Harvard University

Corporation Committee on Shareholder Responsibility

Annual Report, 2008-09

CCSR Members:

Robert D. Reischauer, Chairman
James R. Houghton
Patricia A. King

Secretary to the Committee:

Elizabeth A. Gray

December, 2009
Corporation Committee on Shareholder Responsibility  
2009 Annual Report  

Introduction  
In 1972 Harvard established two committees to assist the University in addressing its ethical responsibilities as a large institutional investor: the Corporation Committee on Shareholder Responsibility (CCSR) and the Advisory Committee on Shareholder Responsibility (ACSR). The CCSR consists of three members of the Harvard Corporation. Acting on behalf of the President and Fellows, it decides how Harvard's shares should be voted on issues of social responsibility and oversees the consistent application of University policy with respect to investments in certain sectors and precedent, actively considering new circumstances or information that may suggest changes in policy or practice. The ACSR, a twelve-member committee made up of Harvard faculty, students and alumni, is responsible for analyzing proxy issues and making recommendations on how Harvard should vote its shares. This investigation of issues and communication of analysis is a central function of the ACSR, which provides the CCSR with the reasons underlying each recommendation, including the rationale for divergent views on how the University should vote. From time to time the ACSR has also suggested new policy approaches regarding investments or proxy voting. The purview of these two committees encompasses the range of issues of social responsibility that are put before corporate shareholders. Shareholder proposals addressing corporate governance matters are decided by the Harvard Management Company.  

During the 2009 spring proxy voting season (the period between March and June when most publicly-traded corporations hold annual meetings), the Committees considered nineteen proposals dealing with issues of social responsibility that were addressed to corporations whose securities were owned by Harvard. Issues raised through the proxy process this year included corporate environmental practices; company efforts to address global warming; the use of genetically engineered organisms in food products; health care reform; equal employment and diversity; military contracting; corporate political contributions; animal welfare; and executive compensation in relation to issues of social responsibility. (For a list of both Committees' votes by company, see Appendix A.)  

The following report provides a detailed description of the ACSR’s recommendations and the CCSR’s votes on shareholder proposals that came to vote during the 2009 proxy season. The report also provides a description of the University's policies with regard to oil companies doing business in Sudan (see Appendix B) and to firms involved in the sale and manufacture of tobacco products (see Appendix E).
I. 2009 Proxy Season

During the 2009 proxy season, the University voted on shareholder proposals addressing a wide range of social issues. The University’s approach to proxy voting is to consider each proposal on a case-by-case basis in the light of the ACSR’s discussions and CCSR precedent on comparable issues. The ACSR’s analysis of proxy issues is supported by background material provided by RiskMetrics Group, a financial risk management company that provides institutional investors with analyses of issues of social concern and corporate responsibility raised through the proxy process. Because the CCSR’s role emphasizes consistency in applying precedent, and the ACSR is responsible for keeping abreast of new information or circumstances which may suggest taking a different position, the ACSR is often a leading indicator for change on shareholder issues.

While the two Committees occasionally disagree on the appropriate response to a shareholder proposal, the voting pattern over a period of years shows a high percentage of agreement. Of the nineteen proposals considered by the Committees during the 2009 proxy season, the ACSR and the CCSR were in complete agreement on seventeen proposals (89.5%), and the Committees partially agreed (e.g., one Committee abstained while the other voted against or in favor of the proposal) on two (10.5%).

<table>
<thead>
<tr>
<th>Year</th>
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<td>111</td>
</tr>
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<td>2009</td>
<td>19*</td>
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</table>

* Due to changes in asset allocation in effect during the 2009 proxy season, the ACSR considered only 19 proxies.

A. Environment

For many years, corporate policies and practices related to the environment have been of particular interest to shareholders. In 2009, the University voted on five proposals related to this topic. Below is a detailed account of the ACSR’s recommendations and the CCSR’s votes on each of the proposals.
1. Climate Change

The shareholder campaign on climate change began in 1994. Resolutions on this topic outnumbered any other single issue in 2009 and received a high percentage of shareholder support. This year, Harvard voted on three proposals to Exxon Mobil related to the issue of global warming. The first proposal addressed the possibility that new regulations regarding greenhouse gas emissions, such as those proposed by the Obama Administration, may increase corporate responsibility for reducing such emissions. The resolution asked Exxon Mobil to

“adopt quantitative goals, based on current technologies, for reducing total greenhouse gas emissions from the Company’s products and operations; and that the Company report to shareholders by September 30, 2009, on its plans to achieve these goals. Such a report will omit proprietary information and be prepared at reasonable cost.”

The ACSR unanimously voted (9-0-0) to recommend support, viewing the proposal as a reasonable request that Exxon Mobil follow the lead of its competitors and take action to address the company’s own conduct with regard to greenhouse gas emissions. They believe that that such action is likely to be mandated by legislation in the near future, and that adoption of the proposal would benefit the company from a public relations standpoint. The CCSR abstained, recognizing the recent shift in ACSR position from opposition to support for this type of proposal. In the past, both Committees have been reluctant to endorse proposals that call on companies to adopt quantitative goals.

The second resolution called on Exxon Mobil to

“establish a task force, which should include both (a) two or more independent directors and (b) relevant company staff, to investigate and report to shareholders on the likely consequences of global climate change between now and 2030, for emerging countries, and poor communities in these countries and developed countries, and to compare these outcomes with scenarios in which Exxon Mobil takes leadership in developing sustainable energy technologies that can be used by and for the benefit of those most threatened by climate change. The report should be prepared at reasonable expense, omitting proprietary information, and should be made available to shareholders by March 31, 2010.”

The ACSR voted 2-5-1 to recommend opposition. Opposing members think it is inappropriate to ask the company to undertake research on the possible consequences of climate change, and that scientific organizations are better sources for this type of research. They believe the resulting report would be of questionable value, since there could always be questions about the accuracy and impartiality of such research undertaken by a corporation that has an interest in the outcome. Some opposing members also questioned the value of research on climate change that is limited to specific communities. ACSR members recommending support view the proposal as a reasonable request that the company review existing research on global warming and use the findings of that research in the development of future business strategies. They point out that Exxon Mobil’s “Outlook for Energy” report is vague and does
not address the effects of climate change on the communities that are most likely to be impacted. The abstaining member is sympathetic to the concerns raised by the proponents, but agrees with opposing members that the requested report would be of limited value to shareholders.

The CCSR voted against the proposal following ACSR recommendation. As opposing members point out, there are better sources for research on the likely consequences of climate change, and asking Exxon Mobil to undertake such research could politicize the results of the study.

A final related proposal addressed the issue of renewable energy. According to RiskMetrics, Exxon Mobil has taken the position that, as an oil and gas business, its expertise is not in renewable energy, and that for the foreseeable future renewable sources will account for only a small portion of the world’s increasing energy needs. The company intends to focus its resources on the development of low-emission technologies for oil and gas. The proponents are concerned that the company is unprepared for possible major shifts in U.S. energy policy, and believe that Exxon Mobil could play a significant role in the development of renewable energy technology. The resolution called on the company to

“adopt a policy for renewable energy research, development and sourcing, reporting on its progress to investors in 2010.”

The ACSR voted 7-2-0 to recommend a vote in favor. Supporting members believe it would be prudent for Exxon Mobil to give greater consideration to alternative energy sources given the likelihood of new regulations at both state and federal levels requiring companies to reduce greenhouse gas emissions. They further point out that the company’s competitors have invested significantly more in this area, and are concerned that Exxon Mobil could lose its competitive edge if the market shifts away from oil-based energy. Opposing members believe the request is extreme in requiring the company to adopt a policy on renewable energy, especially in light of the company’s stated position on the issue. The CCSR voted in favor of the proposal following ACSR recommendation.

2. Recycling

A group of shareholders would like PepsiCo to review its recycling program and to develop goals for increasing beverage container recovery rates. They argue that both recycled content and container recovery goals are essential to an effective recycling strategy. The resolution called on PepsiCo to

“review the efficacy of its container recycling program and prepare a report to shareholders, by September 1, 2009, on a recycling strategy that includes a publicly stated, quantitative goal for enhanced rates of beverage container recovery and recycling in the U.S. The report, to be prepared at reasonable cost, may omit confidential information.”
The ACSR unanimously voted (10-0-0) to recommend support of the proposal. Members noted that recycling rates in the U.S. have been steadily declining. At the same time, PepsiCo continues to oppose container deposit systems, has not put forward a plan to increase container recovery rates, and is lagging behind its competitors in efforts to increase the use of recycled content in its beverage containers. ACSR members believe that the company should be encouraged to be more proactive in its efforts to encourage recycling, and cited strong precedent in support of an identical proposal to the company last year. The CCSR voted in favor following ACSR recommendation and precedent.

3. Gene-Engineered Crops

Although federal agencies with oversight responsibility of gene-engineered (GE) crops have determined that they pose no risk to human health or the environment, questions remain about their safety and many scientists are concerned that bioengineered plants may contaminate non-bioengineered species. Critics of bioengineering have also argued that unexpected or unintended changes (such as allergenic reactions) could arise in gene-modified plants. The proponents of a resolution to PepsiCo are concerned that current regulatory systems do not sufficiently address these concerns, and given the likelihood that PepsiCo’s products—which include corn, wheat, and soy—contain GE ingredients, they would like the company to

“review Company policies and procedures for monitoring genetically engineered (GE) products and report (at reasonable cost and omitting proprietary information) to shareholders within six months of the annual meeting on the results of the review, including:

(i) potential of GE contamination to affect Company product integrity;
(ii) contingency plans for removing GE ingredients from the company’s products should circumstances so require.”

The ACSR voted 8-3-0 to recommend support of the proposal. ACSR members recommending support believe the request is reasonable, especially since PepsiCo operates in many countries that have restrictions regarding the use and labeling of GE products. They believe the development of contingency plans for removing GE ingredients would be in the company’s best interest. Opposing members agree with arguments made against a similar proposal to the company last year: that in the absence of evidence that bioengineered crops are hazardous to health, the request that the company develop such contingency plans is premature. In addition, they believe it would be difficult for PepsiCo to remove all GE ingredients from its products, since most GE crops come from the U.S. and it is likely that a large percentage of prepared foods in this country include some GE ingredients.

The CCSR abstained on the resolution. The proposal’s wording is new, and the ACSR has shifted from unanimous opposition on a similar proposal to the company last year to support for the
current request. Although the resolution does not ask the company to undertake a specific scientific study (outside their expertise), as had last year’s proposal, it continues to call for the development of contingency plans for the removal of GE ingredients from the company’s products—a request that some ACSR members last year thought would be difficult or impossible to implement.

B. Equal Employment

Although federal law prohibits employment discrimination based on race, color, religion, sex, or national origin, there is no federal legislation protecting lesbian, gay, bisexual, and transgender/transsexual workers from discrimination in the workplace. For over ten years, shareholders at Exxon Mobil have criticized the company for its refusal to expand its non-discrimination policy to include sexual orientation and gender identity on its list of protected categories. A resubmitted proposal called on the company to

“amend its written equal employment opportunity policy to explicitly prohibit discrimination based on sexual orientation and gender identity and to substantially implement the policy.”

The ACSR unanimously voted (8-0-0) to recommend support of the proposal, agreeing with past arguments that it is important for companies to include explicit language in their anti-discrimination policies that would prohibit workplace discrimination on the basis of sexual orientation. They noted that Exxon Mobil is one of only three Fortune 500 companies that do not explicitly prohibit discrimination based on sexual orientation in their non-discrimination policies. The CCSR voted in favor of the resolution following ACSR recommendation and precedent of both Committees.

C. Military Issues

Since the early 1970s, faith-based institutional investors have been submitting shareholder proposals that address the ethical issues associated with military contracting. Although foreign military sales are highly regulated by the U.S. government, public information about foreign military sales is difficult to obtain. The proponents of a resolution to Boeing agree with the American Red Cross that increases in availability of arms will result in greater violations of human rights. In addition, they are concerned that the sale of weapons overseas has resulted in a threat to U.S. security. Since the company provides very little information to shareholders regarding such sales, they would like Boeing to

“within six months of the annual meeting, the Board of Directors provide a comprehensive report, at reasonable cost and omitting proprietary and classified information, of Boeing’s foreign sales of weapons-related products and services.”
The ACSR voted 8-4-0 to recommend support of the proposal. ACSR members recommending support believe the proposal raises a general policy concern, and that there is not enough transparency in general about foreign military sales. They note that while Boeing has provided some information about the countries it is selling to, it does not identify the products it is selling. They believe that disclosure could add value to public discourse about foreign weapons sales and may encourage the development of stricter rules regarding disclosure. Some members stressed that the requested report would not be a burden to produce, since the company already is required to gather this information for the government.

Opposing members agree with arguments made on an identical proposal to the company last year that the resolution raises a public policy issue that is better addressed in the legislative arena. They point out that foreign military sales are highly regulated by the government, and that it is inappropriate to ask Boeing to release sensitive information, especially without any indication of wrongdoing on the part of the company. In addition, some opposing members pointed out that the request is vague, since there could be many interpretations of what constitutes a “weapons-related” product. Some members questioned the value of asking a single company to report on its foreign weapons sales, given the large number of defense contractors in the U.S.

The CCSR voted in favor of the resolution following ACSR recommendation and CCSR precedent.

D. Corporate Contributions

1. Political Contributions

For several years, shareholder activists have been concerned about the increasing level of corporate spending in the political process. Despite passage of campaign reform legislation, the amount of money flowing from corporations into the political process is growing steadily. Although companies provide shareholders with some information about their political contributions, there is a general lack of accountability regarding contributions made at the state level or to trade organizations that are used for political purposes. This year, the Committees voted on resolutions to five companies asking for

“a report, updated semi-annually, disclosing the Company’s:

1. Policies and procedures for political contributions and expenditures (both direct and indirect) made with corporate funds.

2. Monetary and non-monetary political contributions and expenditures not deductible under section 162 (e)(1)(B) of the Internal Revenue Code, including but not limited to contributions to or expenditures on behalf of political candidates, political parties, political committees and other political entities organized and operating under 26 USC Sec. 527 of the Internal Revenue Code and any portion of any dues or similar payments made to any tax exempt organization that is used for an expenditure or contribution that, if made directly by the corporation, would not be deductible under section 162 (e)(1)(B) of the Internal Revenue Code. The report shall include the following:
a. An accounting of the Company’s funds that are used for political contributions or expenditures as described above;
b. Identification of the person or persons in the Company who participated in making the decisions to make the political contribution or expenditure; and,
c. The internal guidelines or policies, if any, governing the Company’s political contributions and expenditures.

The report shall be presented to the board of directors’ audit committee or other relevant oversight committee and posted on the company’s website to reduce costs to shareholders.”

The ACSR voted to recommend abstention on the proposals to Boeing (0-3-9), AT&T (0-3-9), CVS (0-1-10), Sprint Nextel (0-1-10), and Norfolk Southern (0-2-9). Although ACSR members unanimously support the goal of greater transparency underlying the proposal, they disagree with part 2.b., which calls on the company to identify employees who participated in decisions regarding political contributions. Most members believe that abstention is the appropriate response to the proposal, since they strongly support greater disclosure with regard to political contributions. Some members recommend a vote against, arguing that the proponents have put forward identical proposals for several years—despite the fact that shareholders have expressed concern about part 2.b. These members believe a vote against, rather than abstention, might send a stronger message to the proponents that the resolution is poorly worded. The CCSR abstained on the resolutions following ACSR recommendation and CCSR precedent.

2. Charitable Contributions

As part of a larger campaign by a group of shareholders to discourage companies from making corporate charitable contributions, PepsiCo was asked to

“provide a semiannual report, omitting proprietary information and at reasonable cost, disclosing: the Company’s standards for choosing which organizations receive the Company’s assets in the form of charitable contributions; business rationale and purpose for each of the charitable contributions; personnel who participated in making the decisions to contribute; the benefits to the Company and beneficiaries produced by Company contributions; and a follow-up confirming that the organization actually used the contributions for the purpose stated.”

The ACSR unanimously voted (0-11-0) to recommend opposition. In voting against the proposal, members noted that PepsiCo already discloses significant information about its contributions on its website, including the organizations to which it donates, the rationale for the donations, and amounts donated. Information about individuals who make decisions about the recipients of contributions is not released, but ACSR members consider that request to be inappropriate and one that could put these individuals at risk. In addition, they agreed with past arguments that the proposal could discourage companies from making charitable contributions. The CCSR voted against the resolution following ACSR recommendation and precedent of both Committees on this type of request.
E. Health Care Reform

In 2008, shareholder activists began a campaign to encourage companies to endorse universal health care. This year, over forty proposals on this topic were brought forward, although almost half were withdrawn after companies agreed to support health care reform. Harvard voted on three such resolutions, which asked the companies to

“adopt principles for comprehensive health care reform (such as those based upon principles reported by the Institute of Medicine):

1. Health care coverage should be universal.
2. Health care coverage should be continuous.
3. Health care coverage should be affordable to individuals and families.
4. The health insurance strategy should be affordable and sustainable for society.
5. Health insurance should enhance health and well being by promoting access to high-quality care that is effective, efficient, safe, timely, patient-centered, and equitable.”

The ACSR voted 3-8-1 to recommend a vote against proposals to Abbott Laboratories, Boeing and Honeywell. ACSR members noted that since all three companies provide adequate health care for their employees, additional action required by the proposal would be limited to endorsing the IOM principles. Opposing members agree with management that the proposal raises a public policy issue. They think the request is unnecessarily prescriptive in pressing the companies to endorse a specific set of principles. Since the principles were developed to direct legislative activity, not corporate activity, they stressed that it is not clear what action the companies are expected to take.

Supporting members believe it is reasonable to ask the companies to take a position on an issue of such critical importance. They argued that U.S. companies are less competitive because of high health care costs, and therefore it is in their best interest to support health care reform. Some argued that a strong corporate consensus on health care reform principles might create a social context for moving forward on this issue.

The CCSR voted against the resolutions following ACSR recommendation and precedent of both Committees.

F. Animal Welfare

Many shareholders are concerned about the treatment of animals that are used to test product safety. The proponents of a new resolution to Abbott Laboratories would like the company to report on its animal testing practices and commit to replacing, reducing, and refining (“3Rs”) the use of animals in all research, except where required by law. The proposal called on the company to
“prepare and issue a detailed report to shareholders by November 30, 2009, incorporating (1) an animal use inventory, including, but not limited to designations by species, numbers, and the nature and purpose of each use (e.g., research and development, efficacy, toxicity), and (2) a written plan with a reasonable timeframe for replacing, reducing and refining the use of animals (“3Rs”) in all research, development and testing, where not otherwise mandated by law. The report should address animal use in all of the Abbott’s research, development and testing conducted by in-house or contracting laboratories. Finally, the Board should consider creating a management position committed solely to ensuring Abbott’s realization of the 3Rs.”

The ACSR voted 1-11-0 to recommend a vote against the proposal. ACSR members recommending a vote against noted that Abbott has an existing policy that includes adherence to the 3Rs, has met or exceeded U.S. regulations regarding the treatment of animals, and has received a number of awards for its animal care practices. In addition, Abbott already provides substantial information about its policies and practices on its website. Given the company’s positive track record, and the fact that it has already adopted the 3Rs, opposing members saw no reason to support the proposal. The supporting member suggested that the report would be of interest to shareholders and would not be a burden to prepare. The CCSR voted against the resolution following ACSR recommendation.

G. Executive Compensation

Since the 1980s, shareholders have expressed concern about the excessive compensation packages offered to top executives and the widening gap between executive compensation and the wages paid to lower level employees. Past resolutions have attempted to create a link between executive compensation and a company’s performance in addressing a variety of social concerns. This year, Harvard voted on two executive compensation proposals brought before Exxon Mobil. The first called on the company to

“initiate a review of our company’s executive compensation policies and make available, upon request, a report of that review by December 1, 2009 (omitting confidential information and prepared at a reasonable cost). We request the report include:
1. A comparison of the increase in the total compensation package of our CEO between 1998 and 2008 with the increase in the average US per capita income during that same period.
2. An analysis of changes in the relative size of the gap between the two groups and the rationale justifying this trend.”

The ACSR voted 0-7-1 to recommend opposition to the proposal. Although opposing members agree with the proponents that executive compensation is excessive, they noted that the company already provides a thorough report on CEO pay in its proxy statement. They saw no reason to request an additional report on this issue, and did not see the value of asking for a comparison of the pay packages of top executives and U.S. per capita income. The CCSR voted against the resolution following ACSR recommendation and precedent of both Committees.
A second related proposal was brought forward by a group of shareholders who are opposed to Exxon Mobil’s sponsorship of the Masters Golf Tournament, an event that is hosted by an organization that excludes women from membership. The proponents believe that the company’s anti-discrimination policy, which is extended to contractors, should similarly apply to sponsorships and executive privileges (perks). The resolution called on the company to

“conduct a special review of Exxon Mobil’s antidiscrimination statement as it pertains to corporate sponsorships and executive perks and publish a summary report addressing the following:
1) What company funds are presently expended on corporate sponsorships and executive perks, like country club memberships and entertainment at or in conjunction with institutions that discriminate against groups protected by the company’s antidiscrimination statement?
2) Would the company sponsor an event held at a venue barring African Americans, Jews or homosexuals from membership?
3) How is the company’s antidiscrimination statement applied to decisions concerning sponsorships and executive perks?

The report, prepared at reasonable cost and omitting proprietary information, shall be available to shareholders upon request no later than December 1, 2009.”

The ACSR voted 5-3-0 to recommend support. ACSR members recommending support believe that the provision of the requested information would clarify the company’s basis for making decisions about corporate sponsorships and executive perks, and might encourage greater consideration of issues of discrimination. Opposing members were concerned both about the language of the proposal and their understanding of the intentions of the proponents to influence decisions about corporate sponsorship of events. The CCSR voted in favor of the resolution following ACSR recommendation.

Conclusion

The CCSR would like to extend its thanks to members of the Advisory Committee for their contributions to the analysis of the issues presented by the 2009 proxy season, and looks forward to working with new and continuing members of the ACSR in the coming year. The ACSR’s role in providing analysis of proxy issues and recommendations for voting has proved invaluable to the CCSR in voting the University’s shares and developing investment policy over the years. The CCSR would also like to extend special thanks to retiring members of the ACSR, and to express particular gratitude for the leadership of Professor Allen Ferrell, who in 2009 completed his two-year term as Chairman.
### Appendix A

#### 2009 Proxy Season Summary

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<th>Company</th>
<th>Resolution</th>
<th>ACSR Vote</th>
<th>CCSR Vote</th>
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<td>1. Boeing</td>
<td>Report on foreign military sales</td>
<td>8-4-0</td>
<td>In favor</td>
</tr>
<tr>
<td>2. Abbott Labs</td>
<td>Adopt principles for health care reform</td>
<td>3-8-1</td>
<td>Oppose</td>
</tr>
<tr>
<td>3. Boeing</td>
<td>Adopt principles for health care reform</td>
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<td>4. Honeywell</td>
<td>Adopt principles for health care reform</td>
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<td>Oppose</td>
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<td>5. Abbott Labs</td>
<td>Report on plans to eliminate animal testing</td>
<td>1-11-0</td>
<td>Oppose</td>
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<tr>
<td>6. Boeing</td>
<td>Report on political donations and policy</td>
<td>0-3-9</td>
<td>Abstain</td>
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<tr>
<td>7. AT&amp;T</td>
<td>Report on political donations and policy</td>
<td>0-3-9</td>
<td>Abstain</td>
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<td>8. PepsiCo</td>
<td>Increase container recycling/recycled content</td>
<td>10-0-0</td>
<td>In favor</td>
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<td>9. PepsiCo</td>
<td>Report on gene-engineered food</td>
<td>8-3-0</td>
<td>In favor</td>
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<td>10. PepsiCo</td>
<td>Disclose charitable contributions</td>
<td>0-11-0</td>
<td>Oppose</td>
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<td>11. CVS</td>
<td>Report on political donations and policy</td>
<td>0-1-10</td>
<td>Abstain</td>
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<td>12. Norfolk Southern</td>
<td>Report on political donations and policy</td>
<td>0-2-9</td>
<td>Abstain</td>
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<td>13. Sprint Nextel</td>
<td>Report on political donations and policy</td>
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<td>Report on climate change leadership benefits</td>
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<td>15. Exxon Mobil</td>
<td>Develop renewable energy alternatives</td>
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<td>Set GHG emissions reduction goals</td>
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<td>Review executive pay; consider social link</td>
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<td>18. Exxon Mobil</td>
<td>Review executive perks and sponsorships</td>
<td>5-3-0</td>
<td>In favor</td>
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<tr>
<td>19. Exxon Mobil</td>
<td>Adopt sexual orientation anti-bias policy</td>
<td>8-0-0</td>
<td>In favor</td>
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Appendix B

Harvard's Investment Policy with Regard to Oil Companies Operating in Sudan

In 2005, the CCSR recommended to the Harvard Corporation that the University divest itself of stock held in PetroChina Company Limited (PetroChina), a Chinese oil company with major interests in Sudanese oil production. This decision was made in light of the analysis presented in the spring of 2005 by a subcommittee of the ACSR. In 2006, the CCSR further recommended that the University divest itself of stock held in China Petroleum and Chemical Corporation (Sinopec Corporation). The Corporation’s decision to divest these companies reflected deep concerns about the grievous crisis that persists in the Darfur region of Sudan and about the role of these companies in the production of oil in Sudan. The CCSR concluded that the considerations that led the University to divest its PetroChina holdings in April 2005 militated in favor of divestment of holdings in Sinopec Corporation. (See Appendices C and D for the full text of the CCSR Statements on PetroChina and Sinopec.)
Appendix C

Statement by Harvard Corporation Committee on Shareholder Responsibility (CCSR)
Regarding Stock in PetroChina Company Limited
April 4, 2005

We are announcing today the Harvard Corporation’s decision to direct Harvard Management Company (HMC) to divest itself of stock held by HMC in PetroChina Company Limited (PetroChina).

This decision reflects deep concerns about the grievous crisis that persists in the Darfur region of Sudan and about the extensive role of PetroChina’s closely affiliated parent company, China National Petroleum Corporation, as a leading partner of the Sudanese government in the production of oil in Sudan. Oil is a critical source of revenue and an asset of paramount strategic importance to the Sudanese government, which has been found to be complicit in what the U.S. Congress and U.S. State Department have termed “genocide” in Darfur and what a United Nations commission of inquiry recently characterized as “crimes against humanity and war crimes . . . [that] may be no less serious and heinous than genocide.”

Although Harvard maintains a strong presumption against the divestment of stock for reasons unrelated to investment purposes, we believe that the case for divestment in this instance is persuasive, in view of the confluence of circumstances summarized below, under the heading “Recommendation to Divest from Petrochina.”

The Corporation, on our recommendation, has reached this decision in light of the advice of the University’s Advisory Committee on Shareholder Responsibility (ACSR) to divest from PetroChina. The ACSR is comprised of four faculty members, four students, and four alumni. We asked the ACSR to study the issue and offer its advice to us after concerns had been expressed by members of the Harvard community about PetroChina and the situation in Darfur. We are especially grateful for the efforts of an ACSR subcommittee chaired by Joseph Badaracco, Shad Professor of Business Ethics and former chair of the ACSR. The subcommittee, after hearing from representatives of the group urging divestment from companies doing business with Sudan and otherwise inquiring into the circumstances, prepared a report that thoughtfully addresses the relevant considerations, and we therefore quote from it at length below.

The Crisis in Darfur

The ACSR subcommittee report begins by describing the grave situation in Darfur:

A grievous crisis exists in the Darfur region of Sudan. In March 2004, the United Nations humanitarian coordinator for Sudan described the situation in Darfur as an instance of “ethnic cleansing” and “the world’s greatest humanitarian crisis.” In July 2004, both houses of the United States Congress passed a resolution declaring the atrocities in Darfur to constitute genocide. In September 2004, U.S. Secretary of State Colin S. Powell similarly declared that genocide has been committed in Darfur, for which the Sudanese government and the so-called Janjaweed militia groups bear responsibility.
On January 25, 2005, a special UN commission of inquiry, while stopping short of declaring that “genocide” is underway in Sudan, concluded that “the Government of the Sudan and the Janjaweed are responsible for serious violations of international human rights and humanitarian law amounting to crimes under international law,” including “killings of civilians, torture, enforced disappearances, destruction of villages, rape and other forms of sexual violence, pillaging and forced displacement, throughout Darfur.” It stated that such acts have been “conducted on a widespread and systematic basis,” and that “the crimes against humanity and war crimes that have been committed in Darfur may be no less serious and heinous than genocide.”

Numerous other observers have condemned the Sudanese government for complicity in actions that have reportedly resulted in the deaths of more than 70,000 Sudanese civilians (some estimates are far higher) and the displacement of 1.5 million more. [See note below, regarding a more recent and much higher estimate of death toll.] There have also been reports linking oil production activities in Sudan directly to mass displacement of civilians and other human rights abuses. The grave situation in the Darfur region persists, notwithstanding the recent signing of a peace accord to end the longstanding north-south civil war in Sudan, and several rounds of negotiations concerning Darfur.

Note: On March 29, 2005, after the ACSR subcommittee had completed its report, a British parliamentary report stated that the death toll in Darfur may be as high as 300,000.

The importance of oil to the Sudanese government, and the involvement of CNPC

The ACSR report also discusses the central importance of oil to the governing regime in Sudan, as well as the extensive involvement of China National Petroleum Corporation, the parent company of PetroChina, in the production of Sudanese oil:

Oil production is widely understood to be a crucial source of revenue for the Sudanese government, essential to the government’s capacity to fund military operations, and an asset of exceptional strategic importance to the regime. According to a recent report of the U.S. Department of Energy, “With the start of significant oil production (and exports) beginning in late 1999, . . . . Sudan’s economy is changing dramatically, with oil export revenues now accounting for around 73% of Sudan’s total export earnings.” [Energy Information Administration, U.S. Department of Energy, Sudan Country Analysis Brief, July 2004.] As of January 2004, Sudan’s estimated proven reserves of crude oil stood at 563 million barrels, more than twice the 2001 estimate. As of June 2004, crude oil production had risen to 345,000 barrels per day, up from 270,000 barrels per day just a year earlier. [Ibid.]

The China National Petroleum Corporation (“CNPC”) is wholly-owned by the Chinese Government[. CNPC] conducts oil operations in Sudan. CNPC is the largest single shareholder of the Greater Nile Petroleum Operating Company (“GNPOC”), a consortium that “dominates Sudan’s oil fields.” [“China Invests Heavily in Sudan’s Oil Industry,” The Washington Post, December 23, 2004 (Post article).] GNPOC was created by the Sudanese government and includes, among its joint venturers, the Sudanese state-owned oil company, Sudapet. (United States investors are prohibited by
U.S. sanctions law from investing in the GNPOC joint venture.) CNPC recently reported that its production of crude oil in Sudan exceeded 16 million tons in 2004, which appears to account for a substantial fraction of its total foreign oil production.

It has also been observed that the production of Sudanese oil has been a matter of attention within the United Nations Security Council in discussions of possible international sanctions against Sudan based on the situation in Darfur, and that substantial revenue from Sudan’s oil production has gone toward the purchase of weapons.

**CNPC and PetroChina**

The ACSR report also addresses the relationship of CNPC to PetroChina:

In April 1999, CNPC announced its plans to sell $10 billion shares on the New York Stock Exchange. Human rights groups and others objected to the initial public offering, contending that the deal would be tantamount to U.S. support for genocide in [southern] Sudan. In response, CNPC restructured the transaction. It created a new subsidiary, PetroChina, which would operate only inside China, to be owned 90% by CNPC and 10% by private investors. On April 6, 2000, $2.9 billion dollars of shares in PetroChina were sold on the New York Stock Exchange to private investors. At that time, CNPC’s investment bankers from Goldman Sachs asserted to investors that none of the money raised in the IPO would be used to fund CNPC’s projects in Sudan. [Post article; China’s Involvement in Sudan: Arms and Oil, Human Rights Watch, November 2003 (Human Rights Watch Report).]

Despite CNPC’s assurances, several potential investors viewed with considerable skepticism CNPC’s firewall strategy. Opponents of the IPO pointed out that when PetroChina was created, it incurred $15 billion in debt from CNPC, some of which was incurred in connection with the GNPOC project. [Human Rights Watch Report.] Fund managers were skeptical that PetroChina could make independent business decisions because CNPC owned 90% of its shares. As a result of these concerns, several major institutions, including such pension funds as TIAA-CREF and Calpers, elected at the time of the IPO not to invest.

Within the past few months, there have been further complaints that “[t]ransparency in the relationship between PetroChina and CNPC is so poor that investors are often in the dark about potential cross-subsidies.” [“Assets Plan for PetroChina in Global Drive,” The Standard, October 25, 2004.]

In an effort to determine whether PetroChina can exercise independence from CNPC despite CNPC’s 90% ownership interest in it, the subcommittee examined the management of the two companies. The results of that review were striking. The Chairman of PetroChina is the President of CNPC; PetroChina’s legal counsel is CNPC’s President; PetroChina’s Vice Chairmen, Executive Directors, and Non-executive Directors are also CNPC’s Vice Presidents; and the four subcommittees of PetroChina’s Board of Directors contain substantial representation from CNPC. Indeed, the investment and development subcommittee of the board of PetroChina is comprised solely of two Vice Presidents of CNPC.
Against this background come new reports that suggest the two companies are contemplating the integration of their operations. According to *The Standard*, “Beijing plans to create an integrated oil giant capable of competing on the global stage with the likes of Exxon-Mobil and Royal Dutch Shell by restructuring PetroChina and its parent China National Petroleum Corp. (CNPC).” [Ibid.] As a result of this contemplated corporate restructuring, PetroChina itself may become the direct owner of substantial oil assets in Sudan now owned by CNPC, or CNPC and PetroChina may establish a joint venture through which they would jointly own such assets.

**The Recommendation to Divest from PetroChina**

Finally, the ACSR report recommends that Harvard divest itself of PetroChina stock, recognizing the strong presumption against divestment for reasons unrelated to investment purposes, but also pointing to the unusual combination of circumstances presented by this particular holding:

The subcommittee understands that Harvard manages its endowment to achieve maximum returns to support the academic purposes and programs of the University, consistent with a prudent level of risk. The University maintains a strong presumption against divesting itself of securities for reasons unrelated to investment purposes, and against using divestment as a political tool or a “weapon against injustice”—not because there are not many worthy political causes or deeply troubling injustices in the world, but because the University is first and foremost an academic institution. During his tenure as president of Harvard, Derek Bok wrote thoughtfully and extensively about the reasons for that approach. His writings are a compelling reminder that the University, as an academic rather than a political institution, must take great care to avoid leveraging its endowment or prestige in ways that could embroil the institution in political and social controversies not directly related to its academic pursuits, and thus compromise the core values and independence of the academic enterprise.

Nevertheless, there are exceptional cases in which the strong presumption against divestment may be overcome. As President Bok noted, “Although trustees have a legal and moral obligation to enhance and conserve the university’s resources, there are rare occasions when the very nature of a company’s business makes it inappropriate for a university to invest in the enterprise.” Typically, in such cases, the act of divestment is not taken with the expectation that it will induce a company to cease its objectionable operations; rather, to paraphrase President Bok, the University simply does not consider it proper to make investments in the enterprise in question.

We believe the unique pattern of circumstances relating PetroChina to the crisis in Sudan counsels in favor of taking the extraordinary step of divestment:

- the declarations by the United States Congress and the U.S. Secretary of State describing the situation in Darfur as involving a “genocide” in which the Sudanese government is complicit;
- the judgment of a United Nations commission of inquiry that the Government of Sudan shares responsibility for “widespread and systematic acts” in Darfur amounting to “crimes against humanity and war crimes . . . [that] may be no less serious and heinous than genocide”;
• the apparent persistence of the crisis in Darfur notwithstanding the recently negotiated peace agreement intended to end the north-south civil war in Sudan and several rounds of negotiations focused on Darfur;

• the salient importance of oil to the Sudanese government as a strategic asset and source of revenue, available to fund military and other operations;

• the reports that oil-related activities themselves have exacerbated the humanitarian crisis in Sudan;

• the magnitude and scope of CNPC’s active involvement in Sudanese oil production activities (especially in GNPOC), the importance of its Sudanese activities in its overall range of foreign oil activities, and CNPC’s status as a direct joint venture partner of Sudapet, owned by the Sudanese government;

• the express inclusion of the GNPOC joint venture on the list of entities with which persons in the United States are prohibited from doing business under U.S. sanctions law;

• CNPC’s 90 percent ownership of PetroChina, and the lack of realistic opportunity for an owner of a small fraction of PetroChina’s publicly traded shares to exercise “voice” in a way that could be expected to exert significant influence on the conduct of CNPC, which is wholly owned by the Chinese government;

• the fact that PetroChina’s Board of Directors is dominated by CNPC’s senior management;

• the recent reports that PetroChina itself may soon become the direct owner of international oil assets (including Sudanese assets) now owned by CNPC, or that CNPC and PetroChina may form a joint venture through which they would jointly own such assets, as a result of a contemplated corporate restructuring.

Conclusion

The CCSR is persuaded, and the Corporation agrees, that this particular combination of circumstances, taken together, warrants the rare step of divestment. We accordingly are directing Harvard Management Company to divest its holdings of PetroChina stock.
We are announcing today the Harvard Corporation’s decision to direct Harvard Management Company (HMC) to divest itself of stock held by HMC in China Petroleum and Chemical Corporation (Sinopec Corporation).

The Corporation, on our recommendation, has reached this decision in light of the analysis presented last spring by a subcommittee of the University’s Advisory Committee on Shareholder Responsibility (ACSR) for divestment from PetroChina Company Limited (PetroChina), another Chinese oil company with major interests in Sudanese oil production, and developments since that decision regarding Sinopec Corporation’s involvement in Sudanese oil production. The decision to divest from Sinopec reflects these new developments as well as deep concerns about the grievous crisis that persists in the Darfur region of Sudan and about the role of Sinopec Corporation and its closely affiliated parent company, China Petrochemical Corporation (Sinopec Group), in the production of oil in Sudan. Oil is a critical source of revenue and an asset of paramount strategic importance to the Sudanese government, which has been found to be complicit in what the U.S. Congress and U.S. State Department have termed “genocide” in Darfur and what a United Nations commission of inquiry has characterized as “crimes against humanity and war crimes . . . [that] may be no less serious and heinous than genocide.”

Having monitored recent developments regarding Sinopec Corporation’s involvement in Sudanese oil production, the CCSR has concluded that the considerations that led us to divest from PetroChina in April 2005 counsel in favor of our now divesting from Sinopec Corporation. Those considerations are set forth in the statement available at http://www.news.harvard.edu/gazette/daily/2005/04/04-sudan_statement.html. With particular regard to Sinopec, the CCSR has further noted the following:

- Sinopec Corporation is a publicly listed company in which a dominant (68%) interest is held by China Petrochemical Corporation (Sinopec Group). Sinopec Group is wholly owned by the Chinese government, and Sinopec Corporation and Sinopec Group have substantially overlapping management.

- Sinopec Corporation is a partner in Petrodar Operating Company Ltd., a consortium whose partners also include China National Petroleum Corporation (CNPC, the 90% owner of PetroChina) and Sudapet (the Sudanese state-owned oil company), among others.

- In August 2005 Petrodar commenced production of oil in blocks 3 and 7 in Southeast Sudan. In December 2005 Petrodar announced that its first shipment of crude oil would be shipped from Sudan in January 2006. Petrodar’s operations represent a major increase in overall Sudanese oil production, with Petrodar’s output expected to reach 250,000 barrels/day by the end of 2006 and to grow to 350,000 barrels/day in 2007.
In November 2005, Sinopec Group announced plans to partner with CNPC to purchase an oil field in Sudan, and has reportedly indicated an interest in expanding its business in Sudan.

**Conclusion**

Although Harvard maintains a strong presumption against the divestment of stock for reasons unrelated to investment purposes, the CCSR is persuaded, and the Corporation agrees, that the particular combination of circumstances bearing on Sinopec Corporation’s involvement in oil production activities in Sudan warrants the unusual step of divestment. We accordingly are directing Harvard Management Company to divest its holdings of Sinopec Corporation stock.
Appendix E

Harvard's Investment Policy with Regard to Tobacco

In 1990 the University completed sales of its stock in a number of companies in the tobacco industry and adopted a policy prohibiting the future purchase of stock in companies producing significant quantities of cigarettes or other tobacco products. These actions followed extensive consideration by both of Harvard's Committees on Shareholder Responsibility of the issues associated with direct investment in the tobacco industry. In 1988 at the urging of the ACSR, the CCSR wrote to portfolio companies in the tobacco industry, asking them to address the ethical responsibilities associated with tobacco sales in developing countries and to provide information on their policies for informing consumers of tobacco-use risks in nations having minimal governmental regulations concerning smoking health risks. In some cases this information was not forthcoming; in others the firms had made considered decisions not to follow the World Health Organization code for tobacco marketing or contested the evidence linking tobacco use with disease. In September of 1989 after reviewing this correspondence, the University reached the decision to sell its holdings in the stock of several companies involved in the manufacture of cigarettes and other tobacco products. This decision was motivated by the University's belief that in this case it would be unable, as a continuing shareholder, to influence the policy of the companies in regard to the marketing practices mentioned above, and by the desire not to be associated as a shareholder with companies engaged in significant sales of products that create a substantial and unjustified risk of harm to human health. The sale of stock was completed early in 1990, and later in the year the ACSR encouraged the University to adopt a formal policy precluding any future purchase of such stock. The Corporation subsequently adopted a policy prohibiting the purchase of stock in companies producing significant quantities of cigarettes or other tobacco products.