Chair’s Foreword

The Joint Advisory Committee on the Ethics of Investment (JACEI) serves the Methodist Church by providing a mechanism for tackling ethical dilemmas associated with investment and publishing an account of its work to Conference. This Report covers the twelve months to 31 March 2012.

This has been another busy year for the Committee. During the year we approved one Policy Statement on Pornography, and modified two existing ones, on the Media and Caste Discrimination.

We have long viewed collaboration with other Church investors as a key strength of the CFB approach to ethical investment, and during the year we welcomed significant ecumenical activity. The first ever international meeting of Church Investors Group (CIG) took place in Paris bringing together faith investors from Europe, America, Australia and Africa and included a delegation from the CFB. As a result it is hoped that faith investors around the world will develop increasingly close working relationships in the years ahead. The Committee also welcomed representatives of the US Interfaith Center for Corporate Responsibility and the Uniting Church of Australia, receiving presentations on their approach to the ethics of investment. Closer to home, in response to the Anglican Methodist Covenant, we wrote to the Chair of the Church of England Ethical investment Advisory Group to suggest reciprocal observer status between our two committees. This received enthusiastic agreement and is now in operation.

We reviewed and welcomed considerable engagement activity during the year including with companies involved in the hospitality industry and the potential risks from human trafficking. The Central Finance Board of the Methodist Church (CFB), working as part of an international coalition of faith investors, took a leading role in talks with Whitbread and InterContinental Hotels Group on their approach to managing the risks from traffickers operating on their premises. We also welcomed the involvement of the CFB Chief Executive in a public debate hosted by the Ecumenical Council for Corporate responsibility (ECCR) on vulnerable workers, trafficking and the leisure industry. This work will continue throughout 2012.

During the year we encouraged companies to adopt the Living Wage. The CFB is supporting the Fair Pensions JustPay campaign, and has written to a number of UK companies encouraging its full adoption. Further details can be found in the Short Ethics Report, published simultaneously with this Report to the Methodist Conference.

We continued to review companies failing to respond to the Carbon Disclosure Project (CDP) survey, and welcomed continued endeavours to encourage companies to take part. In early 2012 a new round of engagement commenced, with plans to escalate matters with long-standing corporate laggards via a Church Investors Group led process.

We took a particularly close interest in discussions with Alstom and Veolia, two French companies with interests in the Jerusalem Light Rail Project. At the end of the period under review, both companies had progressed contractual commitments to sell their equity and operating interests in the consortium, although both will continue to have a maintenance and advisory role. Further, escalated engagement is taking place with Veolia following concerns about bus routes operated by the company in the Occupied Territories.

We reviewed the ecumenical approach to voting and judged that it continues to work well. The CFB UK and European voting reports can now be consulted in full on the website. The dominant subject for voting against Board resolutions was executive pay in the UK, and the make-up of Board and shareholder capital issues in Europe.

We commend this report to Conference as evidence of the breadth and depth of issues regularly considered by JACEI and as part of the CFB’s commitment to invest ethically in accordance with Methodist teaching. We confirm on page 3 that we judge that the CFB has managed the Funds ethically in keeping with the aims of the Methodist Church. We are always delighted to receive comments and feedback on the Report itself, and on the work undertaken.

I would like to thank my colleagues who serve on JACEI for their time, commitment and contributions.

We hope you enjoy reading the Report.

Revd John Howard
Chair JACEI
Executive Summary

Policy Statement on Pornography
The Committee developed a Policy Statement on Pornography, which was approved by the CFB Council and is now available on the CFB website. The Policy complements the CFB Media Policy, which was slightly amended. The two statements reflect the approved guidance for investing in the media sector.

Amended Caste Discrimination Policy
The Committee met with Kasta Dip, Co-ordinator, Justice, Peace and Reconciliation for the Church of North India. He advised that the term ‘scheduled caste’ used throughout the CFB Policy statement, excluded Christians and other non-Hindus and it would be more appropriate to replace it with ‘Dalit’, whilst the term for the more inclusive phrase ‘scheduled tribes’ was ‘Adivasi’. It was agreed to make these changes to the Policy Statement.

UK Banks and Cluster Bombs
The Committee strongly endorsed CFB engagement with five UK banks regarding their policy on providing loan finance to the defence industry, and to cluster munitions manufacturers in particular. This followed unfounded allegations that HSBC had provided such finance to a US company involved in manufacturing cluster bombs. Engagement with all five, which revealed a varying quality of information in the public domain, is continuing.

Trafficking & the Leisure Industry
Engagement with Intercontinental Hotels Group and Whitbread has continued in the run up to the London 2012 Olympics. Following active engagement led by US investors in the run up to the 2010 World Cup in South Africa, UK church investors have taken a lead in dialogue with UK-based hotel groups on the risks of possible exposure to human trafficking on their premises.

Executive Remuneration and CFB Voting
The Committee monitors CFB proxy voting decisions at every meeting, placing high importance on the CFB exercising its shareholder stewardship. The CFB has long taken a robust position on excessive remuneration, voting to oppose executive remuneration that fails to deliver superior performance or is deemed to be excessive in aggregate. During the calendar year 2011, the CFB opposed 76 remuneration reports and voted to abstain on a further 32 from a total of 126 remuneration reports voted (86%).

The Living Wage
The Committee endorsed the CFB commitment to help the Methodist Church put its policy on the Living Wage into practice by joining a coalition of investors with combined assets of some £13bn. These investors agreed to sign letters to the chief executives of all FTSE100 companies calling on them to work towards adopting the Living Wage within the UK. The CFB continues to encourage employers to become Living Wage compliant employers.

Fossil Fuels and Ethical Investment
During the year, the Committee continued its long-term aim of developing an investment policy on fossil fuels and ethical investment, suggesting that any future policy on fossil fuels should include specific reference to power generation. The Committee also wishes to understand the impact of different fuel sources by examining any trade-off between climate change and economic progress in developing economies.

Investment in Israel/Palestine
The Committee spent considerable time during the year reviewing engagement with Veolia and Alstom around their involvement in the Jerusalem Light Rail Consortium. JACEI has recommended that both companies remain acceptable for investment based on the constructive dialogue achieved so far, and the decision taken by both to sell their stakes in the project. There have been further discussions with Veolia about their other transport interests in Israel/Palestine.

Carbon Disclosure Project (CDP) Engagement
The Committee regularly reviewed engagement with companies regarding participation in the CDP survey as part of the CFB Climate Change policy work. The Committee supports moves by CFB to encourage corporate ‘laggards’ to take part and wrote to several additional companies during the year. It was pleasing to note that Smith & Nephew reversed its 2010 decision not to take part in CDP and completed the 2011 survey request.

The Church Investors Group (CIG)
The Committee continues to view CFB collaboration with the ecumenical CIG as making an important contribution to the impact of faith-based investment in the UK and Ireland. 2011 marked an important milestone with CIG organising its first international ecumenical meeting of faith-based investors in Paris.
Conclusion

The Committee judges that the CFB has managed the funds under its control according to an ethical stance which is in accordance with the aims of the Methodist Church.

In arriving at this conclusion the Committee scrutinised compliance with CFB ethical policies through the:

- voting record of the CFB;
- ethically excluded list of UK and European companies;
- monthly ethics meeting minutes of the CFB;
- company engagement record of the CFB;
- Trucost and EIRIS reviews of the CFB UK portfolio carbon footprint;
- participation of the CFB in the Church Investors Group (CIG) (page 7); the Institutional Investors Group on Climate Change (IIGCC) (page 9); the Carbon Disclosure Project (CDP) (page 7); the UN Principles for Responsible Investment (UN-PRI) and the Extractives Industry Transparency Scheme (EITI);
- collaboration with the General Board of Pensions and Health Benefits (GBOPHB) of the United Methodist Church.

Resolution

That the Conference receives the report of the Joint Advisory Committee on the Ethics of Investment.
Significant Issues

Policy Statement on Pornography

A Policy Statement on Pornography was developed to complement the existing Media Policy Statement. This followed engagement with WH Smith, as a result of which it was recognised that this complex area required more detailed policy guidance. Subsequently the Policy Statement was approved by the CFB Council, and is available on the CFB website:

Policy

The CFB will seek to balance competing demands: to reflect in its investment policy that pornography degrades, exploits, manipulates and deviates from the ideal of God’s Kingdom, whilst noting that it is also more widely available and sometimes demanded, in ever more extreme forms. Therefore:

1. Companies are expected to operate wholly within the law (domestic and international) and to take swift corrective action to prohibit and proscribe any activity (such as hosting websites) that is judged illegal or criminal;

2. Companies, a major part of whose business activity is engaged in the production, transmission, publication or distribution of pornographic content should be avoided;

3. A distinction between production and distribution/transmission remains valid, except where distribution, transmission, marketing and promotion are pronounced.

4. Companies involved in production will be considered case by case as there are likely to be some instances where the activity, however small, will be unacceptable, in particular:
   - Publishers of pornographic print media;
   - Owner producers of pornographic television channels;
   - Owner producers of pornographic media formats such as film, video and games;
   - Owners of pornographic digital, virtual or online content such as websites.

5. Mobile telecommunication companies that facilitate the transmission of pornographic content will be assessed according to the strength of the controls in place to protect vulnerable groups. Mobile telecommunication companies that seek to derive material revenue from the provision of pornographic content will be subject to greater scrutiny and engagement, which may lead to disinvestment.

6. In keeping with our general policy, companies owning or operating premises providing pornographic experiences or live shows will be subject to investment exclusion.

7. Investment avoidance based on the contribution to company revenues alone is not appropriate and needs to be accompanied by qualitative ethical judgements based on the principles outlined in this Policy Statement.

8. In keeping with CFB policy, engagement will often be the most appropriate response in cases of broadcast, transmission and retail of pornographic material where this is not the main business, and may, in part, be based on the protection of vulnerable groups via age or access restriction. Such instances may include:
   - The retailing and siting of pornographic magazines and print media within high-street store chains;
   - The protection of taste and decency standards including age, access and encryption restriction by broadcasters;
   - The publishing of pornographic and non-educational sexual content in teen and young persons media;
   - The protection of minors via age, access and encryption restriction by premium telephone line providers;
   - The protection of minors via age, access and encryption restriction by Internet service providers hosting web sites, chat-rooms, blogging sites and other social and interactive media.

The existing Media Policy, first published in March 2001 was amended to reflect publication of the Policy Statement on Pornography. The two now reflect the approved guidance for investing in the media sector, which includes print, broadcast, online, telephone sex and chat lines, and live venues.

The committee reviewed, and welcomed positive dialogue with WH Smith over the display of explicit magazines within High Street shops. The company, whilst asserting consumer choice, nevertheless recognised the need for discretion and sensitivity in their display. Therefore it stated its intention of tightening up its current policy for the display of visually explicit material so that children are not exposed to inappropriate images. The CFB, alongside ecumenical partners continues to engage with Vodafone where the focus has been concentrated on access, protection and revenues derived from pornographic mobile content.

The Committee welcomed the publication of the Bailey Report on the Commercialisation and Sexualisation of Childhood. This recommended that companies should sign up to a family friendly code of conduct, and that sexualised images should not be in easy sight of children. The CFB continues to engage with companies regarding the premature sexualisation of children via retail imagery or fashion.
Amended Caste Discrimination Policy

The CFB Caste Discrimination Policy was published in June 2010. At its September 2011 meeting, JACEI was delighted to welcome Kasta Dip, Co-ordinator Justice, Peace and Reconciliation for the Church of North India. Mr Dip provided a fascinating background into working with discrimination based on caste, and commended JACEI for its forward looking policy as a tool for engaging with companies. He noted however, that although recognised within the Indian Constitution, the term ‘scheduled caste’ used throughout the policy excluded Christians and other non-Hindus, and that the correct terminology should refer to ‘Dalit’, and for scheduled tribes, ‘Adivasi’.

The Committee responded to Mr Dip’s recommendation, and agreed to amend the Policy to reflect this more inclusive definition of caste. The amended Policy was approved in March 2012 and can be found on the CFB website.

Where opportunity allows, the CFB engages with companies operating in India around the issue of caste discrimination to understand the employment and training opportunities for Dalits and Adivasis that can be encouraged.

UK Banks and Cluster Bombs

The Committee responded pro-actively to news reports that UK banks had provided loan finance to manufacturers of cluster bombs. News reports alleged that HSBC in particular had provided loan funding to Textron, a US manufacturer of munitions and cluster bomb parts. The CFB engaged with HSBC and received a detailed response that categorically denied that it provided finance to companies primarily involved in the manufacture or sale of weapons. This was supported by a detailed policy that is one of the most stringent within the sector. The Committee welcomed this position, seeing it as a benchmark for all the banks.

As a result, the CFB wrote to the other leading UK banks to understand their position on providing syndicated loan finance to the defence industry generally, and to US makers of cluster bombs in particular. Responses varied with Barclays having a public policy that acknowledges support for the defence industry but bars funding to makers of weapons of mass destruction including cluster bombs. Royal Bank of Scotland was exposed by Amnesty International as having provided funding to certain companies in contravention of its own policy upholding the Oslo Convention on Cluster Munitions. Its monitoring of loans against policy has now been tightened. Lloyds Banking Group provided a poor response and does not disclose its policy publicly whilst Standard Chartered indicated its policy restricts the funding of cluster and land mine munitions but it too does not disclose the policy publicly.

The Committee welcomed engagement with the leading UK banks which provided a comprehensive picture of where each stood with regards to their provision of loan funding to defence manufacturers. The Committee asked for further dialogue with Lloyds Banking Group and Standard Chartered with a view to encouraging more public policy disclosure, and this is continuing.

Trafficking and the Leisure Industry

The Committee welcomed continued CFB participation in the international faith community’s engagement with hotel groups regarding the potential risks from human trafficking in the run up to the 2012 Olympics. The Christian Brothers Investment Services (CBIS), which led a similar programme during the 2010 World Cup, was once again prominent. During the year, the CFB was part of a Church Investors Group delegation which met with Whitbread and Intercontinental Hotels Group (IHG), the two leading UK hotel groups.

It was noted that Whitbread has begun to put processes in place to monitor and manage the potential risk of exposure to human trafficking. Whilst the company believed the risk was small, it had identified an implication for its Costa Coffee outlets at points of entry into the country. The seriousness with which Whitbread was approaching the issue, including its support for the International Tourism Partnership Statement on Human Trafficking, was welcomed. IHG had also become a founding signatory to the Statement but was at an earlier stage than Whitbread in responding to its main recommendations. Whilst the company has a human rights policy, engagement suggested IHG was more exposed to risk, given its global reach, and more vulnerable to trafficking taking place on its premises given the rudimentary mechanisms in place for dealing with it. The Committee is encouraged by the close co-operation of Church investors in this engagement which will continue throughout 2012.

The Chief Executive of the CFB took part in a panel of experts hosted by ECCR at their annual open meeting in November 2011. Entitled Vulnerable Workers, Trafficking, Pornography and the Economics of Exploitation, the event brought together speakers from the Metropolitan Police, Object, Fair Pensions and Opposition Spokesperson for Crime Prevention, Dr Stella Creasey MP, to discuss the reality of sex and economic trafficking in Britain today.

Executive Remuneration and CFB Voting

The Committee monitors CFB proxy voting decisions at every meeting, placing high importance on the CFB exercising its shareholder stewardship. The CFB is a signatory to the UK Stewardship Code, which marked its first anniversary in 2011. The Code is generally seen as having made a useful contribution to the debate on shareholder responsibilities, although given the active position the CFB takes, it has affirmed rather than amended the general approach taken by the CFB towards voting. The CFB has an agreed template for voting, which is followed and executed by PIRC in the UK and Glass Lewis in Europe. Voting is conducted collaboratively with other church investor partners with a view to building a critical mass of consistent faith investor opinion in the exercise of proxy voting.

The CFB has long taken a robust position on excessive remuneration, which was outlined in the JACEI short ethics report last year, voting to oppose executive remuneration that does not have demanding performance targets or is deemed to be excessive in aggregate. Quarterly voting reports are published on the CFB website for both UK and European
proxies. During the calendar year 2011, the CFB opposed 76 remuneration reports and recorded an abstention on a further 32 out of a total of 126 UK company remuneration reports.

Notable examples of companies in which remuneration was opposed included all five UK domiciled banks (HSBC, RBS, Barclays, Lloyds Banking Group and Standard Chartered), Unilever, BG Group, BP, BT Group, J Sainsbury and Marks & Spencer. Shareholders are given a binding vote to approve Long Term Incentive Plans and during 2011 of 38 new schemes put to shareholders, the CFB opposed or voted to abstain on 45% of them.

The Committee reflected on government proposals to tackle excessive remuneration as announced in January 2012. The Committee noted the proposed imposition of a binding vote that would require 75% support to approve remuneration proposals. The Committee welcomed proposals that would empower shareholders to police excessive pay deals through improved transparency, and supports the publication of meaningful ratios between the highest and average or lowest paid within a company as a means to begin tackling economic injustice and social divide.

During the year the CFB met, alongside other church investors, Barclays, HSBC and Royal Bank of Scotland specifically on executive remuneration. All defended aggregate awards of over 400% of base salary in bonus and incentive awards for executives as vital in retaining key personnel. However they also indicated strong support for deferred awards and payment of bonuses in shares. The CFB also met with BSkyB to discuss the award of a retention bonus to the Chief Executive and other executive remuneration issues. The Committee noted that a significant transaction reward, earmarked for the Chairman of Cairn Energy, was overturned by shareholders working in private with the company, suggesting that investors have the tools to defeat egregious rewards when motivated to do so.

The Living Wage

The Committee received a briefing on the Just Pay Living Wage campaign, publicly endorsed by the Methodist Church at its launch in Methodist Central Hall, and follows the Methodist Church’s public commitment to be a ‘Living Wage Church’

The CFB joined a coalition of investors, with combined assets of some £13bn, which agreed to sign letters to the chief executives of all FTSE100 companies calling on them to work towards adopting the Living Wage within the UK. The Committee commended the CFB’s commitment to help the Methodist Church put its policy into practice.

A number of leading employers such as Barclays, HSBC, and KPMG have agreed to pay the Living Wage since the campaign began, with strong endorsement of progress from others such as Standard Life.

As part of its own employer commitment, the CFB reviewed its workplace practices and as a consequence a new agreement was made with its cleaning contractor to ensure that the Living Wage was paid to all cleaning staff used to fulfil the CFB contract.

None of the four major UK food retailers are living wage employers and with a combined workforce in excess of 500,000 this would make a considerable difference to the lives of the poorest in work. Therefore, the CFB engaged with Tesco as the UK’s largest private sector employer asking it to consider working towards being a Living Wage employer. Tesco is recognised as having industry-leading employee terms and conditions, and the company has argued that its salary, benefits and a career average defined benefits pension package amounts to significantly more than the Living Wage. It contends that the package should be considered in the round rather than applying a Living Wage calculation to base salary. The CFB will continue to argue for Tesco to make a commitment to become a transparent Living Wage employer, together with seeking confirmation that under current employment terms staff including contractors are receiving the equivalent of the Living Wage.

Fossil Fuels and Ethical Investment

The Committee continued its work in developing an ethical policy on investment in fossil fuels.

To inform discussion a paper was produced by the Joint Public Issues Team that considered the impact of fossil fuels in the context of public policy and climate change. It also analysed the energy outlook for coal, oil, gas and some of their alternatives, noting the yawning policy gap between international aspirations to reduce greenhouse gas emissions, and the lack of action by governments.

The Committee:

- reflected that the paper provided a useful introduction to what is a challenging subject and could be used to build further thinking;
- believed strongly that the extraction of fossil fuels, such as coal, should not be divorced from the main uses to which they are put;
- agreed that a paper on power generation was required, which would seek to differentiate between the impact of different fuel sources and examine the trade-off between climate change and development aspirations in poorer economies;
- suggested that any policy on investment in fossil fuels should include specific reference to power generation;

Investment in Israel/Palestine

The Committee spent considerable time reviewing engagement with Veolia and Alstom, two French companies held indirectly by the CFB through its investment in the Epworth European Fund. Both companies have been involved in a consortium building and operating a fixed line tramway linking West Jerusalem with Israeli settlements in
East Jerusalem and the West Bank, which allegedly contravene international law. Following extensive engagement with both companies, the advice of the Committee is that to date there is insufficient reason for the CFB to avoid either company on ethical grounds.

At the close of 2011 Alstom confirmed that it had signed a contract to sell its stake in the consortium, which is expected to be completed in the late spring of 2012. The company will continue to have maintenance obligations as the builder of the train units, but will no longer be a partner in the project.

Veolia has experienced a delay to its plans to sell both its stake in the consortium and its operating license to an Israeli bus company, but it is hoped that this can be progressed during 2012. Two other issues were reviewed:

- the Tovlan Waste Disposal Site, which has been sold;
- two bus routes between settlements ruled as unlawful in international law. The company claimed that they were express services connecting cities and were operated without discrimination, serving both communities.

Given the views expressed by the 2011 Methodist Conference on Israel/Palestine, further engagement is underway and is being escalated. The Committee also noted that Veolia recently announced the disposal of its entire transport interests as it restructures its global business.

Carbon Disclosure Project (CDP) Engagement

The Carbon Disclosure Project, which now represents 551 global investors with combined assets of US$71 trillion, surveys 6,000 of the world’s largest companies asking them to report on their climate strategies, energy use and emissions. The Committee believes climate change presents an acute risk for carbon intensive businesses and CDP offers a robust methodology and mechanism for managing and reducing climate change impact. It strongly supports CFB initiatives in engaging with company ‘laggards’ that have not responded or declined to participate in CDP.

It was pleasing to note that Smith & Nephew reversed its 2010 decision not to take part in CDP and completed the 2011 survey request. Halfords chose to provide some quantitative data that fell short of a full survey response, but we were nevertheless encouraged at the pro-active stance the company is pursuing towards reducing its impact. After failing to respond to engagement for three years the Restaurant Group, whilst still declining to participate, has agreed to review this decision in 2012, whilst also setting out its programme to manage emissions and energy use across the restaurant estate.

The continued failure of Cookson Group, Spirent Communications and Halma to participate was disappointing. In 2012 the Committee agreed an escalation process for those high impact companies that have consistently failed to respond to CDP, and in the CFB’s view are inadequately disclosing how they are managing their risks. As part of this initiative all three companies will be targeted for further action using the added weight of the Church Investors Group.

As part of the 2012 engagement process, several new companies have been targeted following a failure to respond to the survey request in 2011; these were ITV, Go-Ahead Group and Aggreko.

The Committee also welcomed CFB involvement with the CDP Water Disclosure Project, which is supported by 354 global investors with combined assets of US$43 trillion, and targets the most water intensive companies among the Global 500. As resources allow, it is hoped to commence a programme of engagement with UK businesses that have not taken part. During the year, the CFB met several times with Tesco and was pleased to record the company’s progress in completing a water footprint of its UK estate. Initiatives to improve water use and conservation through its supply chain were also welcomed. Water is becoming a key issue for responsible investors, and we expect to undertake more engagement on this over time.

The Church Investors Group (CIG)

The Committee continues to view CFB collaboration with the ecumenical CIG as making an important contribution to the impact of faith-based investment in the UK and Ireland. 2011 marked an important milestone with CIG organising a first global meeting of faith investors in Paris. Attendance by over 40 American, European, Australasian and African church investors presented an inspiring opportunity to affirm closer working together, with trafficking highlighted as one positive example where UK and US organisations in particular were now close partners.

The CIG also:

- Received a presentation on sustainability from Xstrata
- Organised a strategy away-day to determine the CIG strategy for the next three years
- Received a presentation from the Financial Reporting Council (FRC) on the anniversary of the launch of the UK Stewardship Code
- Completed a ‘traffic light’ analysis showing the aggregated restricted investments of CIG members by type of exclusion
- Launched a re-designed CIG website
- Organised engagement meetings with Whitbread, IHG, Xstrata, HSBC, Barclays, Rio Tinto, RBS, GSK, BP, Vodafone and Nestlé
- Continued to review and monitor the ecumenical voting policy adopted in 2009 and modified the voting template for use in 2011-12

The Chief Executive of the CFB continues to serve as Vice-Chair of CIG.
Alcohol and Tobacco
The Committee noted the Methodist Church’s on-going support for per unit minimum pricing in the sale of alcohol. The Committee noted commitments made by the major food retailers for a ‘responsibility deal’ and will hold them to account at future engagement opportunities.

The Committee noted the Church of England’s new investment policy on alcohol which was published during the year. It welcomed the attempt to encourage the responsible sale and production of alcohol as well as the useful theological contribution.

At various meetings with Tesco, their alcohol display and sale policy was raised. Whilst acknowledging the commercial challenges in acting alone, Tesco has been the most supportive of unit pricing among food retailers, which the Committee welcomes and supports.

The Committee noted that a ban on the display of tobacco products in larger shops in England comes into force in April 2012, although smaller premises will not have to comply until 2015. The other countries of the UK are expected to follow suit at some point.

Armaments
The Committee considered a CFB note on the logistics and supply chain company Wincanton which had won a contract to supply spare parts for military vehicles and was also involved in a joint venture with Serco providing logistical support in the transfer of prisoners in South Eastern England. The company does not handle strategic weaponry, and the transfer of prisoners is in principle ethically acceptable. It was noted that revenue from both contracts would amount to approximately no more than 4% of turnover. It was concluded that there were insufficient ethical grounds to exclude Wincanton.

The Committee noted that Avon Rubber would be subject to investment exclusion on its entering the FTSE All Share. Avon Rubber supplies protection and respiratory apparatus direct to the US and UK military, with 77% of Group revenues earned from defence contracts.

Corporate Governance and Business Ethics
Executive remuneration has once again dominated the political agenda, leading to government proposals for reforming pay disclosure. The Committee welcomed these developments, believing the provision of a binding vote on pay may lead to improved shareholder stewardship.

During the year the Committee received regular news reports and updates on corporate governance and executive pay, and noted engagement by the CFB with several companies specifically on levels of pay, including HSBC and BSkyB. In deciding how to vote, the CFB considers the quality of disclosure, how stretching performance hurdles are and the potential for excess.

The Committee reviews the quarterly CFB voting reports and welcomed the successful ongoing execution of the CIG template for voting CFB UK equity holdings. PIRC is the appointed research and execution provider. For Europe, the CFB uses a template in common with the three national investment bodies of the Church of England, employing the Glass Lewis proxy voting service. More information on how the CFB voted can be found on the website where quarterly voting reports are posted.

Supply Chain Issues (Including Debt Relief and Fair Trade)
The CFB met with Tearfund during the year to hear about their tax justice campaign in coalition with other non-government organisations. Transparency related to corporate tax payments is exercising increasing attention from civil society. We encourage companies to manage their tax affairs efficiently, whilst noting the economic justice issues arising from those that avoid tax.

The Committee noted a project backed by UK retailers to provide accessible banking for India’s lowest paid. In a single year the scheme has attracted 58,000 account holders in five cities through 74 street kiosks. One of the principal backers is fast-fashion chain Primark, owned by Associated British Foods, which is encouraging its suppliers to introduce electronic pay rolls.

Environment
During 2011 the CFB has maintained close contact with BP as it rebuilds confidence following the Deepwater Horizon tragedy in the Gulf of Mexico in which 11 people died and causing widespread ecological damage. The Committee welcomed CFB participation in the coalition of faith and other investors working for both an improved safety regime and improved shareholder communications. Given the progress made by BP as it attempted to restore the Group’s reputation, it was decided that a shareholder resolution would not be appropriate at the 2011 meeting. The CFB along with 43% of registered proxies voted against the re-election of the Chair of the Safety, Ethics and Environmental Assurance Committee on whose watch the accident happened. Subsequently, his retirement from the BP Board in April 2012 was announced.

The Committee also noted ongoing engagement with Royal Dutch Shell on a range of operational issues. The company admitted liability for two spills in the Niger Delta following a claim brought against the company by the Bodo Community through the UK courts. The Committee welcomed Shell’s decision to accept liability. CFB also participated in a sustainability day for responsible investors where the Group
results on environment and safety were presented. The Committee also noted Shell’s prompt clean up response to a leak on the Gannet Alpha Platform in the North Sea.

Prior to the Rio Tinto AGM in April, the Committee noted a CFB meeting with activists from the USA and Indonesia who were in London to engage with investors about the company’s operations. The matters raised formed the basis of a detailed meeting with Rio Tinto later in the year which covered operations in various locations as well as reviewing the process for embedding sustainability in the development of new mine sites.

During the year Glencore, a Swiss domiciled mining and commodities trading company listed in London becoming the largest flotation in UK history. The Committee welcomed ecumenical engagement with Glencore around sustainability, and especially on safety, which was judged to be below industry best practice. As the CFB policy is only to consider extractive companies for investment once it has been confirmed they comply with ‘best industry practice’, Glencore was not included in the universe of acceptable companies. The Committee recognised that the announcement that Glencore might seek a merger with Xstrata, would require further considerable work to determine if the combined entity meets CFB ethical requirements, given Xstrata is a current holding.

Several other mining companies entered the index during the year, none of which met ethical due diligence requirements and were excluded from investment by the CFB. These were Bumi, Evraz, Polymetal and New World Resources.

The Committee noted publication of an Institutional Investor Group on Climate Change document, ‘Institutional Investors Expectations of Corporate Climate Change Management’, as a useful tool for engaging with companies around climate change risk.

House builders are well placed to apply cutting edge energy and water saving technologies within the residential sector. The Committee welcomed the 2011 results of sustainability benchmarking in the house building sector which showed that several CFB holdings and in particular Berkeley Group and Taylor Wimpey, scored well against their peers.

Gambling

The CFB excludes companies principally involved in betting and gambling. During the year one company involved extensively in gambling, Perform Group, entered the index and was excluded. The CFB regularly monitors the small exposure to gambling at BSkyB via its online platform, and raised the subject when it met with the company.

Medical and Food Safety Issues

JACEI members and other faith investor representatives attended a meeting organised by CFB with GSK in which an extensive range of issues were raised including clinical trials in emerging markets, pricing and marketing and carbon management.

The Committee welcomed continued engagement with Nestlé during the year. Staff from CFB and the Joint Public Issues Team (JPIT), met with Nestlé UK staff and discussed cocoa and coffee initiatives. A half day expert seminar with key personnel from Switzerland was also attended to look specifically at water management and scarcity issues.

Methodism is strongly represented in the FTSE4Good consultation process on breast milk substitutes that saw Nestlé enter the FTSE4Good Index in March 2011. As part of this process Nestlé was audited in two ‘high-risk’ countries (India and Zambia) during the year. JPIT is represented on a working group of interested NGOs and others that have also reviewed this work. A member of the CFB team sits on the FTSE4Good Expert Committee on Breast Milk Substitutes, which monitors the process, the audits, and recommends inclusions or exclusions to the Index.

The Committee noted correspondence with Christian Ecology Link, which enquired about CFB investment policy towards investing in agricultural chemicals, intensive factory farming and GMOs. A policy on ethical issues relating to the food industry was published in November 2005, and such issues are routinely raised when engaging with food producers. CFB staff attended an UKSIF briefing on animal welfare issues relating to investment.

Human Rights

The UN Secretary General’s Special Representative on the issue of human rights and transnational corporations, Professor John Ruggie, produced his final report on Guiding Principles for Business and Human Rights during the year. This is a significant landmark and all businesses whose activities have a real or potential impact on human rights should take note. The published ‘norms’ have three guiding elements to:

- **Protect** - the State has a duty to protect against human rights abuses by third parties, including business, through appropriate policies, regulation, and adjudication;

- **Respect** - the corporate responsibility to respect human rights, which means to act with due diligence to avoid infringing the rights of others and to address adverse impacts that occur; and

- **Remedy** - both State and business responsibility to provide greater access by victims to effective remedy, both judicial and non-judicial.

The Committee welcomed this important contribution to thinking around business and human rights.

The Committee noted the challenges faced by Vodafone when it was forced to issue pro-government messages during the Egyptian uprising, and subsequently to shut down its network. The company proactively met with human rights organisations to discuss how it can mitigate against similar action elsewhere when faced with ‘freedom of expression’ challenges.
The considerable focus on trafficking and the Olympics is reported elsewhere (Page 5). The Committee supports and welcomes the resource allocated to this area of work which affects some of the most vulnerable and invisible in society.

Media

As part of its work on trafficking, the Committee was made aware that the Metropolitan Police recognise that publishing small ads for sexual services in regional and local newspapers can be a front for trafficking. Work has just commenced to review whether this activity takes place within any newspaper investment held by the CFB, with a view to engaging with the groups concerned.

The Committee’s main focus for media during the year has been in developing a standalone Policy Statement on Pornography (page 4). As part of this work, the Committee welcomed the Bailey Report on the sexualisation of children, believing it made a helpful and timely contribution on the proliferation of sexual imagery in the media.

2011 was dominated by the phone hacking scandal, and the role of the media in engaging in actual and quasi criminal activity to garner stories. The crisis led to the closure of the News of the World, published by News International and the setting up of the Leveson Enquiry to examine press standards and the relationship the media has with politicians, the police and other public figures. All this the Committee welcomed. A free, investigative press is vital for a free society, but it comes with the responsibility to act in the public interest and to resist prurience, intrusion and invasion of privacy purely for commercial gain. Although the CFB has no direct exposure to the holding company, News Corporation, the Committee noted international ecumenical activity, condemning the activities of News International. The Committee appreciated receiving a briefing on the outcome of the AGM at which a representative of the Church of England’s Ethical Investment Advisory Group had spoken.

Networking

The CFB reported that it had had contact with overseas church bodies including the General Board of Pension and Health Benefits of the United Methodist Church (GBPHB), the Uniting Church of Australia, the Methodist Church in New Zealand, the Mennonite Church in Canada and the Christian Brothers. Mr Graeme Rough of the Uniting Church of Australia attended the September 2011 meeting of JACEI and Ms Laura Berry, Executive Director of the Interfaith Centre for Corporate Responsibility (ICCR) attended the November 2011 meeting. The Committee was also delighted to welcome to the September meeting Mr Kasta Dip, Co-ordinator Justice, Peace and Reconciliation of the Church of North India.

The Committee was delighted to welcome reciprocal observer status with the Church of England Ethical Investment Advisory Group with the EIAG Chairman and Secretary attended the March 2012 JACEI meeting.

The Committee was interested to note the new GBPHB policy on investment in private prisons, whereby investment would be proscribed in companies deriving more than 10% of revenue from the management and operation of prison facilities.

The CFB was actively involved in the Church Investors Group (CIG) and the Committee particularly commended the initiative to convene an international meeting of faith investors in Paris. Other important partnerships include the Institutional Investors Group on Climate Change (IIGCC), the Carbon (and Water) Disclosure Projects (CDP), the UN Principles for Responsible Investment (UNPRI) and the Extractive Industries Transparency Initiative (EITI).

Other contacts included the Ecumenical Council for Corporate Responsibility (ECCR) where a Connexional Team member sits on the Board, and UKSIF (UK Sustainable Investment & Finance). The CFB uses the specialist services of EIRIS, PIRC, Glass Lewis & Co and Trucost.

The Committee commended the important input on a variety of subjects made by the Connexional Team at Methodist Church House.

The CFB Ethical Review

The CFB voting records (UK and European), ethical overview of UK sectors, list of ethically excluded European and UK companies (approx 9.3% of the Eurofirst 300 ex-UK Index and 14.6% of the FTSE All Share Index, respectively) and minutes of the monthly CFB ethics meeting were all noted.

The ethically adjusted index underperformed the FTSE All Share Index by 1.1% in the year to 29 February 2012 and by 0.6% pa over both three and five years.

A significant number of CFB reports and reviews of individual companies were received during the year including notes of meetings with Anglo American, Rio Tinto, Barclays, Royal Bank of Scotland, Whitbread, InterContinental Hotels Group, Tesco, Nestlé, GSK, HSBC, Xstrata and Glencore.
Appendix - Role and Function of the Committee

Terms of Reference

The Joint Advisory Committee on the Ethics of Investment (JACEI) was established in 1983 by a Resolution of the Methodist Conference to provide a mechanism for the Methodist Church to tackle ethical dilemmas associated with investment and report annually to the Conference. Its terms of reference, which were last revised in 2001, are as follows:

The Joint Advisory Committee of the Ethics of Investment shall have a Chair appointed by the Methodist Council. The Committee shall have five members appointed by the Central Finance Board of the Methodist Church (CFB) and five members appointed by the Methodist Council. The function of the Committee shall be:

- to advise the CFB of ethical considerations relating to investment, it being accepted that the CFB legally has responsibility for making the final decision on the purchase or disposal of any share;
- to make public where appropriate any ethical policy of the CFB and in particular any investment decision taken on ethical grounds and any other advice the Committee may provide on ethical matters relating to investment;
- to report to the Conference on the workings of the Committee and in particular to comment on the performance of the CFB in managing the funds under its control according to an ethical stance which is in accordance with the aims of the Methodist Church.

JACEI Procedures

The latest procedural amendments (2008) agreed that each meeting should have:

- one or two major items for debate either previously agreed by the Committee, requested by the CFB or driven by events;
- regular reporting items to keep the Committee fully informed of ethical issues relating to investment and to assist in the selection of items requiring a major debate;
- a report from the CFB on its ‘ethical performance’. This would include the EIRIS screen, voting records and any disinvestment on ethical grounds.

That the Committee should:

- hold four meetings a year (in 2011/12 these took place in June, September, November and March);
- have its own identity with an address located at Methodist Church House;
- advise the CFB in relation to current Methodist Church policy;
- examine all aspects of a company’s operations rather than simply focus on one particular issue;
- take responsibility, where appropriate, for making public any ethical policy of the CFB and in particular any investment decision taken on ethical grounds;
- seek ways to make the advice provided by the Committee available to the wider Methodist Church.

That Committee members should:

- feel free to contact the Secretary between meetings about issues of concern to them;
- email their comments on position papers or other matters to the Secretary if unable to attend a particular meeting.

SRI Reporting Requirements

In July 2000 regulations came into force obliging pension funds to consider their policy, if any, on socially responsible investment (SRI). In April 2005 similar requirements were extended to charities under the SORP guidelines. The UK Stewardship Code, published in July 2010 provides further clarity on reporting by investors. The CFB is investment manager to large pension funds that use the JACEI Conference Report as part of their assessment of CFB compliance with their SRI policies. The report should therefore enable trustee bodies to assess clearly whether the CFB has operated in a way consistent with the aims of the Methodist Church.
Committee Membership

The Revd John Howard is the Chair of the Committee.

Members nominated by the Methodist Council are: Professor David Clough, Dr Brian Gennery, Ms Alison Jackson, Mr Chris Moorhouse, and Ms Rachel Lampard

Nominated by the Central Finance Board (CFB) are: Dr Keith Aldred, Mr Alan Emery, Mr Bill Seddon, Mr Roger Smith, and Mr Terry Wynn (from September 2011)

The Revd Winston Graham attends as a representative of the Trustees of the Methodist Church in Ireland.

In attendance from time to time to facilitate the workings of the Committee were: Mr Russell Sparkes, Mr Miles Askew, Mr Stephen Beer, Mr Christophe Borysiewicz, Mr Stephen Hucklesby and Ms Kate McNab.

Mr Neville White is the JACEI Committee Secretary neville.white@cfbmethodistchurch.org.uk

The Committee agreed that a member of the Ethical Investment Advisory Group of the URC could attend as an observer, and Mr Frank Kantor was invited to attend from time to time in this role.

The Committee agreed a reciprocal arrangement with the Church of England Ethical Investment Advisory Group during the year, whereby representatives of JACEI and the EIAG would attend as observers of each other’s meetings.

(Enquiries about the Committee’s work are encouraged, with letters to be addressed to the Committee’s Chair c/o 25 Marylebone Road, London NW1 5JR, or by email to: jaceichair@methodistchurch.org.uk).