US Public Pension Funds and CSR

Responsibility for the developing world?

Öffentliche Pensionsfonds sind eine Marktkraft, mit der Regierungen und Firmen rechnen müssen. Einer der Hauptvertreter von Shareholder-Verantwortung hat versucht, bei Investitionen Umwelt-, soziale und finanzielle Aspekte zu balancieren.

Von Susanne Soederberg

The particular feature of public pension funds, their membership base being comprised of public-sector labour unions, has facilitated an active relationship between its shareowners (labour) and corporate executives through the promotion of good corporate governance principles in the United States (Ghilarducci 2004; Hawley/Williams 2000; Hebb 2001; Blackburn 2003) (1). Unlike private pension funds, CalPERS has attempted to balance social including environmental and financial issues vis-à-vis its investment decisions and strategies.

California Treasurer and CalPERS Board Member, Phil Angelides, argues that 'enduring value' should act a guiding principle for investments as opposed to short-term economic thinking. By this Angelides means 'that the current laissez-faire, let-'er-rip system damages important social values – equitable treatment of workers, the environment and other commonly shared public assets – and that both workers and retirees (and the state taxpayers who put up the money for public pension funds) have a strong self-interest in husbanding the distant future: a healthy society and strong economy for themselves and their families' (Greider 2005).

Extended understanding of corporate governance

By emphasising socially responsible investing practices, CalPERS employs an extended understanding of corporate governance that transcends the short-term oriented behaviour and narrowly defined confines of pure fiduciary responsibilities aimed at ensuring that corporate management and the Board of Directors work toward the Anglo-American principle of maximising shareholder value (Lazonick/O'Sullivan 2000; OECD 2004; Soederberg 2004a).

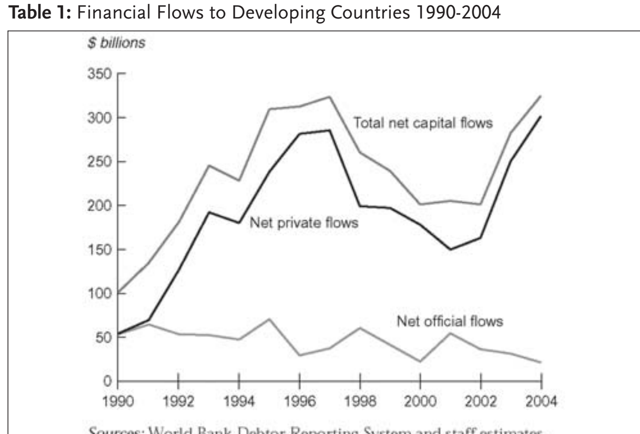
CalPERS' extended view of corporate governance is evident in its Permissible Country Index (herewith PCI), which was devised in 1987. The PCI presents itself as a highly dynamic initiative that interacts and changes with the demands of the ever-changing global economy. It is worth emphasising here that the PCI has teeth. Amid the height of Enron-style scandal in the US CalPERS 'announced that it was going to pull out of all its investments in Thailand, Malaysia, Indonesia and the Philippines mainly because of concerns about social conditions in these countries' (Blackburn 2003: 516; Greider 2005).

CalPERS AND THE PCI

The economic power behind the 3 largest public sector pension funds in the United States are evident by their vast holdings: CalPERS manages over 182 billion Dollar of assets (CalPERS 2005b), the California State Teachers Retirement System, the country's second largest fund, holds another 125 billion Dollar in assets, whilst the third largest, New York State Common Retirement Fund, represents 121 billion Dollar in assets (Greider 2005). While the majority of CalPERS' assets are invested on a long-term basis in US corporations, the fund does hold investments in emerging markets.

In February 2005, for instance, the fund held $3.9 billion in assets in emerging markets. This trend will persist, as the role of emerging markets vis-à-vis production facilities and consumer markets continue to flourish (World Bank 2005a+b) (2). The surge of foreign financial flows to the 'emerging markets' also coincided with the low interest rates in the G-7 countries during the early 1990s, which was brought about by one of the deepest recessionary environments in post-war period, outweighed official development assistance (see Table 1).

Table 1: Financial Flows to Developing Countries 1990-2004



Source: World Bank (2005b)

It is against this backdrop that the PCI was forged and became an important tool for monitoring performance and enhancing value of investments abroad. The Index should be regarded as a dynamic document that seeks to be sensitive to changes and challenges in the global investment environment. It was not until 1999 in the wake of the East Asian crash of 1997 that the Investment Committee at CalPERS requested that Wilshire Associates undertake 'a complete review of the analysis and looked to expand it since more information regarding countries and markets has become available' (Wilshire Consulting 2005: 3).

In the light of the losses incurred by the Enron and subsequent debacles in the US and the ensuing loss of investor confidence, the CalPERS' Investment Committee sought to fine-tune the PCI by adding two new features to the Index as well as a broader treatment of political risk (Wilshire Consulting 2005).

Measuring 'Enduring Value'

The first country factor of the PCI is political stability, comprised of two parts: a macro-factor and several sub-factors. Political stability, the macro-factor, refers to progress in the creation of basic democratic institutions and principles, such as guaranteed elimination of human rights violations, and a strong and impartial legal system. Political stability is seen as vital components in guaranteeing the development of a free market in the Third World, which in turn will attract and retain long-term capital. There are several sub-factors that further define political stability: civil liberties, independent judiciary and legal protection, and political risk (Wilshire Consulting 2005).

It is worth emphasising that the 'credible independent' third-party sources that are used to evaluate these sub-factors is the Freedom House rankings, which are published on an annual basis. For the most part, the Freedom House's findings are guided by the Universal Declaration of Human Rights (Freedom House 2005). It should be noted that the same criteria supplied by the Freedom House is used by President George W. Bush's highly controversial 'global development compact': the Millennium Challenge Account (cf. Soederberg 2004b).

Judiciary and legal protection sub-factor

To determine the independent judiciary and legal protection sub-factor, Wilshire draws on the Contracts and Law Sub-Index that is published annually in the Global Competitive Report, which is affiliated with the World Economic Forum. Lastly, for the political risk sub-factor, Wilshire draws on the risk ranking published in the International Country Risk Guide of a private consultancy firm, PRS Group, which caters to top Fortune 500 companies. Similar to the other PCI factors, each of these three sub-factors is scored out of three. The highest score is three (good) and the lowest is one (poor). For a country to remain on the investable market list, they must achieve a passing score of two.

„The criteria supplied by the Freedom House is used by President George W. Bush's highly controversial global development compact."

The second macro-factor is transparency. Wilshire sees this factor as comprising primarily financial transparency, but including 'elements of a free press necessary for investors to have truthful, accurate and relevant information on the conditions in the countries and companies in which they are investing.' (2005: 6). The transparency factor includes four sub-factors: freedom of the press, monetary and fiscal transparency, stock exchange listing requirements, and accounting standards (2005: 6-7). Productive labour practices comprise the third macro-factor. To assist in the evaluation of this macro-factor, Wilshire Consulting identified a credible third party: Verité is a non-profit research organization based in Amherst, Massachusetts.

Role of the International Labour Organisation

As Wilshire states, in the attempts to facilitate of economically-productive labour practices, markets shall be evaluated based on their ratification of and adherence to the principles laid out by the International Labour Organization (ILO), which 'cover labour rights and prohibitions on abusive labour practices, and the degree of effectiveness of implementation through relevant laws, enabling regulations and their degree of enforcement through the judiciary process' (2005: 7).

The Productive Labour Practices macro-factor is accompanied by the following four sub-factors, which total to a maximum of 40 points per country: ILO Ratification, Quality of Enabling Legislation, Institutional Capacity, and effectiveness of implementation. Moreover, these sub-factors are more heavily-weighted toward the quality of enabling legislation and the effectiveness of implementation (ibid.). Drawing on the ILO, Wilshire defines the sub-factor of 'effectiveness of implementation as: 'The procedures that exist for enforcement and monitoring of enforcement of laws in the convention areas and evidence that exists that these procedures are working effectively; the existence of a clear grievance process; evidence that workers and/or unions utilize this grievance process; the extent to which penalties provided for in the laws are levied; and the evidence that penalties have deterrence value' (Wilshire Consulting 2005: 8).

For CalPERS, the PCI is a useful rating-system in which to gauge not only company level adherence to good corporate governance practices, but also a developing country's commitment to ensuring an institutional framework that will support the ➜

„PCI is a tool to protect workers' deferred wages by improving economic efficiency, rather than radical ideas of social justice aimed at mitigating harmful effects of economic exploitation rooted in capital accumulation."

'proper' functioning of equity investments. This is an important point as it reflects the nature of the PCI as a tool to protect workers' deferred wages by improving economic efficiency, rather than radical ideas of social justice aimed at mitigating and/or reducing harmful effects of economic exploitation rooted in capital accumulation, such as the low wages, long working days, and lack of adequate health and social benefits (Altvater/Mahnkopf 2002; Harvey 2001).

Relatedly, the reformist nature of the PCI also rests on a key assumption that the links between economic efficiency and political democracy are historical and logical trends. Bob Jessop identifies Milton Friedman, as one of the main proponents of this assumption. Friedman argues that the typical state of mankind is tyranny, servitude, and misery and that the nineteenth and early twentieth century in the Western world are remarkable exceptions to the general trend that the free market and the development of capitalist institutions are necessary conditions for political freedom (cf. Jessop 1983: 275).

The issue that is neglected in this assumption, as Jessop reminds us, is that democracy secures capitalist interests by ensuring that the working class can be legitimately subjected to the exploitation of capital – or, '[where] exploitation takes the form of exchange, dictatorship tends to take the form of democracy' (1983: 277). CalPERS and the 'independent' third parties, upon whom it draws its expertise, are not alone in sharing this correlation between political democracy and free market enterprise.

Questionable knowledgebase

Just as the above assumption is neither neutral nor a natural occurrence, the knowledge base underpinning the PCI must also be put into question. It is worthwhile highlighting that Wilshire Associates do not determine which factors and sub-factors comprise the PCI; instead, they are determined by the CalPERS Board of Directors, although the revised PCI was initiated by both the Treasury Department of California and the former CEO of CalPERS, Sean Harrigan (3). According to a senior associate at Wilshire, it is the consultancy firm's job 'to find appropriate, credible independent third-party sources that evaluate the factors and sub-factors'(4). One needs to recognise that despite Wilshire's assertion that 'credible independent third-party sources' are used in the evaluation process of these factors and subfactors, knowledge is not an objective abstraction that is devoid of a material basis.

As Susan Strange argues, 'knowledge structures exist which have the effect of valuing or devaluing different forms of knowledge.' Moreover, a knowledge structure 'determines what knowledge is discovered, how it is stored, and who communicates it by what means to whom and on what terms' (1988: 115-117). As mentioned above, in 2002, the year that Wilshire devised the expanded PCI detailed above, CalPERS decided to pull out of all its investments in Thailand, Malaysia, Indonesia and the Philippines. However, after intense lobbying by the Philippine government and community living in the United States, CalPERS reversed its decision in May 2002.

In February 2003, Wilshire Associates, once again, advised CalPERS to divest from its Philippine holdings. Instead of heeding this advice, CalPERS management devised a 'cure period', which refers to 1 year of grace before CalPERS liquidates its investments in any emerging market that slips out of public pension funds' permissible list. In February 2004, Wilshire once again advised CalPERS to exit the Philippines, as it did not meet the criteria set out by the PCI, despite the cure period.

Enduring Value in the Developing World

This brief account has sought to provide a broad and critical overview of CalPERS' attempt at ethical investment practices in the Third World. The PCI, despite its limitations, does contain potential to challenge the increasing power of corporations and finance over everyday lives in the global North and South. Although, CalPERS current investments in the developing world are quite small (3.9 billion Dollars) compared to over 279 billion Dollars in private capital flows, there are at least two important global trends, both of which suggest that struggles for social justice via international investment practices could gain critical levels of momentum in the near future (Bose 2005).

First, the money managed under the PCI initiative represents part of a larger ethical fund industry, which generates approximately 2.4 trillion Dollars, indicates that many investors and savers are beginning to feel more sympathetic to the critiques against neoliberal-led globalisation and they are able to back up these sentiments with money. Second, at the international level, workers' deferred wages amount to approximately 13 trillion Dollars (Guinan 2003). However, before CalPERS could act as the model ethical investor, it should move toward a more radical approach in ensuring social accountability that rests on more critical understanding of the role of capital accumulation in the Third World, as well as the advanced industrialised countries.

Literature

Altvater, E./ Mahnkopf, B.: *Globalisierung der Unsicherheit: Arbeit im Schatten, schmutziges Geld und informelle Politik*. Münster 2002.

Blackburn, R.: *Banking on Death or, Investing in Life: The History and Future of Pensions*. London 2003.

Bose, S.: *Capital Flows to Emerging Markets: Illusory Gains*. Networkideas.org, 29 January 2005. Download at: www.networkideas.org/news/jan2005/print/prnt290105_IIF.htm.

Ghilarducci, T.: *The American Labor Movement's (Surprising) Economic Impact: How Unions Challenge Consumerism and Corporate Governance*. In: *Research in Social Movements, Conflicts and Change*. Vol. 25, 2004. Pp. 321–352.

Greider, W.: *The New Colossus*. In: *The Nation*. 28 February 2005.

Guinan, J.: *Pension Fund Socialism: The Left Needs A Capitalist Strategy*. In: *The Voice of the Turtle*, 2003. Download at: www.voiceoftheturtle.org/show_article.php?aid=321#_ftn1.

Harvey, D.: *The New Imperialism*. Oxford 2004.

Hawley, J.P. / Williams, A.T.: *The Rise of Fiduciary Capitalism: How Institutional Investors Can Make Corporate America More Democratic*. Philadelphia 2000.

Hebb, T.: Introduction: *The Challenge of Labor's Capital Strategy*. In: Fung, A./ Hebb, T./Rogers, J (eds.): *Working Capital; The Power or Labor's Pensions*. Ithaca, New York 2001. Pp 1–13.

Jessop, B.: *Capitalism and Democracy: the Best Possible Political Shell?* In: Held, D. et al. (Eds.): *States & Societies*. Oxford 1983. Pp. 272-289.

Lazonick, W. / O'Sullivan, M.: *Maximizing shareholder value: a new ideology for corporate governance*. In: Economy & Society. Vol. 29, Nr. 1, 2000. Pp. 1–35.

OECD: *OECD Principles of Corporate Governance*. Paris 2004. Download at: www.oecd.org/dataoecd/32/18/31557724.pdf.

Soederberg, S.: *American Empire and Excluded States: The Millennium Challenge Account and the Shift to Pre-emptive Development*. In: Third World Quarterly. Vol. 25, Nr. 2, 2004. Pp. 297–302.

Soederberg, S.: *The Politics of the New International Financial Architecture: Reimposing Neoliberal Dominance in the Global South*. London 2004a.

Strange, S.: *States and Markets: An Introduction to International Political Economy*. New York 1988.

Wilshire Consulting: *Permissible Equity Markets Investment Analysis. Prepared for The California Public Employees' Retirement System*. Santa Monica, CA 2005.

World Bank: *World Development Report: A Better Investment Climate for Everyone*. Oxford 2005.

World Bank: *Global Development Finance 2005: Mobilizing Finance and Managing Vulnerability*. Washington, DC 2005b.

Notes

(1) This paper forms part of my forthcoming book Social Accountability versus Corporate Governance: *Understanding and Transcending the Construction of a False Binary*.

(2) Confidential interview staff member of the Council of International Investors, Washington, DC on 13 May 2005.

(3) Confidential interview with representatives from the Treasury Department of California on 6 May 2005.

(4) Confidential e-mail exchange with a Senior Associate at Wilshire on 21 June 2005.

AUTORIN + KONTAKT

Susanne Soederberg ist Canada Research Chair & Associate Professor für Development Studies an der Queen's University Kingston, Canada.

Mackintosh-Corry Hall, Room E-323, Queen's University, Kingston, Ontario, Canada K7L 3N6. E-Mail: soederberg@queensu.ca