

Model Ordinance: Divestment from Fossil Fuel Companies

Summary:

This act requires that a municipal public fund create a list of fossil fuel companies that match specific criteria, divest all holdings from the companies on this list over a 3-year period, and reinvest funds in socially responsible investments that satisfy prudent person standards.¹ This act also requires investment offerings for participant-directed retirement funds that are devoid of holdings in fossil fuel companies. This act also urges divestment action from fiduciaries of local government investment pools and that credit agencies factor climate risks into their ratings of publicly held companies.

SECTION 1. SHORT TITLE. The act shall be known as the “Municipal Divestment from Fossil Fuels Act”.

SECTION 2. DEFINITIONS. For the purposes of this act:

(1) “Asset manager” means the individual(s) or firm(s) endowed with the responsibility to physically invest the public fund’s assets. Asset managers may also advise the public fund on investment strategies.

(2) “Coal extraction activities” means activities including exploring for, extracting, processing, transporting, or wholesale selling or trading of coal, as well as the facilitation of such activities, including the provision of supplies or services in support of such activities.

¹ Municipal government pension funds are exempt from the strict prudent investor rules laid out by ERISA, but they are usually governed by state laws, including state statutes, state constitution, and common law. Municipal advocates and policymakers will need to review the legal landscape before drafting a final bill, including determining the effects of state passage of the Uniform Prudent Investor Act and/or the Uniform Management of Public Employee Retirement Systems Act. But it should be noted that one state court ruled that a municipal government did not violate common law fiduciary standards by making investments based on external benefits when the difference in expected returns relative to risks were “de minimis.”

(3) "Company" means a sole proprietorship, organization, firm, association, corporation, utility, partnership, venture, franchisor, franchisee, trust, or other entity, its wholly owned subsidiary or affiliate that exists for profitmaking purposes or to otherwise secure economic advantage.

(4) "De minimis" means:

(A) less than [0.35%] of the value of total fund assets for initial costs; or

(B) less than [0.25%] of the value of total fund assets for ongoing annual costs.

(5) "Direct holdings" means all publicly traded securities of a company held directly by a public fund or in an account or fund in which a public fund owns all shares or interests.

(6) "Divestment action" means selling, redeeming, transferring, exchanging, or otherwise disposing or refraining from further investment in certain investments.

(7) "Fossil fuels" means an energy source formed in the earth's crust from decayed organic material. The term includes petroleum, coal, natural gas, heating oils, light and heavy diesel oil, motor gasoline, propane, butane, residential fuel oils, kerosene, and aviation fuels.

(Policy option: exclude natural gas from this list)

(8) "Fossil fuel company" means a company which directly or through an affiliated instrumentality meets any of the following criteria:

(A) Derives more than [15] percent of its revenue from:

(i) sale of fossil fuels;

(ii) coal extraction activities; or

(iii) oil-related activities.

(B) Owns or holds leases for fossil fuel reserves that if extracted and burned would account for more than [0.1] gigatons of carbon dioxide; or

(C) Is a conglomerate or holding company in which one or more of its subsidiary companies meets either criteria in Subsection (A) or (B).

(9) "Indirect holdings" means all publicly traded securities of a company held in an account or fund, such as a mutual fund, managed by one or more persons not employed by the public fund, in which the public fund owns shares or interests together with other investors.

(10) "Invest" or "investment" means the purchase, ownership, or control of stock or other securities of a company, corporate bonds or other debt instruments issued by a company, or the commitment of funds or other assets to a company, including a loan or extension of credit to that company.

(11) "Oil-related activities" means, but need not be limited to, owning rights to oil blocks; exporting, extracting, producing, refining, processing, exploring for, transporting, selling or trading of oil; constructing, maintaining, or operating a pipeline,

refinery, or other oilfield infrastructure; and the facilitation of such activities, including the provision of supplies or services in support of such activities.

(Policy option: "Oil-related activities" does not include the mere retail sale of gasoline and related consumer products.)

(12) "Public fund" means the [municipal board of investment commissioners], the [municipal finance director], the [board of directors of the fire and police pension association], the [board of directors of the municipal officials and employees retirement association] and the [board of directors of the municipal public school retirement system].

(13) "Publicly traded securities" means ownership interest or debt instruments that are currently traded on a securities exchange that is officially recognized, sanctioned, or supervised by a governmental authority of the country in which the market is located or currently traded through the United States over-the-counter market that is reflected by the existence of an interdealer quotation system.

(14) "Socially responsible investment" means a fund that invests in companies that operate by moral standards approved of by their investors, such as, but not limited to, not manufacturing or selling weapons, not trading with countries with poor human rights records, not selling addictive substances (like alcohol, gambling and tobacco), and seeking out companies engaged in environmental sustainability and alternative

energy/clean technology efforts, such as companies that use only environmentally acceptable sources of raw materials.

SECTION 3. APPLICABILITY. This act applies to all public funds, including trustee-directed pension plans, short-term accounts, endowments and foundations in which a municipal officer acts as the trustee or asset manager for the fund.

SECTION 4. IDENTIFICATION OF FOSSIL FUEL COMPANIES.

(a) Within ninety days of the effective date of this section, a public fund shall make its best efforts to identify all fossil fuel companies in which the public fund has direct or indirect holdings. Such efforts may include, as appropriate in the public fund's judgment:

(1) Reviewing and relying on publicly available information regarding fossil fuel companies, including information provided by nonprofit organizations, research firms, international organizations, and government entities, such as, but not limited to CarbonTracker.org; and

(2) Contacting asset managers contracted by the public fund that invests in fossil fuel companies.

(b) By the first meeting of a public fund following the ninety-day period described in Subsection 8(a), the public fund shall assemble all identified fossil fuel companies in a fossil fuel companies list.

(c) A public fund shall update the fossil fuel companies list every six months based on evolving information from, among other sources, those listed in Subsection 8(a).

(d) A public fund may engage a reputable and non-biased third-party research firm or organization that offers services related to social screening of companies. It shall be reasonable and sufficient for a public fund to rely on information and work product obtained from such research firm or organization, such as, but not limited to:

- (1) Institutional Shareholder Services, Inc.;
- (2) Glass Lewis & Co.;
- (3) HSBC Global Research;
- (4) Investor Responsibility Research Center;
- (5) McKinsey & Co.
- (6) Mercer
- (7) Calvert
- (8) Domini

(e) Research and analysis methodology and a complete list of fossil fuel companies that are attained through the process in this section shall be made publicly available.

(f) Reasons for eliminating or adding a company from a preliminary list of identified fossil fuel companies based on the process outlined in this section must be justified in writing and supported by available research.

SECTION 5. DIVESTMENT FROM FOSSIL FUEL COMPANIES.

(a) Upon completion of a fossil fuel companies list pursuant to Section 4 of this act, the public fund shall immediately determine the companies on the fossil fuel companies list in which the public fund owns direct or indirect holdings, and shall take divestment actions to sell, redeem, or withdraw all publicly traded securities of the aforementioned fossil fuel companies as quickly and prudently as practicable within the following schedule:

(1) At least [twenty-five] percent of such assets shall be removed from the public fund's assets under management within [nine] months after the company's most recent appearance on the fossil fuel companies list.

(2) At least [fifty] percent of such assets shall be removed from the public fund's assets under management within [eighteen] months after the company's most recent appearance on the fossil fuel companies list.

(3) At least [seventy-five] percent of such assets shall be removed from the public fund's assets under management within [twenty-seven] months after the company's most recent appearance on the fossil fuel companies list.

(4) [One hundred] percent of such assets shall be removed from the public fund's assets under management within [thirty-six] months after the company's most recent appearance on the fossil fuel companies list.

(b) During the [thirty-six] month period described in Subsection 5(a), the public funds shall make quarterly reports to the [mayor] and [city council or town board] concerning the progress of divestment from fossil fuel companies.

(c) During the [thirty-six] month period described in Subsection 5(a), the public funds may from time to time suspend the divestiture program provided the public fund adopts a resolution pursuant to this section.

(d) That when a public fund adopts a resolution suspending the divestment actions under this section, the suspending board shall find as follows:

(1) That the current rate of return on the funds are substantially lower than the average of the annual earnings on the funds over the past five years due to divestment actions taken pursuant to this act;

(2) That continued divestment actions under this act will be inconsistent with generally accepted investment standards for fiduciaries or conservators of pension funds notwithstanding the intent of this act; and

(3) That continued divestment actions from fossil fuel companies will cause financial losses to the fund.

(e) That when a public fund adopts a resolution suspending the divestment actions under this section, the resolution shall:

(1) State the standards and conclusions for the suspension;

(2) Set forth the duration of the suspension and the time of resumption of the divestment actions; however, the period of suspension shall not exceed 90 days and the time limit shall be tolled for the period of suspension; and

(3) Be in writing and shall be sent to the [mayor], [president of the city council or town board], and the [department of legislative reference].

(f) Private equity. Public funds shall annually notify asset managers of private equity assets of the public fund that public policy in [name of municipality] is to avoid participation in fossil fuel companies and request the asset managers not undertake any investments that would constitute such operations. Prior to investing in a new private equity fund that is not in the public fund's portfolio as of the effective date of this act, the public fund shall perform due diligence to prevent investment in any private equity fund where the offering memorandum or prospectus identifies the purpose of the private equity fund as investing in fossil fuel companies.

(g) At no time shall a public fund acquire direct holdings in securities of companies on the fossil fuel companies list. Public funds shall not undertake investments in an indirect passively managed fund that is not held in the public fund's

portfolio as of the effective date of this act, where the passively managed fund contains publicly traded securities of a company on the fossil fuel companies list.

(Policy option: require two investment funds be set-up: (1) one with fossil fuels and (2) one without + require asset managers to periodically justify any investments in fund with fossil fuel investments.)

(Policy option 2: Excluding indirect holdings: (1) Notwithstanding any other section of this act, subsections 5(a) and 5(b) do not apply to indirect holdings in actively managed investment funds. A public fund shall, however, submit letters to the asset managers of such investment funds containing companies on the fossil fuel companies list requesting that they consider removing such companies from the fund or create a similar actively managed fund with indirect holdings devoid of such companies. If the asset manager creates a similar fund and if the public fund determines investment in the similar fund is consistent with prudent person standards, the public fund shall replace all applicable investments with investments in the similar fund in an expedited time. (2) In addition, notwithstanding any other section of this act, for passively managed indirect holdings, if the asset manager does not remove companies listed on the fossil fuel companies list or create a similar fund consistent with prudent person standards within nine months after the date the public fund requests the asset manager to act, then the public fund will divest all funds from the passively managed indirect holdings.)

SECTION 6. REINVESTMENT IN SOCIALLY RESPONSIBLE INVESTMENTS.

(a) Asset managers shall reinvest at least [10] percent of funds divested in accordance with Section 5 of this act into socially responsible investments that meet the following criteria:

(1) Equivalent level of risk compared to similar investment instruments that are not socially screened. Asset managers may consider the risk assessment implications for fossil fuel companies due to:

(A) future constraints on carbon-intensive revenues and the risk of a “carbon” asset bubble due to stranded fossil fuel reserves;

(B) potential actions taken by foreign governments with large carbon reserves, such as the countries that are members of OPEC;

(C) improvements in automobile fuel economy and other factors leading to reduced demand for oil;

(D) increased adoption and lower future costs of renewable energy;

and

(E) any other factor that the public fund deems prudent.

and

(2) No more than a de minimis reduction in expected return on investment compared to similar investment instruments that are not socially screened.

(b) Socially screened investments in this section, including socially responsible investments, shall generally meet the standards expected of a reasonably prudent person.

SECTION 7. ALTERNATIVE INVESTMENT OFFERINGS FOR PARTICIPANT-DIRECTED MUNICIPAL RETIREMENT FUNDS.

(a) Notwithstanding any other section of this act, public funds, when discharging their responsibility for operation of a participant-directed municipal retirement fund, shall engage the asset manager of the investment offerings in such plans requesting that they consider removing companies on the fossil fuel companies list from the investment offerings or create two alternative investment offerings, both devoid of fossil fuel companies:

(1) Investment offering devoid of direct or indirect holdings of public equity, corporate bonds, or other debt obligations of a company on the fossil fuel companies list; and

(2) Investment offering that in addition to Subsection 7(a)(1), also includes at least [10] percent of its direct or indirect holdings in socially responsible investments as described in Section 6 of this act.

(b) Socially screened investments in this section, including socially responsible investments, shall generally meet the standards expected of a reasonably prudent person.

(c) Information on the two additional investment offerings created in this section shall be distributed electronically and in print to all participants in a participant-directed municipal retirement fund, and this information will be prominently posted in online and print materials related to asset allocation.

SECTION 8. LOCAL GOVERNMENT INVESTMENT POOL DIVESTMENT FROM FOSSIL FUEL COMPANIES.

(a) The [city council or town board] urges the [state investment board or state treasurer] to take the following actions in regard to [municipality's name]'s assets held in any state-run local government investment pool:

(1) Determine the amount of municipal assets in which the state is the fiduciary agent;

(2) Direct the state asset managers for the local government investment pools to take divestment action on any direct or indirect holdings of public equity, corporate bonds, or other debt obligations of a company that meets the criteria in Section 4 of this act in an amount equal to or greater than the total municipal assets being managed by the [state investment board or state treasurer];

(3) Direct the state asset managers for the local government investment pools to invest at least [10] percent of its holdings in socially responsible investments as described in Section 6 of this act.

(b) The [city council or town board] urges [city council or town board] in other municipalities with assets in a state-run local government investment pool to urge the [state investment board or state treasurer] to take divestment action against holdings in fossil fuel companies.

(c) The [city council or town board] urges the [state investment board] to prepare a report that analyzes the direct and indirect economic impact of divesting from fossil fuel companies and investing in socially responsible investments.

SECTION 9. CLIMATE RISK IN CREDIT RATINGS.

(a) The [city council or town board] urges credit rating agencies to incorporate climate risks into their credit ratings for publicly held companies.

(b) The [city council or town board] intends to circulate a letter to other city councils or town boards in the state urging their signing onto a letter that will be sent to the three largest credit rating agencies, Standard & Poor's, Moody's, and Fitch Group, requesting that the credit rating agencies take steps to factor the risk of climate change in their ratings.

SECTION 10. IMMUNITY.

(a) With respect to actions taken in compliance with this act, including all good faith determinations regarding companies as required by this act, a public fund shall be exempt from any conflicting statutory or common law obligations, including any such

obligations in respect to choice of asset managers, investment funds, or investments for the public fund's securities portfolios.

(b) With respect to all actions taken in good faith compliance with this act, a public fund, its board of directors, individual board members, agents, trustees, officers, employees, custodians, and fiduciaries shall be immune from any liability.

SECTION 11. SEVERABILITY. If any provision of this act or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of this act which can be given effect without the invalid provision or application, and to this end the provisions of this act are severable.

SECTION 12. EFFECTIVE DATE. This act takes effect on January 1, 20xx.