

Report and Recommendations
of the
Senate Assembly Advisory Committee on Financial Affairs
on
Investment Policies and Social Responsibility

February 28, 1978

Preface

At the "Public Comments" section of Regents' meetings held in May and June, 1977, students asked that the University divest itself of its investments in companies having business operations in South Africa because of the South African government's system of apartheid. At the request of the Vice-president and Chief Financial Officer and in accordance with the "Policies in Handling Stocks" adopted by the Senate Assembly in October 1971, the Senate Assembly Advisory Committee on Financial Affairs undertook a review of the issue.

The Advisory Committee initiated its deliberations at the September 29, 1977, meeting and has discussed the question regularly during the past five months. The Advisory Committee has reviewed the status of University investments and has received extensive background material from numerous sources including other colleges and universities, the Investor Responsibility Research Center, Inc., and the Forum on Corporate Investment in South Africa sponsored by the University Committee on Communications.

General Principles

The Advisory Committee began its deliberations with several fundamental assumptions about the University's social responsibilities. The Committee recognizes that the principal purpose of the University is to further the education of its students and the general public through teaching and research. Most of society's goals are served indirectly by the education acquired by students and through the advances in knowledge and the broad cultural developments fostered by the University. The University is not primarily an agency dedicated to direct social or political action. Its overriding responsibility is to maintain itself as a neutral forum for analysis, debate, and the search for truth.

Few societies in the world have been able to protect the academic neutrality of their universities. Even an institution as firmly established as The University of Michigan has sometimes found it extremely difficult to maintain an atmosphere of toleration and mutual trust that allows for critical evaluation and the free exchange of ideas. In pursuing the crucial role of society's chief guardian of intellectual freedom, the University must insure that prejudices of all kinds are eliminated from all phases of its own operation, and it must adhere to all of society's laws governing the management of its internal affairs. The University can often render important services to the community through technical assistance or consultation, but it must make strenuous efforts to avoid making commitments, as a corporate body, to political positions that may intimidate its members, produce an atmosphere of distrust and suspicion, or create obstacles to free inquiry.

The right to dissent is precious both to the University and to our society; but this is the right of the individual member of the university community and its exercise should in no way compromise the freedom of others. If the University operates successfully, members of the community should be free to discuss any question or analyze any issue, no matter how controversial or unpopular. However, when the University, acting as a corporate body, adopts a political position by formal statements of the Regents, or by their official actions, it runs the risk of impairing its essential role as a neutral forum for discussion or debate. Such large and dangerous risks should be taken only in those cases where the University's policies or practices clearly affect fundamental human rights and liberties.

Managing the Endowment

The University's endowment includes gifts from various organizations and private citizens. A few of these are unrestricted gifts intended to support the central educational mission of the University. Most have been donated with a special purpose in mind such as the creation of a scholarship, the maintenance of a laboratory, the support of an artist in residence, the encouragement of research on the peaceful uses of atomic energy, or the acquisition of works of art for the University's museums. The Regents' first responsibility, acting as trustees of these funds, is to insure that they are managed properly and used for the educational purposes for which they were donated. The University's endowment must not be regarded primarily as an instrument of political or social power; its principal purpose is to provide income for the advancement of the important educational and cultural objectives to which the University is dedicated.

Decisions concerning the utilization of the University's properties and the investment of its endowment must also be consistent with the applicable provisions of federal and state laws. The state courts have power to regulate the fiduciary behavior of the trustees of charitable trusts, and the federal and state taxing authorities have the power to enforce the conditions upon which the University enjoys federal income tax exemption and exemption from state and local property taxes. If these laws were violated, the University could lose a substantial portion of the benefits that come from receiving tax deductible contributions from its alumni and friends.

The chief responsibility of the Regents in directing the investment of endowment funds is to seek the maximum return consistent with an acceptable level of risk and with the investment goals of the particular fund. Only if there are compelling reasons should other factors be taken into consideration.

Occasionally certain stockholder issues arise that affect the administrative or managerial functions of a corporation. Ordinarily, these issues are not controversial and require little discussion since the interests of the University are usually best served by agreement with management. However, when controversial issues arise over the rights of shareholders or the prerogatives of management, the University should vote its shares in its own self interest. Sometimes, depending on the dictates of sound business judgment, that will mean taking the side of management and sometimes voting against management.

The University's Responsibility as a Shareholder

Although maximum return within acceptable levels of risk should be the University's principal guide for investment, the Advisory Committee recognizes that by investing in a firm the University must accept some responsibility for the political and social implications of a company's activities. If a set of noncontroversial investments could be found that would not offend the moral sensibilities of any members of the University community, the University's portfolio would never become an issue, but it is doubtful that such investment opportunities exist. The great issues of peace, human rights, and the preservation of the environment arise in all sectors of the economy. There are probably no corporations whose actions could be endorsed in every detail by every member of the University community. Since the University cannot maintain constant surveillance over all activities of every corporation in which it invests, it does not automatically endorse every decision taken by a firm's management. Nevertheless, some measure of responsibility does remain, especially in those cases in which an extraordinary social evil is apparent and a broad consensus develops within the University community concerning the moral shortcomings of a particular firm or type of investment.

Although a stance of political neutrality in the management of its investments is preferred, the Advisory Committee concludes that the Regents should be prepared to express censure or encouragement to the management of portfolio companies in the exceptional cases where political conditions raise serious moral or ethical questions.

The Committee believes that the University should not seek out controversy but rather should act only when a general consensus on a significant moral question has emerged within the University community. The Advisory Committee further believes that in many cases expressions of opinion, either through verbal or written communication, or by the voting of proxies, may often be more effective in stimulating change than selling the securities or refraining from their purchase. It would be inappropriate, however, for the University to join in legal actions or other similar efforts designed to force corporate managements to change their questionable policies. If, after making efforts to encourage change through direct communication with corporate managements and by statements of opinion and proxy voting, the Regents become convinced that the companies in question are not likely to alter their questionable behavior within a reasonable period of time, then the University should sell its shares and should not purchase

any other securities of these firms until their policies have been changed. When required, it is recommended that actions be taken in the following sequence:

- (1) direct communication of the University's concern to corporate management via letters or meetings;
- (2) the publication of statements describing the University's general position on the issue, and, when appropriate, explanation of these statements at shareholders meetings;
- (3) divestiture of University holdings in the corporation.

When divestiture of the University's holdings in a corporation is to be considered, hearsay evidence must be avoided and all reasonable means must be employed to be sure that the position of corporate management is unmistakably clear.

Procedures for Determining Shareholder Actions

As indicated above, the Advisory Committee believes that the University's 1971 policy of voting all shares with management should be revised. A more active policy is in order in those cases in which the rights of the University as a stockholder are in danger of being diluted or in which serious issues regarding fundamental rights arise. The University should reserve the right to vote in its own best interest and, when appropriate, in a manner consistent with its interest in furthering fundamental human rights.

There are many stockholder initiatives each year on a wide range of issues but only on rare occasions does an issue with such significant social or moral implications arise that the normal investment practices should be altered. To assist in the determination of an appropriate course of action when such issues arise, the Financial Affairs Advisory Committee believes that the Regents should consider establishing an Investments Advisory Committee. The Investments Advisory Committee would be charged with the responsibility of gathering information and formulating recommendations for the Regents' consideration. Although this committee's function and mode of operation would be predetermined, it would otherwise be an ad hoc committee whose members would be appointed only after the Regents had determined that a particular issue that might require a deviation from the normal investment policy had arisen.

Membership on an advisory committee of this kind should not be restricted to faculty members; instead it should be broadly representative of the University community and might include the following:

Two members of the University Senate appointed by the Senate Advisory Committee on University Affairs,

Two students appointed by the current official student government organization,

Two administrators appointed by the President.

The South African Issue

Since the issue of investments in corporations having business operations in the Republic of South Africa has become one of considerable immediate concern to members of the university community, for purposes of this issue the Advisory Committee on Financial Affairs will function as if it were the committee charged with the responsibilities described for the Investments Advisory Committee. In formulating a recommendation the Committee recognizes that changing political or social conditions may require that the recommendation be amended or even replaced at a future time.

The aggressive pursuit of the policy of apartheid, and the increasingly severe repressive measures taken by the government of the Republic of South Africa against opponents of that policy are in direct conflict with the most basic concepts of human rights. The Advisory Committee on Financial Affairs is convinced that a general consensus exists among members of the university community that this is such a serious violation of human rights that the University must formally recognize the issue. No such clearly apparent consensus exists, however, regarding the best procedure to follow with respect to the management of University investments in corporations having operations in South Africa.

A wide range of options is available to the University. Many universities, churches, and other financial organizations have reviewed the question and have developed different positions vis a vis corporate activities in South Africa. At one extreme is the total disregard of the political, social, and economic conditions in South Africa. Proponents of this view argue that the University should adhere strictly to the principle that maximum return from endowment investments is

paramount. At the other extreme is the divestiture of securities of any company having business activities in South Africa. Proponents of this view argue that withdrawal of investments from corporations doing business in South Africa is the only means of achieving the desired political change and that immediate action is required.

The Committee recommends that neither of these extremes be followed. To support the one extreme is to completely ignore the repugnant and morally reprehensible policy of apartheid and give tacit approval to the status quo in South Africa. This position is indefensible if basic concepts of human rights are to have any true meaning. Full divestiture, at the other extreme, would preclude any further influence that The University of Michigan might have in effecting change in South Africa. A position of continual, unequivocal opposition to apartheid will have a greater effect over a longer time than immediate divestiture. The immediate sale of University holdings in corporations that operate in South Africa would be a one-time gesture. Beyond the immediate effect of a public pronouncement it would serve no useful purpose. For these reasons the Committee recommends that the University support the ending of apartheid in South Africa through the judicious exercise of its rights as a shareholder. There are numerous ways by which shareholders rights may be used to exert influence on corporate management. As indicated earlier, these include:

- (1) direct communication of the University's concern to corporate management via letters or meetings;
- (2) the publication of statements describing the University's general position on the issue and, when judged most effective, explanation of these statements at shareholders meetings;
- (3) divestiture of University holdings in the corporation.

These represent progressively stronger actions in the support of corporate social responsibility in South Africa.

The Committee recommends that the first and second of these be undertaken at the earliest possible time. The initial communication with management should indicate that the University considers the endorsement of principles such as those embodied in the statement formulated by the Reverend Leon Sullivan (appended), and active pursuit thereof, as the minimum prerequisite for continued investment of University

funds in any corporation. The Committee further recommends that, in addition to the Sullivan principles, corporations should be encouraged to work for the enhancement of political, social, and economic rights for all of their employees in South Africa. The initial communication with corporate management should indicate clearly that the University expects that corporations will provide regular public disclosure of their progress toward full achievement of these goals.

If a corporation fails to satisfy these minimum prerequisites within a reasonable time period, the third alternative, divestiture, should be undertaken. In addition, the Committee recommends that, in view of the current political climate in South Africa and barring substantial improvements in that climate, the University should divest itself of shares in any corporation that undertakes significant capital expansion of its operations in South Africa. The Committee also recommends that the University, without delay, terminate its business dealings with banks that are making or renewing loans to the government of the Republic of South Africa.

The Sullivan Principles

These principles, originally proposed by the Reverend Leon Sullivan, a member of the Board of Directors of the General Motors Corporation, have been adopted by numerous United States corporations doing business in South Africa.

The six principles are:

1. Nonsegregation in all eating, comfort, and work facilities.
2. Equal and fair employment practices for all employees.
3. Equal pay for all employees doing equal or comparable work for the same period of time.
4. Initiation of and development of training programs that will prepare, in substantial numbers, blacks and other non-whites for supervisory, administrative, clerical, and technical jobs.
5. Increasing the number of blacks and other non-whites in management and supervisory positions.
6. Improving the quality of employees' lives outside the work environment in such areas as housing, transportation, schooling, recreation, and health facilities.