerned. From any reasonably sophisticated ethical point of view, just about every issue on which ethical funds have criteria is beset by a variety of subtle ethical difficulties. Instead of black and white, there are many subtle shades of grey. On this basis, when an investor considering ethical investment looks at an ethical fund, one might expect her to see this complexity, to perceive the unsettled nature of many of the ethical issues. In fact what ethical funds' published material offers such investors is a simple list of negative criteria, and a simple list of positive criteria. These two lists may seem to indicate that the issues are cut and dry; that the ethical funds, have studied the issues long and hard and have come to clear, principled conclusions on them, adopting investment criteria to fit. In fact, as we have seen, this is not what happens. Investor-led funds base their choice of criteria on their perceptions of public concern, and do not offer detailed arguments for the adoption of particular criteria. The deliberative funds have much more sophisticated thinking on the issues, but as we have seen in the previous section, on many they are far from having a clearly articulated justification for their criteria. If the public face presented by ethical funds implies that the complex ethical issues of corporate practice can be adequately responded to by a simple list of positive and negative investment criteria, then one might expect that this would not be a very helpful contribution to the development of public thinking about the ethics of corporate practice.

If furthering the development of intelligent public moral debate is important, and if deliberative ethical funds have considerable debates in private, why are their public contributions limited to simple lists of areas they will avoid, and areas they will positively select? More than one of the fund managers I talked to said that according to some IFAs, it was easier to sell ethical investments if ethical funds keep things simple. It is, after all, hard enough for consumers of financial products to choose between competing products on financial grounds alone. When ethical issues are introduced, the choice develops yet another degree of complexity. For example, one way in which investors are asked to choose between ethical funds is on the basis of whether the fund's published criteria match their personal moral concerns. As I indicated in Chapter 5 (see p.123ff.), this can be quite hard to work out given that it is likely that no fund will match the investor's principles exactly, and the investor will have to choose between several differing compromise funds. It is also argued by some people who sell ethical funds that people like moral issues to be black and white. Funds that imply they have produced authoritative lists of 'ethical' and 'unethical' companies, might be more attractive than ones who announce that no company is totally ethical, and none is completely unethical; that no stock market investment can be made without supporting companies engaged in some kind of harmful activity.

Another reason why ethical funds might prefer publishing simple lists of criteria to explicit ethical positions, is that as I have argued above (p.181ff.) it might be considered easier to persuade people of differing moral perspectives to unite behind an investment criterion, than it would be to persuade them to unite behind a clearly specified moral position. For example, more people might be expected to support the policy 'We will not invest in arms companies' than the ethical positions 'We believe that the manufacture of armaments is wrong because we are committed to the principles of pacifism.' There are many different moral perspectives from which one can justify avoiding investment in arms companies, but the number of moral perspectives consistent with pacifism is rather smaller. This example makes the point, but it is rather extreme. There is no reason why ethical funds could not adopt more mainstream ethical positions which are capable of attracting broad support from many ethical positions.

The reasons for publishing simple screening criteria, rather than sophisticated moral positions may make ethical funds more attractive marketing propositions. However, from an ethical point of view this is not encouraging. Fortunately from a marketing point of view the case is not clear cut. Some IFAs would argue that while keeping things simple makes their life easier, their customers are happy to tolerate complexity. Also from a marketing point of view, it is heartening that the funds that have gone furthest towards ethical complexity are also among the best selling funds, and the funds most highly recommended by ethical specialist IFAs.

In this section I have argued that Anderson and his colleagues' argument that ethical investment makes use of inadequate ethical analysis is founded on mistake. Anderson and his colleagues have missed the distinction between investor-led and deliberative funds, and have failed to grasp the sophistication of ethical deliberation within the deliberative ethical funds. However, those funds that do engage in deliberation do so in a rather constrained way.

7.4 Conclusion

In the introduction to this chapter I said that it was important for ethical funds to engage in deliberation. The grounds I offered for this were that

i) Ethical deliberation is necessary to establish what is ethical or unethical about corporate practice. This is an important first step in addressing the corporate harm and investment ethics problem.

ii.) The ability to deliver ethical arguments is important for engaging with companies in order to persuade them to adopt better practices. In Chapter 6 I tried to show that engagement is a promising approach for addressing the corporate harm problem.

iii.) More controversially, that it would be valuable for ethical funds to be in a position to offer ethical arguments in order to contribute to the development of wider traditions of thought concerning the ethics of corporate practice.

In this Chapter I have argued that investor-led funds do not engage in deliberation so are not in a very good position to develop the kind of arguments which are necessary. Deliberative funds are in a much better position in this respect, certainly much better than Anderson et al. give them credit for. However, even deliberative ethical funds face a considerable challenge if they are to develop the level of sophistication necessary to make and win ethical arguments across the board. An important obstruction to meeting this challenge is the dominance of the screening process. This is partly because the dominance of the screening process absorbs resources that may otherwise be available for the development of ethical argument, and partly because it may require ethical thinking to focus in a different direction. In the next chapter I will consider this conflict further.

Before completing this chapter, it is important to make one final point. The development of well argued ethical positions is by no means all that will be necessary for persuading companies to improve their practices, or for extending traditions of ethical thinking in the public sphere. In order to make arguments publicly effective they will have to be applied in a *strategic* way. Ethical funds will have to, in Vogel's phrase 'lobby the corporation' (1978). In general ethical funds will need to develop considerable tactical and rhetorical skills, and to develop a sophisticated understanding of how best to change a company's policy. While there are a handful of exemplary individuals, these are not skills widely found in ethical funds in the UK. If ethical funds are to make their arguments stick, they not only have to be able to make sound arguments but they will have to bring them before the right people, in the right way, at the right time. Given that the average ethical fund may invest in over 100 companies, and may have concerns in as many different discrete aspects of corporate policy, and given that ethical funds have limited resources, winning arguments will require rather narrow focus on particular issues and particular companies at any one time. Unfortunately the screening approach requires detailed consideration of all issues over all companies at the same time. It militates against the need to focus strategically on focusing on winning a small number of arguments at a time. Let us now turn to the question of the conflicts between screening and persuasion.

8. From Screening to Persuasion

8.1 Introduction

In Chapter 5 I argued that ethical funds do offer an effective solution to the investment ethics problem, by offering screened investment funds using generally reasonable and well researched negative and positive criteria. In Chapter 6, however, I argued that ethical funds were less effective at addressing the corporate harm problem. I argued that the most promising way in which they could improve would be to focus their resources on engaging with companies in order to persuade them to change. In Chapter 7, I argued that in order to develop reliable ethical positions, in order to persuade companies to change, and in order to contribute to wider public debate about corporate ethics, ethical funds need to be able to make intelligent arguments about the ethics of corporate practice. I claimed that investor-led funds are not in an position to do this, and that even the small number of deliberative funds face challenges in this direction. This chapter takes these arguments a step further. I begin by noting some possible conflicts between the screening approach, and the kinds of thinking and action required for effective corporate persuasion. The existence of this conflict means that to some extent a trade off must be made between screening and persuasion. Currently ethical funds make this trade off in a way that strongly favours screening over persuasion. Indeed many ethical funds only do screening, and make negligible efforts at persuading companies to change. In this chapter I want to consider whether the trade off could be made the other way around. Could an *ethical* fund be established which concentrates only on persuading companies to change, while doing little or no screening?

Can a persuasion-only ethical fund which reduces or abandons screening be ethically justified? The big problem here is that screening is the solution ethical funds offer to the investment ethics problem. Less screening would mean more investment in companies with unethical practices. No screening would mean widespread investment in companies with unethical practices. On the prevalent understanding of the investment ethics problem this would be unethical, because by investing in a company one is supporting it, and if that company has unethical practices, such support is unethical. If this is the only plausible way to see things, then the idea that ethical funds might shift resources from screening to engagement seems unattractive, and the idea of an persuasion-only fund seems a non-starter. In this chapter I will try to develop a case which shows that the current shared understandings held by the ethical investment tradition do not offer the only plausible way to view the ethical issues, and that the trade off between screening and persuasion can be understood in an alternative way.

In this chapter I will seek to make use of the 'interpretive' method to business ethics I described in Chapter 1. As MacIntyre claims:

> 'when a tradition is in good order it is always partly constituted by an argument about the goods the pursuit of which gives to that tradition its particular point and purpose.' (MacIntyre, 1984:206-207)

I want to engage in an argument about the goods the pursuit of which gives ethical investment its particular point and purpose. I propose to do this in two ways. Firstly I will seek to show that there may be conflicts between the two primary goods of ethical investment - the attempt to solve the investment ethics problem and the attempt to address the corporate harm problem - at least as they are currently conceived. Then I shall argue that the current conception of the investment ethics problem, based around the idea of 'support', raises certain questions. Thirdly, I shall offer an alternative conception of the investment ethics problem that draws on a different kind of conception of the relationship between investors and companies. In doing these things I will seek to appeal to shared understandings about the nature of investment held within the wider business and investment community. In making my case I will not be claiming that the current conceptions of the investment ethics problem are in any sense 'wrong'. Instead I will merely be pointing out some drawbacks of the current conception, and offering an alternative which I believe may be attractive to the ethical investment community. One reason that I hope it will be attractive is that it offers a means for addressing the investment ethics problem and the corporate harm problem at the same time, without conflict.

8.1.1 Conflicts between primary goods of ethical investment (as currently conceived)

In Chapter 7 I noted two conflicts between screening and the development of arguments about corporate ethics. The first conflict is a resources problem that says that ethical funds may not have the resources to both provide effectively screened funds *and* develop the range and sophistication of argument necessary; and the second is that the kind of ethical thinking required for screening is not the same as the kind necessary for the development of persuasive arguments for corporate change. In this section I will claim that the resource issue is a more general problem. But first there is a more simple and obvious conflict between screening and persuasion.

As practised by ethical funds, screening requires avoidance of companies with unethical or harmful practices, and positive selection of exemplary companies. In order to be effective at addressing the corporate harm problem, persuasion on the other hand will frequently involve investment in companies with unethical or harmful practices. The consequence of negative screening is that the better an ethical fund gets at screening, the fewer companies with unethical practices it invests in. The kind of companies an ethical fund invests in will be the ones which are doing best on ethical issues. These are the companies making the smallest contribution to the corporate harm problem, and so least in need of reform. The companies that are the most unethical, or that do the most damage to people and the environment, are the companies which most need to be persuaded to reform. However these are the very companies which the screening process excludes from the portfolios and subsequently from the scrutiny of most of the ethical funds.

In fact, while, negative screening excludes most companies with unethical practices, leaving some excellent companies, it also leaves some rather more ordinary companies. This means that at the very least the rather ordinary companies, which could become better, could be targets of engagement and persuasion. However, many ethical funds aim not simply at avoiding companies with unethical practices, but also at positive selection - at supporting companies with exemplary practices. When practised effectively, this should mean that the ethical funds, to a varying extent, exclude even these ordinary companies, leaving themselves with only the best companies. An exception to this concerns Friends Provident Stewardship's method of positive selection, which is based, not on investing in the best of the companies which pass the negative criteria, but on allowing the good some companies do to outweigh the modest amounts of harm they do. This approach means that some of the companies in its portfolio, while excellent in some areas, are rather poor in others. Such companies would be sensible targets for engagement, though the point still stands that the companies most in need of reform, will be excluded from Friends Provident Stewardship's portfolio.

Of course, no company, not even the best, is perfect, and even the best companies could be made better, so you could argue that ethical funds could focus on lobbying the best companies to make them better still. But this is not the way to have the greatest impact on the corporate harm problem. To do that ethical funds should be picking the companies whose harmful practices have the greatest impact and which can be reformed fastest and furthest. If corporate reform was an ethical fund's only consideration, it should choose, say, a moderately progressive oil company which, with the adoption of a new technology, such as double-hulled oil tankers, could dramatically cut risk of an Exxon Valdez-style catastrophe. However, because ethical funds focus on avoidance and positive selection, they might instead find themselves, for example, lobbying an environmentally conscious media company whose office energy conservation policy could be tweaked to reduce consumption by a further 2%. The contribution to the corporate harm problem of the former achievement could be many times greater than the achievement of the latter.

The other substantial reason for the conflicts between screening and persuasion, which was introduced in Chapter 7, is that there are limited resources available for ethical activity by ethical funds. As we saw in the last chapter, this resource problem limits the time available to do the kind of 'homework' necessary for persuasion. Ethical screening is an expensive process. If you say that you will not invest in any companies that contravene a list of 20 or thirty specific criteria, you need to be very sure that you have applied the criteria consistently, using adequate information. This kind of task is very time consuming and expensive. Particularly if, as a deliberative, fund you wish to examine companies on a case-by-case basis. This expensive and difficult task is unnecessary for persuading companies to change. As we saw in Chapter 7, making the kind of detailed ethical arguments necessary to persuade companies and the wider public to change their minds requires considerable work - both in terms of analysis, and in terms of planning strategy and engaging in the corporate lobbying process. This work is rather different from the work of screening, and will therefore require extra resources, including, perhaps, a dedicated research and lobbying staff. It is possible that an external agency might emerge to provide these services centrally for ethical funds, on the model of EIRIS, and thereby economising. Indeed there is already an organisation, PIRC Ltd.

which offers some elements of this services to pension funds, but mainly on corporate governance issues. But in the absence of such a central service, it is hard to see how effective attempts at persuasion could be undertaken without full-time, in-house research and engagement capacity.

If we assume that the funds available to pay for the ethical activities of funds are constant, then the only way in which these new engagement activities could be financed is by reducing the resources available for screening. Is it sensible to make this constant funds assumption? Ethical funds already charge fees for their services at the upper end of the scale for those charged by unit trusts. If an ethical fund was to simply hire a research team in addition to their negative and positive screening effort, they would either have to increase charges further (which might make them financial uncompetitive with other ethical funds), cut costs elsewhere (in marketing perhaps), or accept lower profits. None of these options will be attractive to the financial institutions providing ethical funds. However, the cost of the ethical component of these funds is to some degree independent of their size. This meant that as ethical funds grow, the costs associated with running the ethical component of the fund, will tend to fall relative to the revenues arising from the fund. Fees from unit trusts are charged as a percentage of an individual's invested funds. As the funds attract new investors the fee income will grow. Consequently, over time, growing ethical funds become more profitable. Perhaps then these greater profits could be invested in the development of procedures for active engagement? One could also perhaps argue - on the basis of the achievements of Tessa Tennant and her NPI research team in particular - that there are ethical marketing advantages from running a research and lobbying team, in which case an ethical fund which employed a research team might need to spend less money on marketing for the same level of public exposure, for example. Indeed a fund that was in a position to make detailed ethical arguments and to promote public debate, might expect substantially more coverage than a screening only fund.

My argument that there are resource conflicts between screening and engagement is therefore not entirely conclusive. However, the balance of probabilities seems to indicate that there are, in certain circumstances, significant conflicts. In such circumstances, the only way to provide the resources necessary to develop a programme of persuasion, and so to address the corporate harm problem, is to use the resources currently used by screening.

Before concluding this section it is worth noting one reason why it is possible that this conflict between screening and engagement has not have been widely recognised within ethical investment. As I claimed in Chapter 6, at least some members of the ethical investment community hold the belief that ethical funds can persuade companies to change their unethical practices by sending signals to companies via the stockmarket. On this model, the signals are to be sent by ethical funds avoiding investment in companies with unethical practices, and investing instead in exemplary ones. The basis for this process is screening. If market based approaches to changing corporate practice were effective, then screening would not conflict with persuasion. In as much as the market signalling approach is *believed* to be effective, members of the ethical investment community will not perceive there to be a conflict between screening and engagement. In Chapter 6 I argued that such market signalling approaches are not likely to be very effective, thus undermining this perception, and challenging what may be a widely shared understanding held within the ethical investment community.

8.2 Reconsidering the investment ethics problem

If I am right that serious conflicts exist between the two primary goods of ethical investment, as currently conceived, then we must conclude that to a certain extent there must be a trade off between the two approaches. The dominance of the application of the screening approach by ethical funds limits their ability to persuade companies to change, and to contribute to wider debate. But is this trade off inevitable? It would be wrong to dismiss the possibility that techniques of persuasion could be improved without sacrificing screening. It is possible that significant progress can be made by the funds towards greater efficacy at persuasion, while retaining a dominant interest in the screening approach - Stewardship and NPI Global Care are examples of this. However, on the strength of the arguments I have already given, there are limits to the extent of this progress. Ethical funds do not invest in the companies which most need to change if the corporate harm problem is to be addressed; and screening and engagement must fight for the same limited resources. Some trade off must therefore be made between the two goods pursued by ethical funds, at least as they are currently conceived. As I have shown, for most funds this trade off is made in favour of screening and the investment ethics problem, and entirely at the expense of the corporate harm problem. We should at least consider the case for turning the trade off the other way around. For example it *may* be the case that the most effective way of persuading companies to change - and so addressing the corporate harm problem - might be to launch an ethical fund which does *no* screening, but concentrates entirely on winning ethical arguments, and persuading companies to change. But can screening be sacrificed for persuasion? As I have said less screening means more investment in companies with poor practices. How could someone with strong ethical motives allow themselves to invest in an arms company, or one that despoils the environment? To do so would seem to run up against the 'support' conception of the investment ethics problem. There are two ways around this problem. One is to argue that the 'support' conception of the investment ethics problem is not as compelling as it appears. If this can be shown, then it will be rather easier to sacrifice achievement of a solution of the investment ethics problem for achievement at addressing the corporate harm problem. I will attempt to offer such an argument in the next section. The other way around the problem is to suggest an alternative conception of the investment ethics problem which is not in conflict with persuasion, and can therefore be pursued without any need to trade off screening for persuasion; and without having to sacrifice a solution to the investment ethics problem for a solution to corporate harm problem. I will offer this argument in the last section of this chapter.

8.2.1 Questions arising from the 'support' conception of the investment ethics problem

What is wrong with investing in a company which is failing ethically? As I argued in Chapter 5, according to investors, funds, and commentators alike, by investing in a company which acts unethically, one is 'supporting' that company, and in doing so one is behaving unethically. This is a core understanding of the ethical investment community, and it is an understanding which is promoted in their marketing literature, and more widely within ethical investment (see p.118ff.). The rhetoric used is rather strong at times. A good example of this is the 1995 Henderson Ethical fund literature which stated:

> Like any sensible investor, [ethical investors] want a good return on their money. But what they do not want is to have their money invested in any company, activity or regime of which they disapprove. Whether their objections are on moral, political, social or environmental grounds, they know that by investing in something they deplore, they are actually helping to support it and sustain it. (HTR Ethical Fund, brochure, 1995:1)

I noted that sometimes this argument is made in a very strong sense indeed. Bishop Harries of Oxford even seems to imply that by investing in a tobacco company one is investing in a way which kills people. But how seriously should we take this kind of claim? To what extent do investors really support companies? Is it always unethical to support a company that does harm?

Firstly, let us consider the economic aspects of the relationship between investors and companies. How does the act of investment support companies in practice? When shares are first offered to shareholders, either when the company is floated or when it makes a rights issue of extra shares to shareholders, the issuing company receives the capital invested by the shareholders. It may use this capital to invest in the development of its business. For the rest of the time, a company's shares are traded between various individuals and institutions in the stockmarket, and the company sees no additional money. This difference is seen clearly in who one buys the shares from. When shares are issued, a prospective shareholder buys shares by applying directly to the company. In the more usual course of events the prospective shareholder buys the shares from their previous owner in the market. During this market trading process the company does not receive any more money from shareholders. Any gain arising from a rise in share price is made not by the company but by the investor who sells the shares. In fact, once issued, companies do not directly gain capital from shareholders. This is important for ethical investors, because in terms of the number of transactions, buying shares on the market is by far the most common way that ethical funds - and other unit trusts - invest in companies.[1] However, the fact that companies gain no direct capital 'support' from stockmarket trading does not mean that they gain no economic support from shareholders. Shareholders help the company, not by investing new capital in it, but by supporting the price of the company's shares. If a company has a high share price it is able, periodically, to offer new shares in a rights issue which will bring in new capital. It also makes it easier for a company to borrow money, and makes hostile take-overs more expensive and unlikely.[2] If, on the other hand a company's share price falls, then it may

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[1] It is also true that many million members of the public will have bought or received their shares at the initial issue through privatisation, or the conversion of building societies to publicly quoted companies. However, ethical investors are typically more sophisticated investors who are used to buying shares on the market.

[2] This follows the Marris argument (1967)

find it hard to raise new capital, and it may also become vulnerable to a take-over bid. So we can conclude that in a financial sense the ethical investment community is right to think that investors support companies in various ways.

8.2.1.1 Indirect nature of support

However, the kind of support offered is perhaps weaker and less direct than that implied in the rhetoric about support used within the ethical investment community. Is it sensible to imagine that one's money directly finances the unethical or harmful practices carried out by the company? Take the case of someone who invests £5,000 in a conglomerate which has a subsidiary company which makes agricultural machinery, including electric cattle prods. Imagine that some of these prods are sold to countries with oppressive regimes, and frequently find non-agricultural employment when they are used by oppressive policemen to torture local dissidents. One might fear, for example, that one's £5,000 might have been used by the company to purchase a machine which presses a steel component of an electric cattle prod. If you imagine this, then clearly it is easy to think that by investing in a company you are supporting the manufacture of instruments of torture, and being very unethical indeed. But would such fears be grounded? If one simply buys into the company on the stockmarket, then one's £5,000 is not actually going to the company at all, let alone financing a particular piece of machinery. Instead it is supporting the company's share price, which may contribute to a very small degree to enabling the company to raise more share capital in a rights issue, which, subsequently, the company might invest in new steel presses, for example. However, even when investors do pay money direct to the company when shares are first issued, the money any individual small investor places with the company is not apportioned to a particular use (e.g. buying a steel-press). The money in the company's pool of capital will be distributed to many different sources - ethical and unethical. If a company's cattle prod manufacturing division uses hardy, old machinery it may be that that division does not receive investment derived from share capital for many years, so the shareholder's money can not easily be regarded as financing the manufacture of cattle prods that end up being used by police. So, in companies of the scale of those listed on the stockmarket at least, the support offered by shareholders is not as direct as this, but instead is a generalised economic support. This is consistent with de George's claim that

> ‘Shareholders cannot be held morally responsible for what the firm does since the shareholder is in fact very distant from the causal relations between an action of the corporation and it effects - but this does not relieve shareholders of all moral responsibility.’ (1990:174)

While the investor mentioned in the above example would be being unrealistic if she imagined that her economic support was directly financing the manufacture of instruments of torture, this support is still a kind of support and still implies some responsibility. But how significant is this generalised support? If the conglomerate concerned is a typical FT Index top 100 company, it will have a market capitalisation of well over £1bn. In which case an investment of £5,000 represents rather less than 0.0005% of the total share capital. The tangible general economic support this gives to a company is negligible. Even if we imagine that an investor’s funds are used directly by the company, we must conclude that the company would behave in exactly the same way whether this investor was ‘supporting’ it or not. While collectively the investors must bear some responsibility for the activities of the company, it is hard to see how this kind of negligible ‘support’ can be considered to give rise to significant personal blame to investors. One possible comparison might be the responsibility arising from the ‘support’ the average driver gives to the extra deaths caused by traffic pollution each year. While such deaths are a collective problem for society, individual drivers do not tend to feel personal responsibility for them.

These arguments can be applied to a wide variety of the kinds of issues addressed by ethical funds, and the general message is that the link between investment and harm arising from corporate activity is not as direct or as significant as the shared understandings of the ethical investment community sometimes imply. It is an exaggeration, for example, to suggest that ethical investors ‘know that by investing in something they deplore, they are actually helping to support it and sustain it’ (HTR Ethical Fund, brochure, 1995:1); or that ‘Many investors are causing, albeit unwittingly, serious damage to our planet by investing in companies that are harming the environment’ (Merlin Ecology Fund brochure, 1988:1).

8.2.1.2 Non-culpable harm

If de George’s conceptualisation of the investment ethics problem is right, that it is unethical to invest in companies with unethical policies (1990:174), then there is another issue which must be considered when assessing the ethical implications of the support offered by investors to companies. Do all companies whose activities have harmful consequences have *unethical polices*? Many of the harmful things companies do are contrary to company policy. If a rogue employee uses company resources to do something that is contrary to company policy then, arguably, so long as that company has taken due care to see that its policy is enforced, the company may be regarded as blameless. The caveat that the company should take due care is an important one.

If this is so, then on de George's conception it would not be unethical to invest in it. This not however reflected in many of the current ethical fund screening criteria. Many of the criteria currently used by ethical funds are based on absolute standards of measurement - for example, some funds exclude companies which exceed water pollution discharge consents, and take no account of the culpability of companies breaching these standards. There are many other examples where ethical funds avoid companies which do harm, or are engaged in ethically controversial areas, but which, arguably, cannot reasonably be considered to be acting unethically.[3]

Another way in which a company's unethical acts might be mitigated in the eyes of an investor is the case of a company in a dirty industry, making an effort to improve its practices. From the point of view of an investor 'supporting' such a company, should the good achieved by a company struggling to improve itself, outweigh the harm it continues to do? Some industries are generally regarded to have lower ethical or environmental standards than others. For example, the chemical industry causes more environmental damage than the groceries business, but this is because it is inherently more difficult to keep a chemical plant from harming the environment than a supermarket. If one company emerged as a leader in such an industry, working much harder than its competitors to clean up its act, would it be unethical to support it? By investing in it, one is supporting the harm it currently does, but one is also supporting it in its effort to take a lead and set new standards. Indeed some ethical funds now make exceptions for some such companies.

One ethical fund I talked to mentioned the case of the environmental consultancy doing work for the nuclear industry and armed services. This provides another similar kind of example. The fund felt uncomfortable about investing in such a company because it had

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[3] For further examples of situations where a company might be involved with something that is ethically controversial, but may not be regarded as acting unethically, see Sorell and Hendry (1984:59-61).

criteria prohibiting investment in companies involved in the nuclear industry. How could it justify investing in a company that did some of its work for the military and the nuclear industries? The worry seemed to be that, as an ethical fund, it could not support companies which earn their money from military or nuclear contracts, which 'oil the wheels' of these industries. But if one looks at the acts of the company concerned, it becomes harder to say that it is wrong to do environmental impact assessments for firing ranges and waste dumps. If Nirex wants to build nuclear waste dumps, and the law does not prevent it, then we need the best possible knowledge about their potential environmental impact, and we may even, for example, learn from such a study that such dumps are too dangerous. Similarly, if the army really needs another firing range, then we need to make sure everybody knows exactly what the environmental cost will be. Supporting a company that does this kind of work, as long as it does it well and conscientiously, is arguably a good thing.

Whatever the judgements made in each particular case, I hope it is a least plausible that these issues serve to mitigate the investment ethics problem of supporting harmful companies. Arguments of this nature can be entered into on most, perhaps all, of the ethical criteria used by ethical funds. However, in the Introduction, I ruled these issues as beyond the scope of my thesis. The point here is to illustrate that many apparent examples of the investment ethics problem, may not turn out to be as clear cut as ethical funds criteria imply. And we can, in any case, accept that it would be worse to support a dirty company which was doing nothing to improve itself, than one that was improving. It would be worse to support a company with unethical practices that made little positive contribution, than one whose net impact was positive. It would be worse to support a company that did unethical, harmful work for other companies with unethical practices, than a company which worked for such companies, but whose contribution had the potential to reduce the harm done. In the cases mentioned, I have tried to show that there are various ways in which one might be supporting something unethical, but that the judgement about the moral status of this support should be qualified by mitigating factors. While there are important examples within ethical investment of funds which seek to weigh the good companies do against the harm, in general decisions about the ethical status of companies are made in a rather absolute way which ignores questions of culpability and mitigation. From the point of view of some ethical funds, it seems that certain kinds of activity it seems can irreversibly taint companies, whatever good they do. This makes the investment ethics problem seem much more pervasive and clear cut than it perhaps deserves to be.

8.2.2 Putting 'support' in context

The arguments that I have made above seek to raise some questions about the conception of the investment ethics problem used within ethical investment. I do not want to suggest that everybody in ethical investment would share the views I have implied, only that such conceptions are not uncommon. What I have sought to do is not to reject the conception of support used within ethical investment, but to show that it is somewhat less direct, less significant, and less clearly unethical than is frequently understood. There is no doubt that, in a financial sense, by investing in a company one is supporting it. But I have showed that in many cases, the ethical problem arising from this support might be considered to be mitigated, sometimes decisively, by other factors.

However, despite this examination of the ways in which the idea of support can be mitigated, many people will still believe that by investing in a company which has done things which they consider to be grossly unethical - making landmines, exploiting child labour, running a factory farm, destroying the livelihoods of tribal people, take your pick - one is doing injury to one's principles, however small the investment. The issue is not a matter of scale, but a matter or right and wrong, or, as people commonly say, a matter of principle. It is associated with my claim in Chapter 5 that part of the understanding of the investment ethics problem held within the ethical investment community is the imprecise idea that *any* relationship with a company that is engaged in an unethical activity is morally compromising (see p.118ff.). On this understanding, the fact that the support one offers such companies may be negligible makes no difference, because one still has a relationship with the company. However indirect, insignificant, and ethically undecided the relationship is, one may still regard oneself as ethically 'tainted' by investing in the company merely because one is in some sense 'involved' with it. This argument has a rhetorical force, either on the basis of Kantian, deontological approaches to ethics or in an intuitive sense. Unchallenged it might make it very difficult to persuade investors to trade off a solution to the investment ethics problem in favour of more effective attempts at addressing the corporate harm problem.

I do not propose to criticise this 'involvement' conception of the investment ethics problem directly. Instead I seek to put the response ethical investment offers to the problem of support and more general ‘involvement’ into context. This contextualisation, I think, makes it harder to see how the ‘involvement’ conception of the investment ethics problem can be applied consistently (at least not without great financial sacrifice). I will then, in the final section of this chapter, offer an alternative conceptualisation of the investment ethics problem which, if it is attractive, may displace these conceptions of the problem which arise from ideas about ‘support’ and ‘involvement’.

The contextualising argument is that while people may *want* to have nothing to do with companies which do things which they consider ethically intolerable, this may actually be far more difficult to achieve than they first realise. It would certainly be more difficult than investing some of their money in an ethical unit trust. There are two different points to be made. One is that ethical funds are not promising complete avoidance of all companies engaged in unethical practices. One reason for this is that as I argued in Chapter 5, ethical investment requires compromise. Ethical funds, on many issues, qualify their screening criteria in various ways. While on some issues, such as weapons manufacture, they may make total exclusions, on other issues such as factory farming, animal testing, the sale of alcohol and tobacco, for example, their screening is not absolute. In a sense the feeling that one simply cannot be involved with a company that does something unethical, however small one’s involvement, is a restatement of the belief that strict avoidance is what is required, and as we have seen, on many issues, investing in an ethical fund requires some kind of compromise. While ethical investment may offer a reasonable solution to the investment ethics problem construed as a problem of support, it does not provide a solution if one wants to avoid *all* involvement with all companies engaged in unethical practices, although it does make progress in this direction.

However, it seems to me that a stronger form of this argument concerns the wider context of an individual investor’s financial relationships. The fact is that most investors - including, probably, most ethical investors - are enmeshed in a wide variety of financial relationships with a wide variety of different financial institutions. Many of these relationships would be regarded, on typical ethical investment criteria, as ethically compromising. One obvious example is the financial relationship people have with their banks. Money put on deposit with a bank is typically lent out to a variety of other individuals and organisations. Most of the big banks lend money to the very companies which are the focus of the ethical criteria used by ethical funds. Arguably the level of economic involvement with companies with unethical practices arising from a large savings account balance, is of a similar scale to an investment. To be consistent, presumably the ethical investor should make sure her bank account is not with a high street bank, but with, for example, the Co-operative Bank. This bank is the only major bank in the UK to claim that it does not lend money to companies which fail to satisfy a wide ranging ethical policy similar to that used by ethical funds. But bank accounts are only one of the financial relationships we have.

Many investors also have insurance policies of various kinds. Insurance companies invest the money they get from premiums in the stockmarket. In fact the insurance industry collectively owns a substantial share of the equity in UK companies. A life insurance policy involves the payment of considerable premiums over time, which are then invested by the insurance company in a way that will typically support the companies which fail to satisfy typical ethical investment criteria. Would-be purist ethical investors would have to be very choosy about their insurance companies as well as their banks, and their ordinary investments.

But perhaps the most significant difficulty in this respect is people's pensions. Pensions are for most people by far the most substantial form of saving in their lives, and also, not coincidentally, the largest source of investment funds in the stockmarket. By the time an average professional person retires, they might have amassed funds of well over £200,000 in their pension plan. This money is mostly invested in stockmarket companies, and in some cases will be supporting those companies which ethical funds consider to be unacceptable. One ethical investor I interviewed was pleased that he had been able to invest £5,000 in an ethical unit trust. But later in the conversation it emerged that he had an estimated £250,000 invested in his pension fund, which itself invested a total of £250m in Shell, a company which he considered to be engaged in a number of unethical practices. The 'support' of companies with unethical practices which this investor has been able to avoid by investing in an ethical fund is tiny compared to the support which he still offers to such companies through his pension. If one wants to dramatically reduce one's levels of 'support', one would have to try to move one's pension to one of the few ethical plans, and probably incur significant penalties as a result.

The example just given is not atypical of ethical investors. One of the findings of our research in the Morals and Money project with ethical investors, is the fact that many ethical investors have ordinary, unscreened investments as well as their ethical funds - in banks, other unit trusts etc. Of a survey I did with 20 ethical investors, 15 had other investments which contravened their ethical convictions (Mackenzie and Lewis, 1996). For example, one investor was concerned about arms manufacturers, so he invested £25,000 in Friends Provident Stewardship. However, he also had many thousand pounds invested the Foreign and Colonial Investment Trust, which invests in many companies with involvement in the arms business. His explanation for this, was that he wanted to achieve a decent return, and so needed to spread his assets. In addition to this reason, other ethical investors in my survey excused their 'unethical' investments by saying that they had an obligation to their heirs to maintain the size of their capital. From an ethical point of view, these reasons are not necessarily good ones - though it is possible to make ethical arguments which place loyalty to one's family above more general moral responsibilities.

One could also argue that when considering one's relationships with companies, one should not simply stop at savings, investments and insurance. What about the relationships one enters into as a consumer, as an employee, or as a taxpayer? Surely if one desires to avoid involvement with companies engaged in unethical practices, one should also make sure that the companies one buys one's products from are also free of unethical practices. Indeed various organisations - Ethical Consumer, New Consumer, and the Council on Economic Priorities (CEP) in the US - have emerged which seek to provide 'ethical consumers' with the information of the kind that EIRIS provides ethical investors. New Consumer's *Shopping for a Better World* (Adams, et al. 1991) rates thousands of consumer brands according to the ethical practice of their parent companies. As employees we are also frequently involved with other service companies, suppliers as business customers who either directly or indirectly may be engaged in practices which we might consider to be unethical. As taxpayers we are frequently 'supporting' practices which contravene many typical ethical criteria. The fact is that in the modern world it is very difficult indeed to avoid relationships with organisations whose practices we disapprove of.

Before concluding this section on the ethics of the support offered by investment, it is worth mentioning the kinds of 'undesirable' financial relationships which an investor may actually *acquire* when she invests in an ethical fund. One is that some ethical funds are managed by companies which are often themselves owned by larger organisations.

Some of these parent companies are involved in just the kind of ethically questionable activities which would lead to companies being screened out of an investment fund. For example, as Cowton (1994:228) notes, the Eagle Star Environmental Opportunities fund is managed by Eagle Star which itself is owned by BAT plc, a leading tobacco manufacturer. If it is unethical to invest in a fund which invests money in tobacco companies, perhaps it is similarly unethical to invest in fund which is managed by a company, the parent of which itself manufactures tobacco products? BAT is probably the most obvious example of this problem.[4] But a number of the other fund managers in the ethical fund sector have parents which are involved in some ethically questionable activities. A number of them are owned by big banks and insurance companies which do a variety of business with companies which would be ruled out of an ethical portfolio by standard ethical criteria.

Related to this, a second kind of 'undesirable' relationship is that none of the fund managers which manage ethical funds exclusively manage ethical funds. It is usually the case that ethical funds are just one of many funds managed by a fund manager, and in most cases ethical funds are a rather small part of the fund manager's portfolio. Although Friends Provident Stewardship has approaching £1bn in its ethical funds, it also has £18bn of other assets managed without reference to Stewardship criteria. The funds in the rest of the portfolio will consequently be invested in a variety of companies which are engaged in ethically questionable activities. If one is worried about being 'tainted' by investing in these companies, is it not also worrying to invest with a fund manager who chooses to invest its other funds in these companies? I should be clear that the other non-ethical funds managed by a given fund manager are legally separate entities from the ethical fund, and therefore the money invested by an ethical investor is legally separate from the money in the other funds managed by the manager. But that does not take away the fact that the fund management company of an ethical fund is also happy to spend time and resources investing money in companies engaged in unethical practices, and the fees an ethical investor pays to the fund management company help it to continue to do so. I do not wish to make much of this point. Ethical investment would

[4] As I noted in Chapter 3, the Eagle Star fund does not itself rule out investment in tobacco companies, and it does state that the fund 'should not in any way be labelled a 'green' trust, neither is it an ethical trust.' (EIRIS, 1996a). However they are in most respects identical to other green and ethical funds, and their arguments for not being an ethical trust are unclear and apparently contradictory.

certainly not have grown so quickly if mainstream financial services companies had not invested considerable sums of money in its development. I only mention the point to emphasise the great difficulty even ethical funds have of not having *some* kind of relationship of support with companies whose practices are ethically questionable.

It is of course possible to take the 'support' or 'involvement' conception of the investment ethics problem to its logical conclusion. If you feel that there is something profoundly wrong with investing in a company which does something you consider to be unethical, you can seek to purify your investment, savings, insurance, and pension arrangements, expunging all those relationships that you consider to be 'tainted' - which may even involve selling some of your ethical unit trust investments in favour of alternative, non-stockmarket ethical investment vehicles such as Triodos and Shared Interest. These are excellent institutions, and there would be no little doubt that you would be doing good by supporting them. However, such a course would be very costly, both in terms of the transaction costs arising from the rearrangement of your assets, and in terms of the lower long term returns available from such sources compared with stockmarket-based investments.[5]

In this section I have tried to raise some questions about the understanding of the investment ethics problem used within the ethical investment community. I have not sought to claim that the idea that investment implies support is misconceived, only to show that it is not as direct and significant as it sometimes appears - particular when put in the wider context of people's investments. My overall purpose in this chapter is to argue that the decision to trade off screening in order to concentrate on persuasion can be justified. My questioning of the 'support' conception of the investment ethics problem makes it seem less ethically compelling than the ethical funds some time imply. If so then it may make it easier to consider shifting emphasis from the investment ethics problem to the attempt to address the corporate harm problem.

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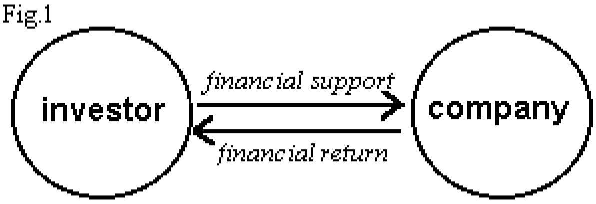
[5] In fact, it is not possible to find the life insurance and pension arrangements within the alternative investment sector.

8.3 The responsibilities of shareholders

On my arguments so far there seems to be an unavoidable conflict between the two primary goods pursued by ethical investment: a solution to the investment ethics problem, and a means of addressing the corporate harm problem. This is not an ideal situation. Whether or not my pragmatic arguments in the previous section make it easier to consider shifting the balance from screening to persuasion, we are still left with an uncomfortable trade off. In this section I will argue that this need not be the case. I will seek to offer an alternative conception of the investment ethics problem which can be solved in a way that does not conflict with attempts to address the corporate harm problem. This is an explicit attempt to extend the argument about the goods the pursuit of which gives ethical investment its purpose (MacIntyre, 1984:206-207).

In our discussion of the ‘support’ conception of the corporate harm problem, the act of investment was presented mainly in terms of its financial characteristics. On this model, what is unethical about investing in companies is the fact that one is giving them financial support. The ethical investment response to this problem is to sever the financial relationship by divesting. Financial relationships of this kind easily be broken under the law. If you consider yourself to be ethically ‘tainted’ by a financial relationship you can easily break it. This relationship can be represented in a very simple way (Fig.1).

Fig.1

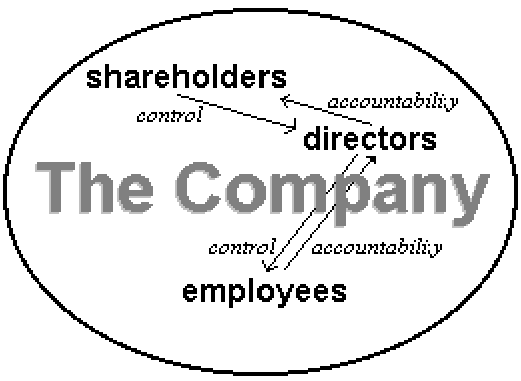


This model fits with a widely held conception of investment as a special kind of saving which produces a higher financial return than, say, building societies. On this model, if an investor divests from a company, she simply erases the two arrows in the diagram, and can thereby think of herself as completely unattached ethically speaking.

However, concentrating on the financial aspects and viewing investment as a kind of saving leaves out certain ethically important aspects of the relationship between investors and companies. By investing in a company one becomes a shareholder in it.

Being a shareholder involves becoming a member of that company.[6] Membership confers certain rights and responsibilities well beyond those of a simple financial relationship. The rights of shareholders are quite clear and set down in successive Companies Acts, and are sometimes modified by the company's Articles of Association. They include the right to attend shareholders' meetings; to bring resolutions before the meetings; to vote on resolutions; to vote on the appointment of directors and auditors; to ask questions of the directors (see Mackenzie, 1993: 46ff.). These rights, particularly the right to appoint and dismiss the directors, means that shareholders are in effect the ultimate source of control of companies. When the institutional framework of the company was first established by law in the 1850s in Britain, it was founded on the principle of self-regulation.[7] The law established a system of checks and balances. The directors were appointed by shareholders and given day to day control over the running of the company and its employees. In return company directors were given various fiduciary duties to look after the interests of the company, to report in detail their activities to the shareholders, and to submit themselves for re-election by the shareholders. The shareholders, also were expected to do their part in holding the directors to account by scrutinising company reports and by voting at shareholders' meetings. This self-regulatory system gives a rather different picture of the relationship between shareholders and companies (Fig. 2).

Fig. 2.



[6] Shareholders are also often considered to be 'owners' of companies. This is not quite accurate, see below (p.214ff.).

[7] See Tricker (1984) and Goyder (1987) for discussion of the origins of the modern company, and the idea of self-regulation.

On this model, shareholders are *part of* the company. They are its members. They do not float outside it, linked only by a thin financial umbilicus. They are an integral part of its governance structure. Indeed, they are in a real sense its *ultimate* source of control (Goyder, 1987:35). This brings with it a rather different conception of the investment ethics problem. If a company is doing something unethical, shareholders might not able to get themselves off the ethical hook simply by divesting. Furthermore, if a company is doing something unethical, its shareholders need not simply be considered as ‘supporting’ it. In order to show why this might be the case, let us consider an example.

8.3.1 Membership and responsibility

Imagine a wealthy widow who, many years ago, inherited a 10% stake in a small company that runs a shoe-making factory. Imagine that in recent years she has developed a concern about the environment. To her dismay, it comes to her attention that the factory has lax procedures for handling the chemicals it uses and frequently pollutes the local river. The widow is faced by a practical example of the investment ethics problem. How should she respond?

One response would be to do nothing. But this will not allay her concerns. It does not solve her investment ethics problem, but ignores it. I hope it is not controversial to suggest that this is the least desirable thing for her to do.

Alternatively she could sell her stake in the company. On the ‘support’ conception of the investment ethics problem, she is supporting a company that is engaged in unethical practices. The typical ethical investment approach says that she should cease that support immediately. From a purely financial point of view this may be fairly easy to do - she could sell to the other investors, or on the market if the company is listed. On this model, by erasing the arrows in Figure 1 (above), she has cut herself free from her moral obligations. She is no longer ‘tainted’ by her involvement with the company. After all, the widow is concerned about the environment, how could she justify supporting a company which needlessly pollutes a local river? If she sells she has saved herself the worry and guilt of the pollution risk. This response could also be a shrewd financial move, because it saves her the financial risk of this environmental liability. Of course, she might feel slightly uncomfortable that she has sold her shareholding to other investors who are not aware of, or concerned about the environmental problem, but now that she has nothing to do with the company, she may decide she can forget about it. It is no longer her problem.

How does this action look from the point of view of her role as a member of the company. To begin with, as a member, she is part of the problem. Over the years she has had a shareholding in the company, and never sought to monitor its environmental practices, never to ask questions about its environmental impacts, or sought to exert her authority as a shareholder. To a significant degree the poor environmental performance of the company has arisen because the directors have not been very responsible for controlling its environmental procedures. And this negligence is at least partly due to the shareholders' collective failure to hold them to account. The widow certainly has the legal right to leave the company by selling her shares, and by doing so she would be free of the company in a legal sense. If criminal proceedings arose, the directors may be liable, but having sold her shares she would be free of any legal obligation. However profitable her investment in the company had been over the years, she would also face no financial liability for the pollution damage done. But her *ethical* obligations would seem to go deeper than this. As a shareholder in the company, and as its ultimate source of control, her responsibility may be regarded to persist, even if she leaves the company. If a captain notices that his ship is on a collision course with an iceberg, we would not consider him responsible if he simply abandoned ship, without first trying doing his utmost to rectify the situation.

The widow's third option is to use her power within the company to try to seek to improve procedures in the factory so it has less chance of causing pollution. She could for example talk to the directors about the problem. If they were unresponsive, she could talk to the other shareholders. Perhaps she could seek to prepare some good arguments about why the company should change; noting that the pollution risk might give rise to large financial liabilities in the long term. If her arguments failed, perhaps she could raise the issue at a shareholders meeting, and maybe seek to dismiss the unresponsive directors. This third course of action is rather more troublesome, it will involve her is some difficult work, and perhaps some unpleasant arguments with her fellow shareholders. It may also involve some expense. And by retaining her investment she also retains her exposure to the ethical and financial risks surrounding the company. Furthermore, at the end of the day, all her good works might fail, and the company may retain is lax procedures. From the financial model of the company (fig 1.), going to all this trouble may seem crazy: what goes on within the company is its own business. If it is acting unethically, or has environmental liabilities, why not get out while you can? From the membership perspective, it is also true that what goes on within the company is its own business. However, the shareholders are part of the company, so it is also *their* business. From this point of view the widow's actions are not crazy but admirable. The widow, for the first time, is taking her membership in the company seriously. She is being a responsible shareholder, holding the directors to account, and taking a long term interest in the governance of the business. She is seeking to make the self-regulatory mechanism of the company do some of the work it was intended for.

While this may be admirable from a membership point of view, there would appear to be something of a contradiction with the 'support' conception of the widow's relationship with the company. By retaining her shareholding isn't the widow 'supporting' the company financially? Yes she is, and 10% is certainly a significant financial stake. However, while she maybe supporting the company in a financial sense, as a member of the company, by taking the third course, she is *opposing* the unethical aspects of the company's policy in a practical, active way. The fact that the captain of a ship which is on a collision course with an iceberg *remains on that ship* in order to try to change its course, can hardly be held against him. On the financial conception, seemingly one cannot invest in a company without being regarded as supporting everything it does. This is not the case on a membership conception. Shareholders as members *can* be regarded as supporting companies: when they vote for the directors, and, perhaps, when they do nothing, leaving the directors to their own devices. But shareholders can also be regarded as opposing the unethical policies of companies, by voting against the directors responsible for the policies, by seeking to persuade the company to change, and by proposing oppositional resolutions at company AGMs. On this membership conception of the investment ethics problem, investment does not entail support for a company's unethical activities, as long as investors are engaging in the attempt to rectify these activities. While the third course of action is difficult, risky, and may not be successful, it does seem to be responsible. Indeed it seems to exemplify the kind of courageous acceptance of ones responsibilities that we typically consider to be admirable in human life.

8.3.2 The membership relationship and ethical investment

What does this argument imply for ethical investment? Ethical unit trusts are shareholders in the companies in which they invest, and as such they are members of companies, and share a part in their control. If ethical funds know that a company is doing things which are harmful, should they sell their shares? Or should they do all in their power as shareholders to seek to rectify the problem? On the basis of the argument I have just made, as *ethical* investors, presumably they might be expected to favour the latter course. However, this is the opposite of what ethical screening achieves. The whole point of ethical screening is that every time an ethical fund learns that a company in its portfolio is acting unethically, it sells its shares. And in most cases without even telling the company that it disapproves of its unethical practices. A table in EIRIS's *Money and Ethics* guide shows that more than half of the ethical funds do not inform the company concerned when they divest from it on ethical grounds (1996a:70) and only three ethical investment institutions seek to actively persuade companies to change. Ethical funds also do not seem to take shareholder responsibilities seriously with regard to their investments in 'acceptable' companies (companies which have passed the negative and positive screening criteria and are in their portfolio). Such companies will often be far from perfect, and so are still doing harm to some modest degree, but ethical funds (with two or three significant exceptions) make little effort to use their power as shareholders to improve the practices of the companies concerned. Furthermore when ethical funds do divest, they sell their shares on a market that is largely composed of people who do not care about ethical or environmental issues very much, and who are unlikely to exert their power as shareholders in an ethically constructive manner.

Ethical funds as I have argued, have a 'support' conception of the investment ethics problem, and seem to follow the financial model of their relationship with companies. The 'support' conception of the problem says that if a company has a policy to engage in unethical practices, as an investor you are supporting that company, and this is unethical. The response implied by the 'support' conception of the problem is that by divesting one is breaking ones relationship of support, and thereby solving the problem. The alternative membership conception of the problem is rather different. If a company has a policy to engage in ethical practices, as a shareholder you have regulatory responsibilities for it as part of its ultimate controlling body. It would therefore be unethical to fail to attempt to challenge the unethical practices. From this point of view, rapid divesting is not a solution, because in divesting immediately one would have failed to attempt to challenge the unethical practices. Rapid divestment is like a captain 'abandoning ship' without first seeking to change its course. On this conception divestment, without first seeking to act, is not a solution. By becoming a shareholder one enters into a relationship of responsibility with the company that cannot be absolved, simply by divesting. This is not a legal responsibility, but it is I think an ethical one. It arises from the historical conception of the company as a self-regulating entity, and the conception of shareholders as the ultimate source of control within this entity.

On this membership conception, the investment ethics problem is in no way inconsistent with the corporate harm problem. Every example of the corporate harm problem, for which the company is culpable, simultaneously becomes an investment ethics problem for its shareholders. Any attempt by the shareholders to seek to challenge the company's unethical practices, is at the same time at attempt to address the corporate harm problem. No trade off is required, and the two primary goods of ethical investment are unified.

8.3.3 Objections to the membership conception

The most powerful objection to my line of argument is that while shareholders might be regarded, in company law, as the ultimate source of control in the company, in practice they may not be able to exercise this control effectively. While ethical investors have the powers of shareholders in theory, in practice do they have anything like the power of the widow in my example? If they have no power to persuade the companies in which they hold shares to change, they cannot have the responsibility to exercise it. There is much truth in the claim that the legal conception of the role of shareholders is rather different from the reality. Individual investors own tiny proportions of the share capital of companies, and acting alone have very little power. However, this point should not be overstated. Shareholders frequently do act to impose their collective will on the directors. In America, as I argued in Chapter 6, activist shareholders have collectively brought significant change to the companies they invest in. This is particularly the case when institutional investors have lobbied companies. Ethical funds are also a kind of 'institutional investor' and, as I have tried to show, can already do much to use their persuade companies to adopt better policies. In time, once they have developed the intellectual and financial resources, it is possible that ethical funds could have power well in excess of the widow in my example.

Another way of packaging this objection is to say that the idea of investors as members of a company might be legally true, but its ethical message is so widely disregarded as to be worthless. However, this would be to ignore the growing demands in recent years for institutional investors to take their shareholder's responsibilities seriously (Drucker, 1991a). In the light of a number of scandals, and corporate collapses - Guiness, Blue Arrow, Polly Peck, BCCI, Maxwell, Barings - the need for shareholders to act on their regulatory responsibilities has been widely appreciated. In the UK the Cadbury and Greenbury committees on corporate governance both recommended that institutional investors take account of their responsibilities as shareholders. Consequently, the members of the National Association of Pension Funds have adopted a policy of voting their shares on certain governance related issues. Indeed there is even talk of a change in pension fund law to require pension fund trustees to vote their shares at AGMs. This demonstrates that the idea of shareholders as regulators of companies is returning to popularity, and is certainly not just dead legal convention.

Another objection that ethical funds may want to offer to my interpretation of the membership conception of the investment ethics problem is that it does not fully apply to the screening process. The membership model applies to *existing* shareholders in companies which have adopted unethical policies. Screening is an attempt by ethical investors to avoid becoming shareholders in such companies in the first place. Surely the widow should not actively look to invest in companies with pollution problems? When it comes to choosing suitable companies to invest in, shouldn't one choose to invest in an ethically clean company, rather than one that is likely to develop unethical policies? One response to this is to say that screening does not entirely allow ethical investors to avoid the membership conception of the investment ethics problem. Ethical funds may well avoid many companies with the worst ethical policies, but they currently invest in a lot of fairly mediocre ones who have less than perfect policies. They could use their power as shareholders to work to rectify this. But this is a side issue. Can the membership conception of the corporate harm problem really *require* ethical investors to invest in companies with unethical policies? I do not think it can. One does not *have to* become a member of an organisation whose practices one does not like. If a sea captain can choose between commanding ships that he knows will be heading into dangerous waters, or ships that will be sticking to the safe routes, he is not obliged to put himself in danger. However, just because ethical investors may not be bound to take this route, that does not mean that they should not *choose* to. The oceans would be a safer place if the most dangerous waters, and the leakiest ships were piloted by the most conscientious and experienced sea captains. There is something admirable about an individual who acts ‘beyond the call of duty’ to take up responsibilities which need not be his, in order to serve the wider interests of society. Ethical investors, and many of those who run ethical investment funds, care deeply about the harm done by companies, and over the years the funds have amassed considerable knowledge about what the chief problems are and how to solve them. Rather than avoiding companies with unethical practices, this membership approach to investor responsibility is an invitation to ethical investors, to choose to accept responsibility. As shareholders in companies with poor ethical and environmental performance, they may try to challenge their unethical policies, and persuade those companies to change. If the corporate harm problem is truly a primary good of ethical investment then ethical funds should take up this invitation. Currently ethical funds seek only the cleanest and best companies, this is understandable on a ‘support’ conception of the problem. But the consequence of this is that the companies with the poorest ethical performance will tend to be populated by shareholders with the least ethical concern.

A final objection to the *wording* of the membership conception of the investment ethics problem is that shareholders are often also considered to be ‘owners’ of companies. As de George says, ‘The shareholder of a large, publicly held corporation is a part owner of the corporation.’ (1990:173). Sternberg similarly says, ‘The shareholders of a corporation are collectively its owners’ (1994:200). And it is probably right to suggest that there is a common ‘shared understanding’ in business and elsewhere that shareholders are the owners of companies. Company directors are often heard to claim that their goal is to achieve ‘owner value’. If this is the case, why have I not based by arguments on the ‘owner’ conception of the investment ethics problem? The main reason is that to do so would be rather controversial. In strict legal terms shareholders are not owners of businesses. As Lord Justice Evershed stated

> ‘Shareholders are not, in the eye of the law, part owners of the undertaking [the company]. The undertaking is something different from the totality of the shareholdings.’ (Short vs Treasury Commissioners, 1948, quoted by Goyder, 1987).

The principal reason for this is that incorporated companies are considered by the law to be independent legal 'persons'. Like real people, companies can own property, they can sue and be sued, and they can enter into contracts. Like people, companies, cannot be owned by anyone (Liegh et al., 1987). Shareholders are not legally owners of companies but members, and their rights over a company are not the same as their rights over an ordinary piece of property, but are tightly circumscribed by the law. In any case, this objection is not a serious problem for my argument. From an ethical point of view, one of the most salient aspects of ownership is the fact that owners *control* their property. This factor has a similar function in my argument about membership. It is the role of shareholders as the ultimate source of control in companies that is the source of their ethical responsibilities.

8.3.4 Conclusion

I argued in Chapter 6 that ethical funds are not currently effective at addressing the corporate harm problem. This is a significant failing because this is one of the primary goals of ethical investment. At the beginning of this chapter I said that this weakness arose partly because there is a conflict between the screening approach used to solve the investment ethics problem, and the procedures necessary to address the corporate harm problem. For the sake of clarity I may have exaggerated the extent of this conflict. As the NPI Global Care funds, for example, have demonstrated, there are certainly ways to pursue a more activist agenda while maintaining a core commitment to screening. However, this conflict is certainly a significant issue for ethical investment. In this chapter I have sought to resolve this conflict in a way that might enable ethical funds to become better at addressing the corporate harm problem. Firstly, I have tried to put the ethical consequences of investing in a company with unethical practices in context. This makes the investment ethics problem (on the 'screening' conception) seem less compelling. It therefore makes it easier to consider transferring resources to engagement approaches. Secondly I have argued that there is an alternative conception of the relationship between investors and companies, which implies a different solution to the investment ethics problem. On the 'membership' approach, the conflict between the two primary goods of ethical investment disappears. Responsible shareholders who engage with their company in order to persuade it to adopt responsible policies, are addressing the investment ethics problem and the corporate harm problem simultaneously.

9. Conclusion

In the keynote address to the 1996 annual general meeting of the UK Social Investment Forum, Charles Jacob said that ethical investment has now reached ‘puberty’. The implication he draws from this is,

> ‘not solely that the ethical unit trust movement had arrived at its twelfth year but that we too have arrived at a time of development, growth, creativity, and the asking of questions.’ (Jacob, 1996)

The great work of ethical funds in the last decade has been to establish ethical investment as an sustainable practice. This has now been achieved. The practice of ethical investment is embodied in a constellation of unit trusts, fund management institutions, research organisations, and financial advisers. It is supported by 150,000 investors, and £1.3bn of assets. The scale of this achievement is far greater than was originally envisaged. But the scale of the achievement is not the only important measure of success. Alasdair MacIntyre offers another. He argues that when a tradition of practice is in ‘good order it is always partly constituted by an argument about the goods the pursuit of which gives to that tradition its particular point and purpose’ (1984:206). Is the tradition of ethical investment practice in ‘good order’? In MacIntyre’s sense, it has perhaps not been so successful. In struggling to establish the practice of ethical investment, potentially divisive arguments about its procedures and purposes have not been a priority.

Charles Jacob can, more than anyone, claim the title of founder of ethical unit trust investment in the UK. The UK Social Investment Forum AGM is the focal event for the ethical investment community. Jacob’s suggestion that the time has come to ask questions and think creatively about ethical investment is therefore a significant one, and a step in right direction. In this thesis I have taken Jacob at his word and sought to ask some difficult questions about the nature and relative importance of the goods which give ethical investment its point and purpose. I hope that this effort may contribute creatively to the development and growth of ethical investment practice.

What are the goods of ethical investment? I have argued that the purpose of ethical investment is to respond to two problems: the investment ethics problem and the corporate harm problem; and that the point of ethical investment is therefore to establish an effective means to address these two problems. On this basis of this I have claimed that the two primary goods it pursues are a solution to the investment ethics problem, and a means of addressing the corporate harm problem.

The corporate harm problem is simply that many companies are engaged in unethical or harmful activities, at least some of the time. The investment ethics problem, as understood by the ethical investment community, is based on a financial model of the relationship between investors and companies. On this model it is unethical to invest in companies with unethical practices, because in doing so one is supporting them financially. On this conception, the solution to the problem is to avoid investing in companies with unethical practices.

I have argued that ethical investment is fairly effective at achieving a solution to the investment ethics problem (at least on a 'support' conception of this problem). However, I have argued that ethical funds are not very effective at addressing the corporate harm problem. Achievement of a means to address the corporate harm problem is one of the primary goods of ethical investment. In failing to address this problem effectively, ethical funds are falling short of achieving a substantial part of their purpose. I would argue that becoming more successful at this is the most significant challenge facing ethical funds.

Lack of success in this area arises because the two principal means by which ethical funds have hoped to address the corporate harm problem do not currently work very effectively. The 'market signalling' approach to persuading companies to change is based on a flawed model of the stockmarket. Until ethical funds grow vastly larger this approach *cannot* work significantly. The engagement approach, on the other hand, has been successfully used to address the corporate harm problem in America. However, in the UK it is pursued by only a few ethical funds, and even then receives only modest resources. In addition to this resources problem, some ethical funds are also not able to engage effectively with companies because they are not in a position to offer persuasive ethical arguments. In order to rise to the challenge of the corporate harm problem, ethical funds will need to devote substantially more resources to the pursuit of the engagement approach, and to developing the strategic and argumentative capacity to persuade companies to change. On current trends this will not happen rapidly.

Perhaps the main reason why ethical funds have a weak record at addressing the corporate harm problem is that the vast majority of their work is devoted to the implementation of the ethical screening process. While this solves the investment ethics problem, it does not contribute substantially to addressing the corporate harm problem. The dominance of screening is likely to continue. I estimate that approaching £1m per year is spent by ethical funds on administering the screening process. On the other hand I estimate that the engagement approach receives less than a tenth of this amount. Of course resources are not everything. But it remains true that in order to rise to the challenge of the corporate harm problem, new resources must be found, or ethical funds must transfer resources from screening to the development and implementation of procedures for engagement and persuasion. However, given that current ethical fund practice is dominated heavily by the screening approach, ethical funds - and ethical investors - will need to be *persuaded* to make this change. The second half of this thesis is an attempt to assemble a case saying why they should do this. And in so doing, to contribute an argument about the goods which give ethical investment its point.

One argument I have tried to make is that it is extremely hard to provide a full solution to the investment ethics problem. This problem (conceived as a problem about 'supporting' companies with unethical practices) can be fully solved by avoiding all investment in companies with unethical practices. The first step in providing this solution is to decide what counts as an unethical corporate practice. As I argued in Chapter 7, such decisions should be based on sound arguments. Investor-led funds do not make these arguments. Deliberative funds do, but in private, so it is hard to know how sound their arguments are. The second step is to offer a fund which avoids all those companies with unethical practices. As I argued in Chapter 5, in practice this inevitably requires compromise. No fund avoids all companies that are involved in practices which might reasonably be regarded as unethical. And individual investors are unlikely to find a fund with a package of exclusions which matches their concerns exactly. In any case, individual investors may also find it difficult to obtain sufficient information about ethical funds' investment policies to make a sound judgement about this. So, while ethical funds come rather closer than ordinary unit trusts to solving the investment ethics problem, there are a number of weaknesses in the solution they offer.

I have also tried to argue that the problem of supporting companies with unethical practices may not be as compelling as it is sometimes made out to be. In Chapter 8 I argued that while an individual investor can sensibly be regarded as supporting companies in a financial sense, the support a typical investor offers is not very direct or significant. It is less significant still when put in the context of the range of other financial relationships investors have with companies engaged in unethical practices; through their bank accounts, their life insurance funds, and their pension funds etc. Avoiding involvement in companies with unethical practices is much more demanding than merely investing a proportion of one's discretionary savings in an ethical fund.

I hope that these arguments make it easier to consider transferring resources from the administration of screening to the development of the procedures necessary to address the corporate harm problem. However, they rest on the idea that there is, at least to some degree, a trade off between solving the investment ethics problem and addressing the corporate harm problem. They are based on the idea that there is a conflict between the primary goods of ethical investment. This should not be too alarming. Many practices are conflicted in this way, and such trade-offs are common place. But practices which are able to bring their primary goods into harmony are more coherent, and therefore stronger. My most radical argument is that the investment ethics problem can be re-conceived in a way that achieves this coherence.

Essentially, I have argued that ethical screening can be viewed as a solution to the wrong problem. As I claimed in Chapter 8, the 'support' conception of the investment ethics problem is based on a purely financial model of the relationship between investors and companies. This model is flawed because it does not properly consider the role of investors as *shareholders* in companies. Shareholders are members of companies and, under company law, have an important regulatory role: they are considered to be the ultimate source of control in the company. This role implies responsibilities. On this 'membership' conception, if a company is acting unethically, the ethical problem for investors is that they are to a degree responsible for the company's actions. And on this model, selling one's shares, as ethical funds routinely do, may *not* be a satisfactory way of taking up this responsibility. This alternative conception of the investment ethics problem implies rather more onerous burdens on investors than those implied by the financial model. And this alternative conception of the problem is not so easily solved. However, the one considerable advantage this way of looking at things has is that the means of addressing the investment ethics problem is largely consistent with the means of addressing the corporate harm problem. When a company is engaged in unethical practices, both problems can be addressed simultaneously if ethical investors seek to engage with the directors, and fellow shareholders of their company in order to persuade it to change. If ethical funds are to pursue both of their primary goods in tandem, then they should willingly accept the difficult challenges of shareholder responsibility.

What might this mean in practice? To begin with it means that ethical funds which currently make no attempt to engage with companies should seek to do so. It means that ethical funds should seek to establish clear public positions on the ethical and environmental issues on which they have investment policies. These positions should be based on sound arguments, and should say what is unethical about current corporate practice, why it is unethical, and suggest how it should change. These positions will establish the basis on which ethical funds may attempt to hold directors accountable, to persuade companies to change, and to seek to influence the climate of moral opinion in the public at large. However, in order to win arguments, ethical funds will have to act strategically. They are involved in so many issues and with so many companies that they could not pursue everything at once. They will therefore have to focus their resources strategically on particular ethical topics and particular companies. They might seek to co-ordinate their activities with one another and with institutional investors with ethical concerns - such as the church funds. CERES in America has shown what strategic active engagement of this kind can achieve.

Of course given the difficulty of achieving these goals, it may be necessary to establish new institutions. For example, ethical funds might collectively finance the development of ethical positions and strategy in the same way that they collectively finance ethical research through EIRIS. It is possible that UK Social Investment Forum, as it expands, might provide the necessary institutional support. This programme of action will take time and cost money. New resources will be needed. However, given the financial success of ethical funds, and the relatively high charges they make for their services, it might be possible to go some way towards financing this development without sacrifice elsewhere. It is possible that such new investment might prove attractive financially: the funds which have moved furthest down this route are amongst the best at attracting new business.

A more radical way to avoid this conflict is to establish entirely new ethical funds based on this new model. These funds may do no screening at all, but devote all their resources to engagement and persuasion. Such funds might invest widely in the stockmarket on financial grounds alone,[1] both in companies with good ethical records and those with poor practices. They would seek to establish intelligent ethical positions on issues of corporate ethical and environmental practice; and to defend them publicly with sound and detailed arguments. On the basis of these arguments they would try to engage with companies in order to persuade them to change. They would also promote wider public debate about corporate ethics in order to seek to change the climate of expectations in which companies operate. They would derive their ethical credentials not from the selection and avoidance of companies based on ethical criteria, but on their ability to engage and persuade. They would, in short, adopt a leadership role in the ethics of corporate practice.

However, perhaps this is too radical a shift. A more conservative model might involve a hybrid kind fund. accepting a reduced set of core screening criteria covering the issues that are generally attract the most acute concern from investors - the arms trade, tobacco manufacture etc.

Charles Jacob concluded his address to the UK Social Investment Forum by saying, ‘What a challenge we have before us as we leave our formative years and enter into our maturity’ (1996). He did not, however, specify the challenge in much detail. In this thesis, I have made an argument about the primary goods the pursuit of which gives ethical investment its point and purpose. In doing so I have tried to establish corporate reform as the foremost challenge facing ethical funds, and to indicate the means by which it may be met.

[1] Indeed the fund could be an ‘index’ fund which, for example, invests in each of the 100 largest companies, in proportion to their market capitalisations. Such an approach would guarantee long term performance at market levels, and would cut the fund management overhead, releasing more resources for ethical research and engagement.

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