Don't Break the Bank, Build a New One: How Investing in Public Banks Can Solve Pensions' ESG Problem

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Pension funds are significant institutional investors with massive capital. Attractive, prosocial investment opportunities abound. Nevertheless, several roadblocks limit American pension managers from engaging in ESG investing, including ERISA, fiduciary rules, anti-ESG state laws, and institutional inertia. This impasse creates an opportunity for public intervention because the private sector may be failing to meaningfully adjust to meet societal goals. This Note argues that public banking may be an appropriate tool to distribute some pension capital to ESG goals, effectively enabling pensions to outsource their present ESG burden. Though currently a rarity in the United States, public banks can serve as sound investments for pensions while in turn using this invested money for prosocial initiatives.

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INTRODUCTION

In 1776, Adam Smith, the progenitor of classical economics, published *The Wealth of Nations*.[1] In the treatise, Smith concluded that competition driven by self-interest promotes social good.[2] Over 200 years later, a new mantra has arisen among economists, academics, and business leaders: "ethics is the new competitive environment."[3] Comporting with this declaration and with classical economic theory, over three thousand financial institutions with more than $100 billion in assets under management have signed onto the United Nations (UN) Principles for Responsible Investing (PRI) as of 2022.[4] As PRI signatories, these institutions have pledged to consider environmental, social, and corporate governance (ESG) factors in their activities.[5] Nearly one hundred of these signatories are U.S. institutions.[6] Yet many of this nation's pensions remain wary of ESG investing, with various stakeholders arguing that codified fiduciary duties preclude trustees from considering ESG factors.[7] Pensions are dominant market forces with significant impacts across industries and meaningful influences in public policy.[8] American pensions

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1. ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS (Jim Manis ed., Electronic Classics Series 2005) (1776).

2. *Id.* at 362 ("[T]he study of his own advantage naturally, or rather necessarily leads him to prefer that employment which is most advantageous to society.").

3. Graham Cole, *Factors That Influence CEO Turnover*, 4 ANNALS IN SOC. RESP. 24, 24 (2018).

4. *See* Simon Jessop, *Exclusive: Five Groups Ousted from U.N.-Backed Responsible Investment List*, REUTERS (Sept. 28, 2020), https://www.reuters.com/article/global-investments-pri/exclusive-five-groups-ousted-from-u-n-backed-responsible-investment-list-idUSL5N2GK24T [https://perma.cc/4HBU-ADEE]; *see also* Public Signatory Reports, UNITED NATIONS PRINCIPLES FOR RESPONSIBLE INVESTMENT, https://www.unpri.org/signatories/reporting-and-assessment/public-signatory-reports [https://perma.cc/BU8Y-M7VV].

5. *See About the PRI*, UNITED NATIONS PRINCIPLES FOR RESPONSIBLE INVESTMENT, https://www.unpri.org/pri/about-the-pri [https://perma.cc/D9KY-9QU6].

6. *See* Jessop, *supra* note 4.

7. *See, e.g.*, Jed Rubenfeld & William P. Barr, Opinion, *ESG Can't Square with Fiduciary Duty*, WALL ST. J. (Sept. 6, 2022), https://www.wsj.com/articles/esg-cant-square-with-fiduciary-duty-blackrock-vanguard-state-stree-the-big-three-violations-china-conflict-of-interest-investors-11662496552 [https://perma.cc/J4UZ-WAW4] (noting that nineteen state attorneys general have written to BlackRock CEO Laurence Fink criticizing the firm's ESG investment policies for violating the fiduciary duty of loyalty).

8. *See* Gordon Clark, *Pension Fund Capitalism: A Causal Analysis*, 80 GEOGRAFISKA ANNALER: SERIES B, HUM. GEOGRAPHY 139, 139 (1998) ("Pensions . . . are a force to be reckoned with when governments seek to manage interest rates. . . . And they are an increasingly powerful voice in . . . domestic public policy.").

alone hold at least $20 trillion in assets.[9] Their lackluster ESG involvement can thus have far-reaching, negative repercussions for social progress.

Public banks are publicly funded depository and investment-oriented financial institutions.[10] In contrast to pensions, these banks operate with a mandate to prioritize community needs over private interests.[11] Although presently only two public banks operate in the United States, these institutions have received great political attention in recent years.[12] This Note argues that pensions should assist in capitalizing new public banks. Most of public banks' potential benefits, like bridging the racial wealth gap or helping governments weather crises, have been discussed extensively.[13] This Note offers a novel benefit: Public banks may enable pension funds to allocate more capital towards ESG goals without compromising their needs to generate reliable returns and abide by state and federal regulations. More importantly, perhaps, leveraging public banks for this purpose could result in a consequential, if small, decline in the private sector's currently outsized influence on public policy.

Part I provides an overview of pension types and the various rules governing the fiduciary duties of their trustees. It presents the evolution of scholarship concerning these fiduciary rules and highlights recent criticisms of the traditional emphasis on short-term profit maximization over other investment criteria. Additionally, Part I discusses the legal protections that may shield trustees from consequences when they neglect ESG investment. Part II then considers the institutional reluctance to make

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9. *See* OECD, PENSION FUNDS IN FIGURES 2 (June 2021) https://www.oecd.org/finance/private-pensions/Pension-Funds-in-Figures-2021.pdf [https://perma.cc/P6YR-R7LL].

10. *See* PUBLIC BANKS IN THE AGE OF FINANCIALIZATION: A COMPARATIVE PERSPECTIVE 1–8 (Christopher Scherrer ed., 2017).

11. *See id.*

12. *See infra* Part III.C; *see also* Emily Stewart, *Exclusive: Rashida Tlaib and AOC Have a Proposal for a Fairer, Greener Financial System—Public Banking*, VOX (Oct. 30, 2020), https://www.vox.com/policy-and-politics/21541113/rashida-tlaib-aoc-public-banking-act [https://perma.cc/F537-QHHA].

13. Ameya Pawar & Harish Patel, *Public Banking Can Help Bridge the Racial Wealth Gap in the Post-Pandemic Recovery*, CHI. REP. (July 7, 2020), https://www.chicagoreporter.com/public-banking-can-help-bridge-the-racial-wealth-gap-in-the-post-pandemic-recovery/ [https://perma.cc/XK8Z-PG2S] (discussing how public banks can reverse the racial wealth gap by lending to Black and Brown families at inexpensive rates); *see also* Travis Lavenski, *Public Banks: What Are They, and How Might They Impact Workers?*, ONLABOR (Jan. 12, 2022), https://onlabor.org/public-banks-what-are-they-and-how-might-they-impact-workers/ [https://perma.cc/JQ2M-64H5] (noting how public banks can help dull the impacts of economic recessions).

investments in accordance with ESG goals, noting how fiduciary hurdles and structural problems have made pensions slow to adopt ESG practices and investment strategies. Finally, after noting the inherent tension between private-sector and public policy goals, Part III introduces public banks worldwide and in the United States to assess their potential financial benefits. It then proposes that pensions ought to support the creation of public banks and invest in them to effectively outsource ESG investment while still meeting fiduciary duties. Not only does this relationship have the potential to generate large returns for pensions, but the subsequent proliferation of public banks could fundamentally change the whole of society through positive externalities.

I. PENSION MANAGEMENT UNDER THE ERISA-PRESCRIBED DUTIES OF PRUDENCE AND LOYALTY

All pensions are governed by the Employee Retirement Income Security Act of 1974 (ERISA) and largely consistent state rules, the most important of which establish the fiduciary duties of prudence and loyalty to pension beneficiaries.[14] Pension trustees often outsource investment to skilled managers, who use criteria like asset type, target industries, or geography to guide their investing.[15] Although many academics have highlighted the benefits of incorporating ESG goals into investment criteria, pension managers are often wary of doing so for fear of violating the duties of prudence and loyalty.[16] Indeed, recent judicial decisions appear to have strictly interpreted these fiduciary rules,

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14. *See* 29 U.S.C. § 1104 (1974); *see also, e.g.*, *What Is Fiduciary Duty and Why Is It Important?*, UNITED NATIONS PRINCIPLES FOR RESPONSIBLE INV. (Sept. 8, 2015), https://www.unpri.org/fiduciary-duty/what-is-fiduciary-duty-and-why-is-it-important/247.article [https://perma.cc/DN6F-ZXX2]; *infra* Part I.B (for a discussion of ERISA and definitions of prudence and loyalty).

15. *See, e.g.*, *Strategy/Investment Criteria*, LUCERN CAP. PARTNERS, https://lucerncapital.com/strategy-acquisitions/ [https://perma.cc/4ARB-ZSX5].

16. *See, e.g.*, Mahmut Aydoğmuş et al., *Impact of ESG Performance On Firm Value and Profitability*, 22 BORSA ISTANBUL REV. S119, S126 (2022) ("Our findings provide evidence for corporate managers to justify mobilizing more resources for ESG."); *see also* Sonal Mahida, *Fiduciary Duty is Not an Obstacle to Addressing ESG*, INT'L ENDOWMENTS NETWORK, https://www.intentionalendowments.org/fiduciary_duty_is_not_an_obstacle_to_addressing_esg [https://perma.cc/F38Y-43QZ] ("Outdated interpretations and limited understandings of materiality have led to the misconception that addressing . . . [ESG] factors falls outside the scope of fiduciary duty.").

likely further hampering ESG investment.[17] As pensions' extraordinary capital could be the harbinger of significant social progress, their inactivity in ESG investing is a tremendous detriment.

A. OVERVIEW OF PENSIONS

By the simplest definition, a pension is a pool of money for employees from which payments may be drawn at the conclusion of their working years.[18] Pensions may be broadly characterized as public or private based on the employees they serve.[19] Private pensions are managed by private employers, generally companies, while public pensions are run through government agencies at the local, state, or federal level.[20] The line between locally-administered and state-administered plans is often blurred. In 2017, for example, over sixty percent of contributions to locally-administered pensions went to state plans.[21] The distinction between state and federal pensions is, however, much clearer: the Federal Employee Retirement System is for all U.S. government employees and does not cover public employees in local or state government.[22]

Public and private pensions can be further divided into defined benefit (DB) and defined contribution (DC) plans.[23] A DB plan allows the employer to invest and manage money on behalf of the employee so as to provide that employee with a predetermined amount upon retirement.[24] Employees rarely have any control over these funds before they retire, but investment risks are borne

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17. *See, e.g.*, Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 426–30 (2014); Ret. Plans Comm. IBM v. Jander, 140 S. Ct. 592, 594–95 (2020); Thole v. U.S. Bank, 140 S. Ct. 1615, 1616 (2020).

18. *See* Nicholas Barr & Peter Diamond, *The Economics of Pensions*, 22 OXFORD REV. ECON. POL'Y 15, 16 (2006).

19. *See* THE FUTURE OF PUBLIC EMPLOYEE RETIREMENT SYSTEMS 1 (Olivia Mitchell & Gary Anderson eds., 2009).

20. *See id.* at 3.

21. *See State and Local Government Pensions*, URBAN INST., https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/projects/state-and-local-backgrounders/state-and-local-government-pensions [https://perma.cc/642V-W5JB] (last visited July 14, 2023).

22. *See* U.S. OFFICE OF PERSONNEL MANAGEMENT, FEDERAL EMPLOYEES RETIREMENT SYSTEM: AN OVERVIEW OF YOUR BENEFITS 17–20 (1998), https://www.opm.gov/retirement-services/publications-forms/pamphlets/ri90-1.pdf [https://perma.cc/WR5R-EZ33].

23. *See* Barr & Diamond, *supra* note 18, at 18.

24. *See id.* at 19.

by the employer.[25] In contrast, a DC plan allows employees to contribute funds to invest over time for their retirement.[26] An employer may contribute its own stock to an employee's retirement plan through a DC arrangement known as an employee stock ownership plan (ESOP).[27] Employers commonly contribute to employee DC plans, and directly or indirectly manage individual plans as a sole or co-sponsor.[28] However, it is the employees who bear the investment risks and have the ultimate say in how their funds are invested.[29] DB plans are most common in the public sector, while DC plans are the norm in the private sector.[30]

All pension plans are controlled by a board of trustees that may be held legally responsible in the event of wrongdoing.[31] A pension's trustees often have limited investment backgrounds, and hire staff to run the plan.[32] Such an arrangement can limit trustees' fiduciary liability to their hiring decisions.[33] Staff often share fiduciary liability as the individuals who actually manage beneficiary funds.[34] They typically look to external third parties to set financial benchmarks or actively manage money in accordance

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25. *See id.*

26. *See id.* at 18.

27. *Employee Stock Ownership Plans (ESOPs)*, INTERNAL REVENUE SERV. (2021), https://www.irs.gov/retirement-plans/employee-stock-ownership-plans-esops [https://perma.cc/7HK5-8X5T].

28. *See* Kate Ashford, *What Is A Defined Contribution Plan?*, FORBES (Oct. 24, 2022), https://www.forbes.com/advisor/retirement/defined-contribution-plan/ [https://perma.cc/89PH-E2PX]; EMP. BENEFITS SEC. ADMIN., U.S. DEPT. OF LAB., UNDERSTANDING RETIREMENT PLAN FEES AND EXPENSES 1 (2021), https://www.dol.gov/sites/dolgov/files/ebsa/about-ebsa/our-activities/resource-center/publications/understanding-retirement-plan-fees-and-expenses.pdf [https://perma.cc/PD7G-D8D2].

29. *See id.*

30. *See* ALICIA H. MUNNELL ET AL., WHY HAVE DEFINED BENEFIT PLANS SURVIVED IN THE PUBLIC SECTOR? 1 (2007), https://crr.bc.edu/wp-content/uploads/2007/12/slp_2.pdf [https://perma.cc/R37H-UWXG].

31. *See* Michael Edesess, *Opinion: How the Failures of Highly Paid Pension Fund Managers Are Costing You $500 a Year*, MARKETWATCH (June 12, 2021), https://www.marketwatch.com/story/how-the-failures-of-highly-paid-pension-fund-managers-cost-you-500-a-year-11623113060 [https://perma.cc/M3MP-FBGV]; *see also* Herman v. Kokonaski, No. 2:98-cv-01376 (W.D. Pa. Sep. 15, 1999) (ruling that two former retirement plan trustees who misused plan assets must restore the retirement plan and are permanently barred from serving as a fiduciary for any plan covered by ERISA).

32. Keith L. Johnson & Frank Jan de Graaf, *Modernizing Pension Fund Legal Standards for the 21st Century*, NETWORK FOR SUSTAINABLE FIN. MKTS. 8 (2009), https://www.oecd.org/daf/ca/corporategovernanceprinciples/42670725.pdf [https://perma.cc/A64Q-NL2X]; CFA INST., PENSION TRUSTEE CODE OF CONDUCT AND GUIDANCE FOR COMPLIANCE 6 (2019), https://www.cfainstitute.org/-/media/documents/code/other-codes-standards/pension-trustee-code-of-conduct-2019.pdf [https://perma.cc/X45C-9SXJ].

33. *See* Edesess, *supra* note 31.

34. *See id.*

with articulated investment criteria, sometimes including ESG factors.[35] These third parties share some fiduciary responsibility as well.[36] To this end, about two-thirds of public pension assets are outsourced to the private sector for management.[37] Similarly, private pension funds are regularly outsourced to asset management firms.[38] Mercer, the world's largest outsourced asset manager, oversees more than $74 billion in private pension funds.[39] In spite of the shared liability, the attenuation between trustees, plan administrators, and beneficiaries often fosters principal-agent problems in the pension chain of command.[40]

The United States is the world's largest holder of assets in pension funds.[41] According to the OECD, U.S. pensions held over $20 trillion in assets at the end of 2020.[42] Given the colossal total of these pensions' holdings, it is no surprise, then, that pensions have a sizable impact on the U.S. economy.[43] Notably, pension funds can trigger developments in capital markets by increasing the availability of long-term capital, lowering volatility, and improving corporate performance in these markets.[44] Alongside their role in capital markets, pensions are also "increasingly powerful voices" in public policy.[45] These significant roles in markets and politics suggest that pensions may also be helpful in heralding change if they were to embrace ESG like many others in

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35. *See id.*

36. *See* CFA INST., *supra* note 32, at 6; Benjamin Braun, *Asset Manager Capitalism as a Corporate Governance Regime*, *in* THE AMERICAN POLITICAL ECONOMY POLITICS, MARKETS, AND POWER 270, 280 (Jacob S. Hacker et al. eds., 2022) (discussing how ERISA incentivized pension fiduciaries to turn to external asset managers).

37. *See* Michael Urban, *Rescaling of American Public Pension Finance: Are State and Local Plans Running Away from Wall Street?*, 8 TERRITORY, POL., GOVERNANCE 431, 431 (2020).

38. *See* Edesess, *supra* note 31 (noting how pensions use consultants to decide investment strategy and choose asset managers); Braun, *supra* note 36, at 280.

39. *See The Largest Managers of Outsourced Assets by Source*, PENSIONS & INVS. (June 28, 2021, 12:00 AM), https://www.pionline.com/interactive/largest-managers-outsourced-assets-source [https://perma.cc/PVB4-X6ML]. The majority of DC plans come from the private sector, so it can be inferred that most of the DC assets managed are from private pension plans. Accordingly, ten asset management firms oversee billions of dollars from private plans, per the second table. *See id.*

40. *See, e.g.*, Johnson & Jan de Graaf, *supra* note 32, at 8–9; *see also* Edesess, *supra* note 31.

41. Note that the U.K., the second-largest, only has approximately $3 trillion held in pension funds. *See* OECD, *supra* note 9, at 2.

42. *See id.*

43. *See* Ashok Thomas & Luca Spataro, *The Effect of Pension Funds on Market Performance: A Review*, 30 J. ECON. SURVEYS 1, 1–2 (2016).

44. *See id.*

45. *See* Clark, *supra* note 8, at 139.

the financial sector.[46] At the same time, however, it seems the potential of pensions to be "the ultimate enablers of a sustainable transition on the financial market" is being wasted.[47]

B. ERISA-MANDATED FIDUCIARY DUTIES

The inability of pensions to catalyze social progress is largely due to an investment model that has dominated academic and regulatory thought for the last half-century, ultimately influencing the passage of ERISA in 1974. In 1952, economist Harry Markowitz introduced Modern Portfolio Theory (MPT), which popularized the idea that an investment universe should not be restricted for any reason.[48] The MPT approach views ESG criteria as detrimental to portfolio diversification, and therefore as threatening to returns.[49] MPT instead posits that any financial instrument is fair game for investment, even if it is tied to an organization that may be detrimental to a particular cause or population.[50] The cultural shifts of the 1960s and 70s led to the creation of a few mutual funds committed to social causes, but even then, "socially responsible investing had many more critics than investment vehicles."[51] Indeed, despite these discrete cultural shifts, the primary theory driving investment strategies from the early 1950s through the new millennium remained the MPT view that no restrictions should be forced on investment portfolios. This

46. *See, e.g.*, Joakim Sandberg, *Socially Responsible Investment and Fiduciary Duty: Putting the Freshfields Report into Perspective*, 101 J. BUS. ETHICS 143, 143 (2011) ("Quite obviously, if a lot of institutional investors could be persuaded to invest according to social and environmental guidelines, the [socially responsible investing (SRI)] movement could become an important force for corporate social responsibility worldwide.").

47. STÉPHANIE LACHANCE & JUDITH C. STROEHLE, THE ORIGINS OF ESG IN PENSIONS: STRATEGIES AND OUTCOMES 2 (Mar. 2021), https://pensionresearchcouncil.wharton.upenn.edu/wp-content/uploads/2021/04/Lachance-and-StroehleCombined_4.8.21.pdf [https://perma.cc/G8LQ-WZTE] (discussing the power of pensions).

48. Blaine Townsend, *From SRI to ESG: The Origins of Socially Responsible and Sustainable Investing*, 1 J. IMPACT & ESG INVESTING 2 (2020).

49. Andrew Rudd, *Social Responsibility and Portfolio Performance*, 23 CAL. MGMT. REV. 55, 57 (1981) (arguing that "imposition of socially responsible criteria may bias the portfolio and cause, except in rare circumstances, an increase in the investment risk" and that, "[f]inancially, these criteria are no different from many other exclusionary and targeting criteria . . ."); Tim Verheyden et al., *ESG for All? The Impact of ESG Screening on Return, Risk, and Diversification*, 28 J. APPLIED CORP. FIN. 47, 51 (2016).

50. *See, e.g.*, *id.*; Townsend, *supra* note 48; Kent Hickman et al., *Social Investing and Modern Portfolio Theory*, 17 AM. BUS. REV. 72, 73 (1999) ("Modern Portfolio Theory recognizes that . . . the lower the correlations are [between securities in a portfolio], the greater will be the reduction in risk. . . .").

51. Townsend, *supra* note 48, at 2.

dominant view is perhaps best exemplified by the famous declaration of former Ford Foundation President McGeorge Bundy: "We don't believe only the virtuous make money."[52] Amidst this theoretical backdrop, Congress enacted ERISA, the first express institutional barrier to ESG investing and the dominant regulatory scheme for pension trustees today.

ERISA is the modern standard for pension fund management.[53] The statute lists five fiduciary duties for trustees: (1) the duty to act prudently; (2) the duty to diversify the assets of the plan; (3) the duty to comply with the provisions of the plan; (4) the duty to act exclusively in the interests of beneficiaries, commonly referred to as the duty of loyalty; and (5) the duty to pay only reasonable plan expenses.[54] In line with the MPT approach, the five ERISA duties were traditionally interpreted to bar investment in ESG.[55] Today, these duties continue to cause confusion among investors when social goals or long-term considerations might seem to compromise a fund's short-term profits.[56] To this end, the most litigated ERISA duties tend to be the duty of prudence and the duty of loyalty.[57] ERISA statutorily defines the duty of prudence

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52. *Id.*

53. State public pension rules vary, and many outline trustee duties in addition to those laid out by ERISA. These rules, however, have little bearing on this Note's argument because ERISA frequently preempts state law. *See* JENNIFER A. STAMAN, CONG. RSCH. SERV., LSB10597, SUPREME COURT DECISION SHEDS LIGHT ON STATE AUTHORITY TO REGULATE HEALTH CARE COSTS 2 (2021).

54. 29 U.S.C. § 1104; John H. Langbein, *Questioning the Trust Law Duty of Loyalty: Sole Interest or Best Interest?*, 114 YALE L.J. 931, 931 (2005). While these rules officially govern only private pension plans, it is commonplace for state public pension laws to borrow from ERISA. Dannae Delano et al., *Fiduciary Responsibilities for Non-ERISA Governmental Plans—Part III*, AM. SOC. OF PENSION PROS. & ACTUARIES (Sept. 4, 2015), https://www.asppa.org/news-resources/browse-topics/fiduciary-responsibilities-non-erisa-governmental-plans-%E2%80%94-part-iii [https://perma.cc/V7QQ-4KD3]. There may be additional state laws governing private pensions, but they will be preempted by ERISA if they conflict. STAMAN, *supra* note 53.

55. *See, e.g.*, Ian Lanoff, *The Social Investment of Private Plan Assets: May It Be Done Lawfully Under ERISA?*, 31 LABOR L.J. 387, 389 (1980) ("To introduce other social objectives may be to dilute this primary objective [of protecting retirement income]. . . . It is not consistent with the prudence standard for the fiduciary to make his or her investment decision based on other objectives. . . .").

56. Benjamin Richardson, *Do the Fiduciary Duties of Pension Funds Hinder Socially Responsible Investment?*, 22 BANKING & FIN. L. REV. 145, 145 (2007) ("However, some confusion among investment decision makers persists about the extent to which their fiduciary duties . . . allow policies that may sacrifice financial returns for . . . philanthropic causes. This is compounded by the belief that they cannot secure the best returns in respect of their fiduciary obligations with current . . . responsible companies.").

57. *See, e.g.*, Andrew Verstein, *Upstream Liability, Entities as Boards, and the Theory of the Firm*, 74 BUS. LAW. 313, 313 (2019); Michel Allen & Shaked Israel, *Fiduciary*

as acting "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."[58] Under ERISA, a trustee's duty to act prudently also requires diversification of plan assets, effectively codifying the core diversification tenet of MPT.[59] Loyalty is defined as "[discharging] . . . duties with respect to a plan solely in the interest of the participants and beneficiaries."[60]

In the event of a fiduciary breach, beneficiaries' only real recourse is to sue for relief in the courts. Lawmakers, however, have tried to limit the need for this course of action. Congress passed the Pension Protection Act of 2006 with the hope of maintaining pension solvency and ensuring pensioners receive owed benefits.[61] Similarly, agencies like the Pension Benefit Guaranty Corporation have mandates to monitor or participate in pension administration, and may be a recourse for beneficiaries in the event of a breach of a fiduciary duty.[62] Neither the ERISA rules nor their progeny, however, have been updated to reflect contemporary insights on the fiduciary duties themselves, particularly with regard to ESG inclusion.

Responsibility in the Case of Defined Contribution Plans, AM. BANKR. INSTI. J., Dec. 2004–Jan. 2005, at 47.

58. 29 U.S.C. § 1104(a)(1).

59. *Id.* ("[A] fiduciary shall discharge his duties . . . by diversifying the investments of the plan.").

60. *Id.*

61. *See* Israel Goldowitz, *Funding of Public Sector Pension Plans: What Can Be Learned from the Private Sector?*, 23 CONN. INS. L.J. 143, 169–70 (2016) ("The 2006 Pension Protection Act made a major overhaul . . . imposing strict rules to shore up the defined benefit system. . . . [New relief provisions added later] gave sponsors more flexibility, but traded off PPA's goal of shoring up the system as a whole.").

62. *See id.* at 144, 155, 157 ("PBGC is the federal agency charged with insuring private-sector defined benefit pension plans. . . . PBGC also enforces the funding rules. . . . On termination of an underfunded plan, PBGC becomes trustee, taking over the plan's assets and obligations."); *Overview of PBGC's Fiduciary Breach Investigations*, PENSION BENEFIT GUARANTY CORP. (Aug. 20, 2021), https://www.pbgc.gov/prac/laws-and-regulations/fiduciary-breach [https://perma.cc/G6UD-RWQP].

C. CALLS FOR FIDUCIARY REFORM

Heightened skepticism of the MPT approach has led to cries for fiduciary reform.[63] Today, many academics instead favor the Theory of Universal Ownership.[64] This theory postulates that large institutions must account for externalities across geographies, industries, and generations.[65] In particular, modern institutional investors are "universal owners" that hold a significant cross-section of public equities, and so must care about the performance of the entire economy rather than just a few companies.[66] Because pensions' sheer size makes them archetypal universal owners, some academics argue that their responsibilities should be expanded to include reducing negative externalities while increasing positive externalities.[67]

Criticism of MPT corresponded with subtle, dispassionate criticisms of ERISA fiduciary standards. For instance, one article pointed out that the increased emphasis on portfolio diversification technically means the ability to meet fiduciary obligations depends on the overall health of the economy—a severe complication, because fiduciaries may technically be in violation of their duties in case of an economic downturn.[68] In 2005, a landmark report

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63. *See, e.g.*, Jay Youngdahl, *The Time Has Come for a Sustainable Theory of Fiduciary Duty in Investment*, 29 HOFSTRA LAB. & EMP. J. 115, 124 (2011) ("Given the link between financial theory and fiduciary duty in investment, if the critics of MPT are correct, the foundation for the operative definition of fiduciary duty in investment must be reexamined as well."); Pete Swisher & Gregory W. Kasten, *Post-Modern Portfolio Theory*, 18 J. FIN. PLANNING 74, 74 (2005) ("The primary reason MPT produces inefficient portfolios . . . is simple: standard deviation is not risk.").

64. *See, e.g.*, Jan Fichtner & Eelke M. Heemskerk, *The New Permanent Universal Owners: Index Funds, Patient Capital, and the Distinction Between Feeble and Forceful Stewardship*, 49 ECON. & SOC'Y 493, 495–96 (2020) (referring to some asset managers as universal owners because of their indefinite investment in thousands of firms across international stock indices); Ellen Quigley, Universal Ownership in Practice: A Practical Investment Framework for Asset Owners 1 (May 28, 2020) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3638217 [https://perma.cc/K76G-CMVS] (referring to pensions, sovereign wealth funds, and more as universal owners who have an interest in the long-term health of the financial system as a whole).

65. *See* Roger Urwin, *Pension Funds as Universal Owners: Opportunity Beckons and Leadership Calls*, 4 ROTMAN INT'L J. PENSION MGMT. 26, 26 (2011).

66. James Hawley & Andrew Williams, *The Emergence of Universal Owners: Some Implications of Institutional Equity Ownership*, 43 CHALLENGE 43, 44–45 (2000); Anju Seth, Book Review, 26 ACAD. MGMT. REV. 668, 668 (2001) (reviewing JAMES HAWLEY & ANDREW WILLIAMS, THE RISE OF FIDUCIARY CAPITALISM: HOW INSTITUTIONAL INVESTORS CAN MAKE CORPORATE AMERICA MORE DEMOCRATIC (2000)).

67. *See, e.g.*, Quigley, *supra* note 64, at 2; Seth, *supra* note 66, at 669.

68. James Hawley & Andrew Williams, *Universal Owners: Challenges and Opportunities*, 15 CORP. GOV. 415, 415–16 (2007).

from Freshfields Bruckhaus Deringer, created in partnership with the UN Environmental Program Finance Initiative, seemed to offer a tentative endorsement of ESG investing. Its Foreword noted the importance of quality of life and quality of the environment "even if not, or particularly because, they are not reducible to financial percentages."[69]

More tangible support for ESG has followed the Freshfields report. A survey of Chinese firms found that high-ESG portfolios generally outperform low-ESG ones.[70] The survey also showed that ESG plays a critical role in portfolio risk management.[71] Another paper aggregating data from over 2000 empirical studies—one of the most exhaustive of such reviews—revealed that approximately ninety percent of these studies found a non-negative relationship between ESG investing and financial returns, making, in the authors' view, "the business case for ESG investing . . . empirically very well founded."[72] Researchers have also noted that ESG screening may cultivate investment in companies with good governance, translating to better returns.[73] Additionally, identifying companies with sound environmental and social policies may help investors avoid high costs, such as litigation expenses connected with derivative actions for fiduciary breaches, down the line.[74] Still other researchers have argued that ESG-aligned companies have unique social capital that better enables them to weather economic storms.[75] And beyond corporate performance and financial metrics, all individuals may derive indirect benefits from prosocial investment; health, safety,

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69. FRESHFIELDS BRUCKHAUS DERINGER, A LEGAL FRAMEWORK FOR THE INTEGRATION OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE ISSUES INTO INSTITUTIONAL INVESTMENT 3 (2005), http://www.unepfi.org/fileadmin/documents/freshfields_legal_resp_20051123.pdf [https://perma.cc/S99M-UKW2] [hereinafter FRESHFIELDS]; *see also infra* Part II.A; Part III.E (for additional discussion on the Freshfields Report).

70. David Broadstock et al., *The Role of ESG Performance During Times of Financial Crisis: Evidence from COVID-19 in China*, 38 FIN. RSCH. LETTERS 10176 (2021).

71. *Id.*

72. Gunnar Friede et al., *ESG and Financial Performance: Aggregated Evidence from More Than 2000 Empirical Studies*, 5 J. SUSTAINABLE FIN. & INV. 210 (2015).

73. Mohammed Benlemlih & Isabelle Girerd-Potin, *Corporate Social Responsibility and Firm Financial Risk Reduction: On the Moderating Role of the Legal Environment*, 44 J. BUS. FIN. & ACCT. 1137, 1139 (2017).

74. Luc Renneboog et al., *The Price of Ethics and Stakeholder Governance: The Performance of Socially Responsible Mutual Funds*, 14 J. CORP. FIN. 302, 305 (2008).

75. Paul Godfrey et al., *The Relationship Between Corporate Social Responsibility and Shareholder Value: An Empirical Test of the Risk Management Hypothesis*, 30 STRATEGIC MGMT. J. 425, 428 (2009).

property rights, culture, community, environment, and political systems can all be impacted by how firms allocate their resources.[76]

The BP oil spill heralded a fundamental shift in academic thought on ESG, validating ESG-inclusive investing strategies and forcing an endogenous repricing of external factors.[77] For multinational finance company MSCI, the disaster highlighted the importance of diversifying pension investments to cover ESG. The company noted that, for example, United Kingdom pensions covering over 18 million residents had held a concentrated amount of BP stock and consequently suffered sizable losses after the crisis.[78] Yet many pension trustees stayed the course following the oil spill: remaining undiversified, maintaining stock in BP, and delegating ESG responsibility to managers who often felt unequipped for the task.[79]

As a result of these developments, scholarship on the relationship between fiduciary duties and ESG seems to have taken a decidedly stronger tone since 2010. Some academics have lamented the "surprising *lack* of attention" on how the financial sector may be contributing to crises, a consequence of "dominant market narratives about . . . 'black swan' event[s] . . . or 'bad apples'" that discourage investors from considering external factors.[80] Another scholar has complained that "the duty to act in beneficiaries' best interests has been reduced to a maxim to maximize profits, usually over the short-term."[81] In 2018, a McKinsey consulting report noted that "[many] institutional

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76. *See, e.g.*, Frank Vanclay, *Reflections on Social Impact Assessment In the 21st Century*, 38 IMPACT ASSESSMENT AND PROJECT APPRAISAL 126 (2019) ("[Social impact assessment (SIA) is] . . . the process of managing a project's social issues . . . . SIA considers: . . . community development, community engagement, community resilience, cultural heritage, . . . gender issues, . . . [and] human rights . . . .").

77. Urwin, *supra* note 65.

78. Roger Urwin, *The BP Oil Spill and ESG*, MSCI (June 2010), https://www.msci.com/documents/10199/5b94cf49-421e-4c71-b65c-39b446d6dab3 [https://perma.cc/M5EE-2DEP].

79. Nina Röhrbein, *BP, Investors' Blind Spot*, INV. & PENSIONS EUR. (Sept. 2010) https://www.ipe.com/bp-investors-blind-spot/36641.article [https://perma.cc/HMT7-5CWT] ("Whether the BP oil spill will have any long term consequences on ESG research is not easy to assess. . . . 'But many pension funds still see themselves as traders rather than owners of those assets,' believes Duncan Exley. . . . '[A] majority of fund managers say that a lack of assertiveness from asset owners is holding them back from properly tackling [ESG] issues. There is also often a focus on very short term issues and quarterly results as a result of the short-term focused research. . . .'").

80. Raj Thamotheram & Maxime Le Floc'h, *The BP Crisis as a "Preventable Surprise": Lessons for Institutional Investors*, 5 ROTMAN INT'L J. PENSION MGMT. 68 (2012).

81. Bethan Livesey, *Pensions in a Time of Climate Change: The Inconvenient Truth About Fiduciary Duty*, *in* SUSTAINABLE FIN. INNOVATIONS 101, 104 (Karen Wendt ed., 2019); Röhrbein, *supra* note 79.

investors continue to treat ESG as a sideshow rather than an integral part of their investing."[82] It is commonplace for academics to at least indirectly support inclusion of ESG factors in investment analyses.[83] They also call for reform of the fiduciary guidelines that investors regularly point to when justifying ESG exclusion, such that the definition of prudence includes considering ESG factors.[84] Unfortunately, practice continues to diverge from scholarship.[85]

D. REDUCED JUDICIAL REVIEW OF FIDUCIARY DUTIES AND INVESTMENT PROCESSES

Recent jurisprudence may have created an institutional barrier to incorporating ESG into pension investing. It is now more difficult to review investment strategies, hold fiduciaries accountable for bad choices, and animate debate on the fiduciary rules by affording them a public forum in the courts. Such difficulties reinforce an anti-ESG investment status quo. Three cases in particular are responsible for this trend. The Supreme Court's ambiguous rulings in *Fifth Third Bancorp v. Dudenhoeffer*[86] and *Retirement Plans Committee of IBM v. Jander*[87] have created a split amongst circuit courts regarding the

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82. Jonathan Bailey et al., *Sustaining Sustainability: What Institutional Investors Should Do Next on ESG*, MCKINSEY & CO. (June 22, 2016), https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/sustaining-sustainability-what-institutional-investors-should-do-next-on-esg [https://perma.cc/C7QH-U9R3].

83. *See, e.g.*, Lasse Heje Pedersen et al., *Responsible Investing: The ESG-Efficient Frontier*, 142 J. FIN. ECON. 572 (2021) (proposing a framework through which investors may evaluate the costs and benefits of ESG preferences and stocks).

84. *See, e.g.*, Slavek Roller, *Pension and State Funds Dominating Biomedical R&D Investment: Fiduciary Duty and Public Health*, 15 GLOBALIZATION AND HEALTH 1, 2 (2019) ("Institutional investors have a fiduciary duty to act in the best interests of their savers-beneficiaries. How can then a situation be explained in which savers' pension assets are invested into companies whose medicines are not available to said savers due to the high cots? [sic]"); Patrick Jahnke, Asset Manager Stewardship and the Tension Between Fiduciary Duty and Social License (Jan. 30, 2019) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3307172 [https://perma.cc/986M-44J5] ("One of the biggest challenges to integrating sustainability concerns within the modern investment chain is the belief by some that prudence is to be understood entirely in financial terms."); Sandberg, *supra* note 46 at 143 ("[T]here is also a need for legal reform and it is important to discuss the political side of SRI.").

85. *See* JOHN HILL, ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) INVESTING: A BALANCED ANALYSIS OF THE THEORY AND PRACTICE OF A SUSTAINABLE PORTFOLIO 3 (2020) ("While ESG investing has grown in importance, it is also clear that most investing today is done with little if any concern about ESG factors.").

86. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409 (2014).

87. Ret. Plans Comm. of IBM v. Jander, 140 S. Ct. 592 (2020).

stringency of plaintiffs' pleading standards, generally damning ERISA suits outside the Second Circuit.[88] Meanwhile, the Court's decision in *Thole v. U.S. Bank*[89] has significantly moved the goal posts for plaintiffs in fiduciary cases, severely limiting who is eligible to sue.[90] That case may have also reduced pensioners' information rights.[91] Though current fiduciary standards already materially restrict the use of ESG in investing, these cases seem to have overshadowed the little daylight available to incorporate it into pension funds. Together, these cases protect pension fiduciaries from accountability under a de facto business judgment rule approach.[92] This, in turn, reduces opportunities for pensioners and external parties to learn of and advocate for ESG investing.

The plaintiffs in *Fifth Third Bancorp v. Dudenhoeffer* alleged that defendant Fifth Third, one of the largest banks in the American Midwest, breached its duty of prudence when it maintained large investments of its own overvalued stock in their ESOP.[93] The Supreme Court first addressed ERISA § 1104(a)(1),[94] interpreting it to mean that the duty of prudence trumps any idiosyncratic plan instruction.[95] Importantly, this means any plan-specific mandate to consider ESG is superseded by the duty, even though the duty's presently-accepted application has been called

88. *See, e.g.*, Dormani v. Target Corp., 970 F.3d 910, 915 (8th Cir. 2020) (citing *Ret. Plans Comm. of IBM*, 140 S. Ct. 592 (2020)) ("As we and nearly every other circuit court to confront this type of argument have held . . . a reasonably prudent fiduciary lacking the Plan participants' faith in arbitrageurs could still believe disclosure was the more dangerous of the two routes."). Note that new precedent may also make the Seventh Circuit a haven for plaintiffs in fiduciary suits. *See* Hughes v. Northwestern, 63 F.4th 615 (2023).

89. Thole v. U.S. Bank, 140 S. Ct. 1615 (2020).

90. *See* Percy Lee, *An Unregulated Asset in a Regulated World: Whether and How Employers Should Pay Employees in Cryptocurrency*, 135 J. TAXATION 26, 35 (2021) ("Because employers bear the responsibility of funding benefits under a defined benefit plan, participants are unlikely to be able to show their entitlement to receive benefits would be affected.").

91. *Thole*, 140 S. Ct. at 1622 (Thomas, J., concurring).

92. The "business judgment rule" is a judicial standard wherein courts will uphold a corporate director's decision so long as it was made in good faith, with the care a reasonably prudent person would use, and with the reasonable belief that the director was acting in the best interests of the corporation. *See Business Judgment Rule*, LEGAL INFO. INST., https://www.law.cornell.edu/wex/business_judgment_rule# [https://perma.cc/8NSE-9YAT] (last visited July 14, 2023).

93. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 409 (2014).

94. 29 U.S.C. § 1104(a)(1) ("[A] fiduciary shall discharge his duties with respect to a plan solely in the interests of participants and beneficiaries. . . .").

95. *Fifth Third Bancorp*, 573 U.S. at 421.

into question.[96] The Court then noted that ESOP fiduciaries are distinguishable from other fiduciary duties on the basis of ERISA § 1104(a)(2),[97] which states that ownership of employer stock does not violate ERISA's diversification requirement.[98] That is, ESOP fiduciaries may be exempt from the duty of prudence only insofar as it concerns the diversification of plan stock (because the ESOP model necessitates inclusion of employer stock), but even this investment must be conducted prudently.[99]

Although many commentators and academics consider *Fifth Third* to be favorable for pension beneficiaries, the case effectively prohibits breach of prudence claims based on public information, regardless of whether these claims rest on overvalued or excessively risky stocks.[100] This includes prudence claims concerning excessive risk as it relates to ESG; for example, beneficiaries may not sue if their fund announces a long-term bet on oil and gas.[101] Moreover, while the ruling does allow for ESOP prudence suits on the basis of *nonpublic* information, the Court failed to outline pleading standards for plaintiffs in such cases.[102]

The Court offered a possible framework for lower courts to consider the issue, but one prong has caused a great deal of confusion. To make a claim for breach of the duty of prudence, a

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96. JEAN-PIERRE AUBRY ET AL., BOS. COLL. CTR. RET. RSCH., ESG INVESTING AND PUBLIC PENSIONS: AN UPDATE 3 (2020), https://crr.bc.edu/wp-content/uploads/2020/10/SLP74.pdf [https://perma.cc/H5KD-HLM2]; discussion *supra* Part I.C.

97. *Fifth Third Bancorp*, 573 U.S. at 419.

98. 29 U.S.C. § 1104(a)(2) ("In the case of an eligible individual accounts plan . . . the prudence requirement (only to the extent that it requires diversification) . . . is not violated by acquisition or holding of . . . qualifying employer securities. . . .").

99. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 418–19 (2014).

100. GARY BOREN & NORMAN STEIN, *§ 15:18. Fiduciary Topical Issues—Investment in Employer Securities; Diversification Rights*, *in* QUALIFIED DEFERRED COMPENSATION PLANS (2021) (noting that *Fifth Third* "essentially bars breach of prudence claims based on public information, regardless of whether those claims are based on the over-valuation of the stock or on excessive risk related to a stock").

101. Academics have shown that oil and gas had reached their maximum energy-return-on-investment (EROI) in the 1930s and 40s, with a markedly declining EROI since. Consequently, it seems reasonable to infer that production will soon have to shift to energy sources with greater EROI. *See* Victor Court & Florian Fizaine, *Long-Term Estimates of the Energy-Return-on-Investment (EROI) of Coal, Oil, and Gas Global Productions*, 138 ECOLOGICAL ECON. 145 (2017). Note that even though oil companies performed very well in 2022, it doesn't suggest a sustainable investment for investors with long-term horizons. *See, e.g.*, Steven Dudash, *ESG Investors Should Support Big Oil*, FORBES (Sep. 30, 2022), https://www.forbes.com/sites/greatspeculations/2022/09/30/esg-investors-should-support-big-oil/?sh=4634b599334e [https://perma.cc/9QK5-SA3W] (arguing for ESG investors to support Big Oil until there are scaled alternatives, but noting that "at the end of the day, most new power projects are renewables regardless of [where] you live").

102. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 426–30 (2014).

plaintiff must sufficiently allege that a prudent fiduciary in the defendant's position could not have concluded that either stopping purchases of employer stock or disclosing negative information about the company would do more harm than good.[103] The vague "more harm than good" threshold may have created a nebulous area for pleading standards, leaving it to the discretion of lower courts to decide whether a complaint offers a sufficient alternative.[104] Many courts have taken strict approaches to the Court's standard. In dismissing an ESOP claim, the Fifth Circuit, for example, ruled that plaintiffs have the "significant burden" of proposing an alternative action clearly more likely to help the plan than hurt it.[105] *Fifth Third*'s legacy is hence a complicated one.

Other circuits have either rejected *Fifth Third*'s pleading standard or failed to choose a standard altogether. The Second Circuit revisited the issue in *Jander v. Retirement Plans Committee of IBM*, another case involving the alleged investment of overvalued employer stock in an ESOP plan.[106] The court split from other circuits by interpreting *Fifth Third* in favor of the plaintiffs.[107] In so doing, however, the Second Circuit failed to choose a standard, because the plaintiffs would succeed using either choice identified by the court.[108] Reviewing the Second Circuit's decision on appeal, the Supreme Court also failed to delineate plaintiffs' pleading standards.[109] More recently, in *Hughes v. Northwestern University*, the Seventh Circuit interpreted the high *Fifth Third* pleading standard as only applying for fiduciary breach claims against ESOP fiduciaries—another ostensibly plaintiff-friendly ruling.[110] It remains to be

103. *Id.*

104. *See, e.g.*, Nicholas Wamsley, *Regulatory Monitor: ERISA Update*, 26 INV. LAW. 31 (2019) ("Participants in dozens of suits strove mightily to articulate the alternative actions that fiduciaries could take that, under this standard, would not have done more harm than good. Every circuit court rejected those efforts . . . [until] the Second Circuit. . . .").

105. Whitley v. BP, P.L.C., 838 F.3d 523, 529 (5th Cir. 2016).

106. Jander v. Ret. Plans Comm. of IBM, 910 F.3d 620 (2d Cir. 2018).

107. Jordan Mamorsky, *The Implications of the Supreme Court's Acceptance of Certiorari in IBM and Intel and What It Means for the Future of ERISA Litigation*, 35 J. COMPENSATION AND BENEFITS 12 (2019).

108. *Jander*, 910 F.3d at 628. The Second Circuit noted that, based on the Court's standard formulations in *Fifth Third*, courts may have to ask what an *average* prudent fiduciary may have thought about alternative actions *or* what *any* prudent fiduciary may have thought about alternative actions. *Id.* at 626.

109. Ret. Plans Comm. of IBM v. Jander, 140 S. Ct. 592, 595 (2020) ("The Second Circuit 'did not address the[se] argument[s], and for that reason, neither shall we.'") (citing F. Hoffman-La Roche Ltd. v. Empagran S. A., 52 U.S. 155, 175 (2004)).

110. Hughes v. Northwestern, 63 F.4th 615 (2023).

seen whether other circuits, or indeed the Supreme Court, will adopt this narrow reading. *Fifth Third* and *Jander*, and now to a lesser extent *Hughes*, are thus notable for perpetuating the ongoing ambiguity for ESOP plaintiffs, diminishing the opportunities for related lawsuits, and stifling the possibility for societal dialogue on ESG and fiduciary rules that may otherwise arise following judicial review of these plans' strategies and choices.[111]

Soon after *Jander*, the Supreme Court heard *Thole v. U.S. Bank*.[112] In *Thole*, the plaintiffs were retired participants of U.S. Bank's DB plan who alleged breaches of the duties of prudence and loyalty, despite receiving their pension payments without issue.[113] The Supreme Court ruled that they did not have standing to bring this claim, distinguishing DB pensioners from others because the plans' structure meant that employers receive surplus funds *after* benefits are paid.[114] It concluded that DB beneficiaries cannot suffer actual injuries traceable to alleged DB fiduciary breaches if they received their defined benefits. Accordingly, the Court held that these plaintiffs did not have standing pursuant to Article III.[115]

Though consistent with jurisprudence on actual versus speculative injuries, *Thole*'s holding on standing is nevertheless grim for pension plaintiffs bringing fiduciary breach claims. If litigation would not change the amount of money a plaintiff would

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111. *See, e.g.*, Susan Wnukowska-Mtonga, *The Real Impact of Impact Litigation*, 31 FL. J. INT. L. 121, 122 (2019) ("Despite [risks of unfavorable decisions or upholding bad laws], a case may nevertheless bring about change by bringing attention to . . . issues."); Prasiddha Pandey, Judicial Review in Supreme Court and Social Change—Implicating Changes through Judiciary 1–2 (May 11, 2012) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2568974 [https://perma.cc/VZE9-RHW8] ("[Legislation] generally succeeds in solving most of the problems but some issues manage to filter and reach to judiciary. . . . The rationality behind the active participation of the judiciary in the judicial review is that change in social condition is felt immediately by the judiciary as the cases arising because of the gap in the law and the social condition is brought before it. . . ."); *see also generally* Erin Myers, *The Manipulation of Public Opinion by the Tobacco Industry: Past, Present, and Future*, 2 J. HEALTH CARE L. & POL. 79 (1998) (a practical example of the previous sources in this footnote, discussing the influence of tobacco litigation on public opinion of tobacco and vice versa); Cynthia Nixon et al., *Mediated Visibility and Public Environmental Litigation: The Interplay between Inside and Outside Court during Environmental Conflict in Australia*, 10 LAWS, no. 35, 2021 (another application of the first source in this footnote, explaining how Australian environmentalists were able to leverage litigation against a mining company to gain support for their cause).

112. Thole v. U.S. Bank, 140 S. Ct. 1615, 1615 (2020).

113. *Id.* at 1618.

114. *Id.* at 1619–20.

115. *Id.* at 1620.

be entitled to under a plan, a plaintiff is unable to sue a trustee even if the trustee may have acted imprudently.[116] Notably, this reduces opportunities to preempt potential trustee wrongdoing. It may even promote it, since the bar for imposing legal liability for wrongdoing is so high. Additionally, the standing requirement effectively limits the pool of potential ERISA plaintiffs to private-sector DC pensioners, further narrowing opportunities to scrutinize a pension's ESG processes.[117] The language from Justice Thomas' concurrence in *Thole* is also cause for concern. There, Justice Thomas stated unequivocally that "none of the [privacy] rights identified by petitioners belong to them. The fiduciary duties created by ERISA are owed to the plan, not petitioners."[118] This declaration wholly denies the existence of a private right to enforce ERISA duties.

A private right to enforce ERISA's fiduciary duties affords pensioners greater latitude to seek legal recourse in the event of trustee wrongdoing.[119] Trustee wrongdoing may, in the eyes of pensioners, include ignoring ESG criteria in investing decisions.[120] But if pensioners no longer have a right to information concerning their money once it goes in a pension plan, they may not be made aware of the investment processes used and whether or not these processes include the consideration of ESG criteria.[121] And if

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116. *See* Lee, *supra* note 90, at 35 (discussing how, since 2015, litigation has enabled DC plan participants to scrutinize fiduciaries for poor investment decisions or monitoring processes, but that DB plan participants will have difficulty doing the same post-*Thole*).

117. *See, e.g.*, *In re* Omnicom ERISA Litig., No. 20-CV-4141 (CM), 2021 WL 3292487, at *8 (S.D.N.Y. Aug. 2, 2021) ("*Thole* . . . has little or no relevance when evaluating standing ERISA cases concerning defined-contribution plans.").

118. Thole v. U.S. Bank, 140 S. Ct. 1615, 1623 (2020) (Thomas, J., concurring).

119. *See* Spokeo, Inc. v. Robins, 578 U.S. 330, 348 (2016) ("A plaintiff seeking to vindicate a statutorily created private right need not allege actual harm beyond the invasion of that private right."); Caroline Newcombe, *Implied Private Rights of Action: Definition, and Factors to Determine Whether a Private Action Will Be Implied from a Federal Statute*, 49 LOY. U. CHI. L.J. 117, 120 (2017) ("A judicially created implied private right of action allows a private plaintiff to enforce a public statute, despite the fact that the statute itself contains no express right of action.").

120. *See, e.g.*, Jackie Stewart, *Why Retirees Who Don't Consider ESG Investing Are Making A Big Mistake*, KIPLINGER (Nov. 18, 2021), https://www.kiplinger.com/retirement/retirement-planning/603772/why-retirees-who-dont-consider-esg-investing-are-making-a-big-mistake [https://perma.cc/VB9P-SMD7] ("You've spent your entire life fighting for a cause. . . . Now those causes seem to matter more than ever. 'Older people may feel a greater urgency because it's their legacy. . . . They aren't going to be in the workforce working . . ., but their assets can continue working for a better world.'").

121. *See, e.g.*, *id.* ("'Not all funds advertised as ESG friendly really are. You have to investigate whether they walk the walk.' For instance, you might check an ESG fund's prospectus for the investing criteria, [Fran] Teplitz (executive at a nonprofit promoting ethical investing) says.").

pensioners do not know about these processes, they can neither lobby to change them nor sue if they believe that ignoring ESG considerations violates trustees' duty of prudence.[122] Even if it is true that such ERISA suits may not be successful given current jurisprudence, the opportunity to publicly debate the fiduciary rules is invaluable and may well catalyze reform.[123] Pensioners' limited rights to information about pensions' investment decisions, combined with their fewer opportunities to sue for pension trustees' fiduciary breaches, may have crystallized the trend of pensions foregoing ESG.

II. PENSIONS' INSTITUTIONAL BARRIERS TO ESG INVESTING

As discussed in Part I *supra*, the Theory of Universal Ownership offers compelling justifications for leveraging pensions' sizable capital for ESG goals. This Part explains why an entirely new vehicle might be needed to prosocially distribute pension money. First, Part II explores the primary forces preventing pensions from effectively allocating capital to ESG through their narrow interpretation of ERISA rules. It then examines state laws that expressly prohibit or otherwise limit ESG investments. Finally, it reviews other barriers to meaningful ESG investment, including the widely differing ideas about ESG and the difficulties of institutional inertia. Together, these factors prevent pension capital from being used more productively—that is, in ways that offer strong returns for pensioners *while also* accomplishing social goals.

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122. *See, e.g.*, Randy Bauslaugh & Hendrik Garz, *Pension Fund Investment: Managing Environmental, Social, and Governance (ESG) Factor Integration*, MCCARTHY TETRAULT (May 1, 2019), https://www.mccarthy.ca/en/insights/articles/pension-fund-investment-managing-environmental-social-and-governance-esg-factor-integration [https://perma.cc/2R3D-88GG]. The law firm McCarthy Tetrault advises pension fiduciaries to keep their ESG disclosures broad and brief, approximately 4–5 sentences maximum. If pensioners have only these disclosures to rely on, and have no right to additional information, they cannot request alternative courses of action. *Id.*

123. *See generally, e.g.*, Douglas NeJaime, *Winning Through Losing*, 96 IOWA L. REV. 941, 941 (2011) ("[A]dvocates may use litigation loss (1) to construct organizational identity and (2) to mobilize constituents. . . . [J]udicial setbacks may, counterintuitively, contribute to the process of reform. . . .").

A. THE REINFORCEMENT OF NARROW ERISA INTERPRETATIONS

Together, ERISA, the Freshfields report, the Department of Labor (DOL), and the judiciary have created rigid fiduciary standards that, combined with pensions' strong regulatory embeddedness, would make any investor understandably wary of ESG.[124] All investment analyses must first comport with ERISA. Some believe incorporating ESG criteria into investing is equivalent to trustees acting on the bases of their own ethics, as opposed to acting in the financial interests of the beneficiaries exclusively.[125] The former technically violates the duty of loyalty.[126] Similarly, it can be difficult to prove that ESG investments cause no financial downside pursuant to the duty of prudence.[127] For instance, even though empirical data largely shows neutral to positive relationships between ESG and financial returns, there are mixed opinions about the effects of the processes used to integrate ESG into investment.[128] Interestingly, it is not uncommon to forego financially uncertain, but otherwise prosocial, investments while maintaining antisocial investments that may be equally financially uncertain. For example, currently fourteen public pensions invest over $80 billion in fossil fuel companies,[129] despite these companies' negative environmental impacts and doubtful future financial outlooks.[130] This paradox arises because

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124. Lachance & Stroehle, *supra* note 47, at 2, 12–16.

125. Max Schanzenbach & Robert Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee*, 72 STAN. L. REV. 381, 401, 409, 436 (2020).

126. *Id.* at 388.

127. Lachance & Stroehle, *supra* note 47, at 7–8.

128. Andreas Hoepner et al., Does Pension Funds' Fiduciary Duty Prohibit the Integration of Environmental Responsibility Criteria in Investment Processes?: A Realistic Prudent Investment Test 4 (Sept. 19, 2011) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1930189 [https://perma.cc/AE6D-X429] (finding that incorporating ESG into investment processes can be done without any harmful effects); Olga V. Efimova, *Integrating Sustainability Issues into Investment Decision Evaluation*, 7 J. REV. GLOBAL ECON. 668, 680 (2018) (finding that lack of standardized data, information comparability, limited tools, and more may make the process of incorporating ESG into investment criteria quite difficult and cause adverse financial effects).

129. CLIMATE SAFE PENSIONS, THE QUIET CULPRIT: PENSION FUNDS BANKROLLING THE CLIMATE CRISIS 1 (2021), https://climatesafepensions.org/wp-content/uploads/2021/12/CSPN-The-Quiet-Culprit.pdf [https://perma.cc/7CSK-MF52].

130. It is true that fossil fuels make lucrative investments in the short term, and perhaps even in the long-term depending on the horizon; for instance, a recent report found that oil and gas companies have delivered a staggering $2.8 billion per day in pure profits. Damian Carrington, *Revealed: Oil Sector's Staggering $3bn-a-Day Profits for Last 50 Years*,

many investors have taken a stringent view of the ERISA-prescribed duty of prudence, emphasizing that "a trustee employing a risk-return ESG strategy must reasonably conclude that the strategy will in fact provide *better* returns for the *same or less* risk."[131]

After ERISA, investors must contend with the 2005 Freshfields report, which remains an influential analysis on fiduciary duties and informs how many investors approach ERISA in the context of ESG investing.[132] ESG proponents often cite the report for the statement, "there appears to be no bar to integrating ESG considerations into the day-to-day process of fund management, provided the focus is always on the beneficiaries/purposes of the fund and not on unrelated objectives."[133] Yet the report simultaneously concludes that the duty of prudence precludes trustees from considering ESG if doing so produces any detrimental financial effects.[134] Its additional assessments may have further deterred adoption of ESG criteria into investment processes.[135]

GUARDIAN (July 21, 2022), https://www.theguardian.com/environment/2022/jul/21/revealed-oil-sectors-staggering-profits-last-50-years [https://perma.cc/KVU7-4YXY]. However, new developments may lead to an aggressive transition away from fossil fuels. For example, the International Energy Agency recently published a report indicating that the global energy crisis prompted by the Russian invasion of Ukraine has forced countries to try to electrify their heat and transport sectors more rapidly than ever. INTERNATIONAL ENERGY AGENCY, WORLD ENERGY OUTLOOK 2022 (Oct. 2022), https://www.iea.org/reports/world-energy-outlook-2022/executive-summary [https://perma.cc/6QQ6-JS8Z]. The report further states that global use of oil, natural gas, and coal, which has been steadily growing since the 1970s, will peak by 2025. *Id.* at 28, 43, 296. Under existing policies, the growth will plateau. *Id.* at 21. If policies change to even conservatively address climate change, however, usage of each will decline. *Id.* at 43, 53, 327, 367.

131. Schanzenbach & Sitkoff, *supra* note 125, at 426 (emphasis added).

132. The report's staying power largely stems from its status as the first prominent publication to clearly address ESG in investing, and further still to actively promote inclusion of ESG criteria in investing (if one liberally interprets the report). Hoepner et al., *supra* note 128, at 2 ("[A] report by Freshfields Bruckhaus Deringer gained prominence for its precise analysis of [the conditions under which ESG consideration is permissible]. . . . [The] conclusions of the Freshfields report have provided a lot of conceptual clarity. . . .").

133. FRESHFIELDS, *supra* note 69, at 8; *see also Fiduciary Duty in the 21st Century*, FIDUCIARY DUTY (2021), https://www.fiduciaryduty21.org/about.html [https://perma.cc/9F7M-LT9Q] ("[The Freshfields report] became the single most effective document for promoting the integration of ESG issues into institutional investment.").

134. *See* FRESHFIELDS, *supra* note 69, at 10–12.

135. *See, e.g.*, Sandberg, *supra* note 46, at 144 ("The Freshfields report . . . rules out exactly the kind of SRI which proponents . . . hold in the highest regard (proactive cases and socially effective investment strategies)."); Hoepner et al., *supra* note 128, at 1 ("The 2005 Freshfields report concluded that pension funds' fiduciary duties . . . only permit the consideration of ESG criterion, only if this process has no detrimental financial effects.").

To understand why, consider Joakim Sandberg's statement: "The Freshfields report seems to allow institutional investors to at least *sometimes* take *some* ESG considerations into account."[136] Sandberg points to three situations in which it might be possible for institutional investors to consider ESG: (1) when weighing investments with exactly the same financial characteristics; (2) when ESG considerations are financially relevant; and (3) when they believe that beneficiaries would unanimously support taking particular ESG factors into account.[137]

The problem with the first scenario, of course, is that such instances are rare if not nonexistent—a fact Sandberg acknowledges.[138] Damning to the second scenario is the fact that the reasoning[139] the report employs to connect climate change to financial value may be used to link any number of other ESG considerations to financial value. The infinite number of such links effectively render this pathway to ESG investing unactionable,[140] and often enables detractors to argue against ESG altogether.[141] Finally, the third scenario poses pragmatic difficulties because identifying and classifying the will of all beneficiaries is often infeasible.[142] This practical infeasibility may prove especially true post-*Thole*. In the wake of *Thole*, pensioners' information rights are in question and they may consequently be unaware of the investment processes utilized by their pensions' decision makers.

The Department of Labor acts as an additional influence on ERISA interpretation through its rule-making process. DOL's

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136. Sandberg, *supra* note 46, at 144.

137. *Id.* at 146–47.

138. *Id.* at 148–49.

139. The report frequently alludes to the intangible benefits of ESG-conscious investment that are likely to have a material impact on financial performance, as well as the potential financial downsides of purely profit-conscious, shortsighted investment. FRESHFIELDS, *supra* note 69, at 11 ("It is increasingly difficult for investment decision-makers to claim that ESG considerations are too difficult to quantify when they readily quantify business goodwill and other equivalently nebulous intangibles. . . .").

140. *See id.*

141. *See, e.g.*, Sandberg, *supra* note 46, at 150–52; Kenneth P. Pucker & Andrew King, *ESG Investing Isn't Designed to Save the Planet*, HARV. BUS. REV. (Aug. 1, 2022), https://hbr.org/2022/08/esg-investing-isnt-designed-to-save-the-planet [https://perma.cc/HQ3G-HRKF] (noting that a key reason ESG investing may be ineffective is because there is no standardized definition of what it means, and its broad nature enables disingenuous greenwashing from investors).

142. *See* Sandberg, *supra* note 46, at 152–54.

support for ESG-inclusive investment processes appears to wax and wane with different presidential administrations:

> During Democratic administrations, the DOL generally views ESG as not inconsistent with ERISA's fiduciary duties and as capable of being applied in a manner that is loyal to ERISA plan interests. Conversely, the DOL under Republican administrations has been resistant to ESG as an appropriate investment factor, and, especially, more cautious that such factors can be used without violating ERISA's duties, especially the duty of loyalty.[143]

Indeed, under President Trump, the DOL finalized a rule that effectively prohibited pension managers from considering ESG unless they could demonstrate without a doubt that the plan's financial goals would be protected.[144] This proposal, however, was ultimately reversed.[145] Less than one year after the Trump DOL rule was finalized, the Biden DOL proposed a rule that seems to require fiduciaries to consider the economic impacts of climate change and other ESG criteria.[146] The DOL's political pendulum swings emphasize the fragile nature of the already-minimal protections for ESG considerations in investment decisions.

Once investors have adjusted their behavior to account for ERISA, the Freshfields report, and DOL's interpretations of the Act, courts may act as an additional, ex-post fiduciary authority on the choices they make. Already, very few cases of fiduciary breach are actually adjudicated because of the heightened pleading standards laid down in *Fifth Third*, *Jander*, and *Thole*.[147] But for

143. Celia A. Soehner & Elizabeth S. Goldberg, *ERISA and the Challenges of Using ESG in Retirement Plan Investing*, REUTERS (Sept. 20, 2021, 12:08 PM), https://www.reuters.com/legal/legalindustry/erisa-challenges-using-esg-retirement-plan-investing-2021-09-20/ [https://perma.cc/FJF4-V3X3].

144. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72846, 72851–83 (proposed Nov. 13, 2020); *see also* Kristina M. Zanotti et al., *Trump Era DOL Rules—Will They Remain Under a Biden Administration?*, NAT'L L. REV. (Jan. 4, 2021), https://www.natlawreview.com/article/trump-era-dol-rules-will-they-remain-under-biden-administration. [https://perma.cc/6AFQ-WY85].

145. *See The DOL Pendulum Swings on ESG, but How Far Remains to Be Seen*, DEBEVOISE & PLIMPTON (Oct. 15, 2021), https://www.debevoise.com/insights/publications/2021/10/the-dol-pendulum-swings-on-esg-but [https://perma.cc/87BW-HW5E].

146. *See id.*; *see also* Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 86 Fed. Reg. 57272, 57276–84 (Oct. 14, 2021) (to be codified at 29 C.F.R. pt. 2550).

147. *See supra* Part I.D.

those claims that see the court room, the probability of a court ultimately finding a fiduciary breach under ERISA is slim: process, not result, is the key in these cases.[148] The courts' emphasis on process means that relying on MPT is usually enough for a fiduciary to withstand judicial scrutiny despite the new scholarship questioning many of the theory's tenets.[149] As discussed in Part I *supra*, the infrequency of these ERISA suits diminishes opportunities for societal discourse around ESG investing by denying the courts the opportunity to consider new ERISA interpretations via amicus briefs and expert testimony, and denying the public from engaging with the courts' treatment of these interpretations.[150] The lack of societal debate, in turn, likely institutionalizes the archaic belief that ESG investing is incompatible with ERISA. In short, through the various pathways that reinforce narrow interpretations of the ERISA rules, trustees often feel inclined to forego prosocial investment through ESG investing.

B. ANTI-ESG STATE LAWS

In 2022, many states began adopting legislation to inhibit or materially limit state pensions from investing with ESG strategies or from doing business with firms adopting specific ESG policies.[151]

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148. *See* Sweda v. Univ. of Pa., 923 F.3d 320, 329 (3d Cir. 2019) ("A court assesses a fiduciary's performance by looking at process rather than results. . . .").

149. *See* Alon Brav & J.B. Heaton, *Brown Assets for the Prudent Investor*, 12 HARV. BUS. L. REV. ONLINE, art. 2, 2021, at 19 ("The lesson of modern portfolio theory is that additional assets that are not redundant with other assets are almost always valuable in creating portfolios with better risk-return tradeoffs. . . . [Avoiding brown assets] could violate ERISA's diversification requirement."); *see also supra* Part I.C.

150. *See, e.g.*, Ruben J. Garcia, *A Democratic Theory of Amicus Advocacy*, 35 FLA. ST. U. L. REV. 316, 341, 354 (2008) ("Social movement organizations use amicus briefs to communicate to their constituencies and the general public. . . . With respect to amicus briefs in the trial courts, there is always the opportunity for the judge to seek testimony from experts. . . ."); Made Schachter, *The Utility of Pro-Bono Representation of U.S.-Based Amicus Curiae in Non-U.S. and Multinational Courts as a Means of Advancing the Public Interest*, 28 FORDHAM INT'L. L. J. 88, 100, 104–05 (2004) ("*Amici* thereby assist judges with their efforts to more fully grasp the applicable substantive law and pragmatic implications. . . . Even when a court rejects an *amicus*' position, its decision may reflect consideration of the arguments put forth."); *supra* Part I.D, pp. 17, 19–20; *supra* notes 108–109, 117–121 and accompanying text.

151. *See* Lance Dial et al., *The Challenge of Investing in the Face of State Anti-ESG Legislation*, REUTERS (Aug. 24, 2022, 10:02 AM), https://www.reuters.com/legal/legalindustry/challenge-investing-face-state-anti-esg-legislation-2022-08-24/ [https://perma.cc/82ZK-H463].

These so-called "Anti-ESG Bills" differ in scope and coverage.[152] Despite these differences, these bills generally fall into one of two main categories: (1) prohibitions on the state's doing business with financial institutions that "discriminate against" companies in particular industries ("Boycott Bills"), and (2) prohibitions on using state funds for "social investment" ("No Social Investment Bills").[153] Legislators justify these Boycott and No Social Investment Bills by arguing that companies that refuse to do business with in-state companies indirectly harm state residents and, therefore, should not benefit from state investment or state contracts.[154]

So far, North Dakota has enacted a No Social Investment Bill, and a few other states seem poised to follow suit.[155] Meanwhile, at least seventeen states have introduced, are debating, or have enacted Boycott Bills, including prohibitions of "discrimination against" firearms (Ohio), fossil fuels (West Virginia), agriculture (Idaho), or lumber (Minnesota).[156] Some states require divestment from entities in violation of an Anti-ESG Bill, others require state contracts to include express representations that a party doing

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152. *See, e.g.*, *id.* ("Some states have Anti-ESG Bills mandating just one of the above actions [prohibiting use of state funds for social investment and requiring the state to divest from entities that "boycott" particular industries, such as fossil fuels], and other states have bills mandating both. . . . [O]n the one hand, states such as Utah (H.B. 312), Minnesota (H.F. 4574), South Carolina (H.B. 4996), and Idaho (H.B. 737) have proposed Anti-ESG Bills limiting state contracting with companies that refuse to finance energy companies, but have no legislation related to the firearms industry. On the other hand, states such as Wyoming (H.B. 0236), Arizona (H.B. 2473), Missouri (S.B. 1048), South Dakota (S.B. 182), and Ohio (H.B. 297) have proposed Anti-ESG Bills targeting companies that supposedly discriminate against the firearms industry, but no legislation related to the energy industry."); *see also* 2021 Tex. Sess. Law Serv. Ch. 529 (S.B. 13) (codified at TEX GOV'T CODE ANN § 809.001 et seq.).

153. *See* Dial et al., *supra* note 151.

154. *See id.*

155. *See id.*; N.D. CENT. CODE ANN. § 21-10-08.1 (West 2021); Press Release, Ron DeSantis, Governor of Florida, Governor Ron DeSantis Announces Legislation to Protect Floridians from the Woke ESG Financial Scam (Feb. 13, 2023), https://www.flgov.com/2023/02/13/governor-ron-desantis-announces-legislation-to-protect-floridians-from-the-woke-esg-financial-scam/ [https://perma.cc/H5ES-PJAT]; *see generally* DEBEVOISE & PLIMPTON, STATE LEVEL ESG DEVELOPMENTS TRACKER, https://www.debevoise.com/-/media/files/pdf/statelevel_esg_investment_developments_tracker2.pdf?la=en&rev=4aebf20b8a0249d099d76a148835a893&hash=69D8161DA413AFD2CA8E74C565A63B4C [https://perma.cc/RA4G-U22Q] (last updated Mar. 1, 2023).

156. *See* Dial et al., *supra* note 151; Leah Malone et al., *ESG Battlegrounds: How the States Are Shaping the Regulatory Landscape in the U.S.*, HARV. LAW SCHOOL FORUM ON CORP. GOVERNANCE (Mar. 11, 2023), https://corpgov.law.harvard.edu/2023/03/11/esg-battlegrounds-how-the-states-are-shaping-the-regulatory-landscape-in-the-u-s/ [https://perma.cc/4897-EEB4].

business with the state does not discriminate against the protected entities, and still other states require both.[157]

This new legislative trend poses a problem for investors. The major challenge lies in determining whether an investment strategy that considers ESG risk constitutes an industry "boycott" or "social" strategy as defined by a state's Anti-ESG Bill.[158] One article notes the interpretive questions, like the bills that raise them, are new.[159] It is entirely possible, for instance, that a financial institution could offer ESG products that "discriminate against" an industry while simultaneously offering products in support of a protected industry, and consequently insulate itself from Anti-ESG Bill repercussions.[160] Nevertheless, the advent of these bills will likely further discourage pensions from adopting ESG strategies or investing in ESG vehicles.

C. OTHER BARRIERS

Varied ESG standards and institutional inertia present additional hurdles for ESG investing. Advocates for ESG-inclusive investment processes are vague about what these processes should actually entail, creating confusion and mixed results. For example, some funds are classified as ESG funds[161] simply because they deal with value stocks instead of growth stocks.[162] Others may be classified this way because they focus exclusively on renewable energy stocks. Still others operate with alternative

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157. *See id.*
158. *See id.*
159. *See, e.g.*, *id.*
160. *See id.*
161. ESG funds are investment vehicles that supposedly use ESG criteria to inform composition and asset allocation. *Environmental, Social and Governance (ESG) Funds—Investor Bulletin*, SECS. AND EXCH. COMM'N (Feb. 26, 2021), https://www.sec.gov/oiea/investor-alerts-and-bulletins/environmental-social-and-governance-esg-funds-investor-bulletin [https://perma.cc/4XGB-WST6].
162. Value stocks tend to maintain a consistent market value, enabling investors to profit from dividends, while growth stocks tend to be more volatile, enabling investors to profit from significant price appreciation. *See* Rebecca Baldridge, *Growth vs. Value Stocks: Which Is Right For You?*, FORBES: ADVISOR (Oct. 27, 2022, 2:52 PM), https://www.forbes.com/advisor/investing/value-vs-growth-stocks/ [https://perma.cc/3NFP-HC6]. Note that these fund positions simply stretch the definition of "ESG," enabling investors to enjoy the marketing benefits of the ESG trend while keeping ESG investing at arm's length in practice.

strategies that may or may not have an ESG ethos in practice.[163] Within these discrete classifications of entities is additional confusion about the classification of individual investments. Some believe a firm's divestment from fossil fuels makes the firm a "green" investment, while others caution that divestment "simply transitions ownership of these assets to some other, perhaps less environmentally conscious, owners"[164] and may not see the firm as "green" on the basis of its divestment.[165] The dynamic, complex web of classifications no doubt makes ESG investing nonviable for many investors irrespective of the laws, regulations, and judicial holdings on point.

Cultural inertia due to institutional structure may also prevent pensions from wholly embracing ESG. Pensions often "lack internal capabilities and are under-resourced."[166] Perhaps because of these constraints, pension managers are also known to be inattentive.[167] More problems foment because pensions uniquely utilize investors acting solely out of legal obligations as opposed to personal interests.[168] Meanwhile, the principal-agent relationship between pensions and asset managers consists of significant feedback loops and a low signal-to-noise ratio.[169] Consequently, while many asset managers attempt to respond to the changing investment landscape, they are ultimately constrained by

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163. *See* R. BOFFO & R. PATALANO, OECD PARIS, ESG INVESTING: PRACTICES, PROGRESS, AND CHALLENGES 32 (2020), https://www.oecd.org/finance/ESG-Investing-Practices-Progress-Challenges.pdf [https://perma.cc/J929-DWR8].

164. Luba Nikolina, *Global Pensions and ESG: Is There A Better Way?* 7 (Wharton Pension Rsch. Council, Working Paper No. 2021-17, 2021), https://repository.upenn.edu/cgi/viewcontent.cgi?article=1715&context=prc_papers [https://perma.cc/5SYD-DJ4F].

165. *See, e.g.*, Larry Fink, Chairman, BlackRock, Keynote Address at the MIT Golub Center for Finance and Policy Conference: Financial Policy and the Environment (Oct. 21, 2021), https://mitsloan.hosted.panopto.com/Panopto/Pages/Viewer.aspx?id=7d4b3b48-cca3-4a8e-8c00-adc801435b75 [https://perma.cc/3Q73-E49V] ("Keep in mind, if a foundation or an insurance company or a pension fund says, 'I'm not going to own any hydrocarbons,' well, somebody else is, so you're not changing the world.").

166. Nikolina, *supra* note 164, at 13.

167. *See generally* William Samuelson & Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. RISK & UNCERTAINTY 7 (1988); Brigitte Madrian & Dennis Shea, *The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*, 116 Q. J. ECON. 1149 (2001); Carolina Lindholm et al., *How Individual Savings Respond to Pension Reform: Implications for Models of Savings Behavior* 5 (Nov. 11, 2022), http://papers.markuspeters.com/JMP.pdf [https://perma.cc/DBU8-DYQL] (discussing how inattentive pension agents do not consider changes to the pension system when making choices).

168. Magnus Dahlquist & José Vincente Martinez, *Investor Inattention: A Hidden Choice of Cost in Pension Plans*, 21 EUR. FIN. MGMT. 1, 2 (2015).

169. *See* Nikolina, *supra* note 164, at 11.

pensions.[170] The top-down limitations on pensions, combined with the increasingly competitive nature of the asset management industry, creates a pension-manager relationship "heavily influenced by short-term results that are rarely due to skill."[171] These assorted structural problems have birthed a pension industry that regularly lags behind the rest of the financial services sector and is unable to deal with the institutional costs of industry-wide change. In short, the pension industry is "slow to adapt, adopt, or innovate."[172]

As the need to meet ESG goals becomes more urgent, it is worth questioning whether pensions can be counted on to evolve quickly enough to ensure their massive capital is adequately deployed to ESG ends. Current practice makes this doubtful. Peradventure then, given their pervasive institutional inertia, perhaps pensions are better served by searching for a new kind of investment, one that can overcome their significant regulatory burdens and the confusion created by the varying ESG standards.

III. PUBLIC BANKS AS PRODUCTIVE INVESTMENTS FOR PENSION FUNDS

In lieu of turning to existing private-sector solutions, pension funds should look to public banks as the solution to their ESG problems, as these banks would effectively allow them to outsource ESG considerations. To many in business, politics, and academia, government intervention is only proper when the private market produces suboptimal results.[173] The current precarious, antisocial pension investment architecture justifies a public or quasi-public solution that expands on existing public-sector interventions. This Part recommends that pensions need a sound, long-term investment that would accord with both social goals and their regulatory burdens. By meeting community needs, public banks

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170. *See id.*

171. *Id.*

172. Gordon Clark & Roger Urwin, *Innovative Models of Pension Fund Governance in the Context of the Global Financial Crisis*, 15 PENSIONS: AN INT'L J. 62, 66 (2010).

173. *See, e.g.*, YOLANDA KODRZYCKI & TAL ELMATAD, NEW ENG. PUB. POL'Y CTR., THE BANK OF NORTH DAKOTA: A MODEL FOR MASSACHUSETTS AND OTHER STATES? 4 (2011), https://www.bostonfed.org/publications/new-england-public-policy-center-research-report/2011/the-bank-of-north-dakota-a-model-for-massachusetts-and-other-states.aspx [https://perma.cc/VFB9-D55M].

can generate positive financial returns for pensions, and positive externalities for pensioners' and society's benefit.

A. A PUBLIC-SECTOR SOLUTION IS DEMOCRATICALLY IMPORTANT

Should pensions wish to allocate more capital to ESG, they currently have two available options: They can either (1) screen for products or funds on the market that more closely align with their investment goals, or (2) direct their focus to ESG funds. Investing in an ESG fund seems comparatively more useful than the former, and such entities would likely meet pensions' ERISA requirements. There are compelling justifications, however, for shifting more public policy influence from private-sector actors, like ESG funds, to partially or wholly public-sector ones, like public banks. First, as one commentator notes, "[t]hinking that fiddling around in the financial markets is going to . . . [help] with broad social problems . . . is simply bonkers."[174] Given the inherent tension usually present between public- and private-sector goals, it is impractical and undesirable for private actors to take the reins of public needs.[175]

Second, allowing or expecting the private sector to assume responsibility for public policy "breaks the link between representative government and electoral accountability . . . and concentrates control over the direction of public policy among a cadre of institutional investors and corporate managers neither equipped with democratic legitimacy nor necessarily expert in the issues over which they hold disproportionate sway."[176] The United States no doubt has a tradition of strong private-sector political influence.[177] But given the current inflection point in the pension

174. Robert Armstrong, Opinion, *The ESG Industry is Dangerous*, FIN. TIMES (Aug. 24, 2021), https://www.ft.com/content/ec02fd5d-e8bd-45bd-b015-a5799ae820cf [https://perma.cc/CS5J-RD9R].

175. *See, e.g.*, Kenneth Lux, *The Failure of the Profit Motive*, 44 ECOLOGICAL ECONS. 1 (2003) (arguing that a profit motive is anathema to the common good); *see also* Aneesh Raghunandan & Shiva Rajgopal, *Do ESG Funds Make Stakeholder-Friendly Investments?*, 27 REV. ACCT. STUD. 822, 822 (2022) (noting that ESG funds "do not appear to follow through on proclamations of concern for stakeholders").

176. Richard Shinder, Opinion, *ESG Investing May Be in Vogue, but Beware—There's Plenty Not to Like About It*, HILL (Oct. 6, 2021, 7:00 AM), https://thehill.com/opinion/finance/574829-esg-investing-may-be-in-vogue-but-beware-theres-plenty-not-to-like-about-it/ [https://perma.cc/8JVG-8X6V].

177. *See, e.g.*, Martin Gilens & Benjamin Page, *Testing Theories of American Politics: Elites, Interest Groups, and Average Citizens*, 12 PERSPS. ON POLS. 564 (2014) (the landmark

landscape, with so many pension futures uncertain[178] and a dire need to pivot some institutional capital to prosocial ends,[179] it is worth considering a paradigm shift of private-sector influence in this realm. Allowing ESG fund managers to direct massive capital flows to prosocial policies of their choice—even simply letting these managers define what a "prosocial" policy looks like—is arguably unjust, as it puts consequential decisions of enormous impact in the hands of only a select few whose interests may be adverse to the those of the general public.[180] Decisions that impact a community, state, or country are best left to its residents.[181] Some public or quasi-public entity with democratic oversight should influence large capital flows, even if the creation of such an entity might entail significant tangible and intangible start-up costs. Any sociopolitical changes that may follow from these capital movements can consequently occur as they were meant to—with the consent of the governed or their elected representatives.

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paper indicating the United States' political system best represents one of economic-elite domination or of biased pluralism, rather than majoritarian electoral democracy or majoritarian pluralism as is popularly thought).

178. *See, e.g.*, Joanna Biernacka-Lievestro & Joe Fleming, *States' Unfunded Pension Liabilities Persist as Major Long-Term Challenge*, PEW (July 7, 2022), https://www.pewtrusts.org/en/research-and-analysis/articles/2022/07/07/states-unfunded-pension-liabilities-persist-as-major-long-term-challenge [https://perma.cc/JU2Q-4SRB].

179. *See, e.g.*, Bernardo Bortolotti, Mind the (Investment) Gap: Fostering the Transition from ESG to Impact 2 (July 29, 2023) (unpublished manuscript), https://iris.unito.it/bitstream/2318/1895223/1/Mind%20the%20investment%20gap_%20Bortolotti%2015_7_22.pdf [https://perma.cc/Z9PW-YGDT] ("[M]eaningful progress in delivering on the [UN Sustainable Development Goals] can be achieved only with the engagement of the global asset management industry, and specifically of institutional investors that manage fifty-nine percent of the total assets.").

180. *See, e.g.*, Benjamin I. Page et al., *Democracy and the Policy Preferences of Wealthy Americans*, 11 PERSPS. ON POLS. 51 (2013) (highlighting that wealthy individuals exert more political influence than other citizens, and are more conservative than the general public regarding many important policies, which may account for why certain government policies seem to deviate from what the majority of U.S. citizens want); Meredith Booth, *Esg Professional Shortage Drives Salaries Higher for Funds Seeking Talent*, INV. MAG. https://www.investmentmagazine.com.au/2022/06/esg-professional-shortage-drives-salaries-higher-for-funds-seeking-talent/ [https://perma.cc/U2BJ-3U8B] (noting that salaries for ESG professionals have been increasing greatly since COVID, with head of research positions earning up to $300,000 annually).

181. *See* Renée A. Irvin & John Stansbury, *Citizen Participation in Decision Making: Is It Worth the Effort?*, 64 PUB. ADMIN. R. 55, 56–58 (2004) (noting several potential benefits of citizen participation, including better environmental management, lower litigation costs, public empowerment, increased policy education and awareness, and more).

B. PUBLIC BANKS AROUND THE WORLD

Today, over nine hundred public banks account for forty percent of the world's banking.[182] Public banks' biggest advantage, perhaps, is that they may be chartered to cater to a community's unique needs. Accordingly, public banking models vary extensively, from full-state ownership to partially-private, partially-public ownership.[183] Missions vary greatly—some public banks are pure investment banks with portfolio makeups and investment strategies dictated by their charters, others offer only basic financial services, and still others offer a mix of investment and financial services. With these different models and missions come different, corresponding regulations.[184] All public banks, however, operate with a general prosocial mission of regional betterment, and provide gap-filling in areas where the private sector fails to act, such as in retail or institutional financial services, infrastructure investment, or small business support.[185]

To better understand the wide range of public banking models, consider a few examples. The Banco Ciudad de Buenos Aires is a wholly-owned state bank funded through bond issuances and other forms of debt.[186] It is regulated by Argentine authorities just the same as the country's private banks.[187] Like private banks operating in Argentina, it is subject to certain public reporting requirements to promote transparency.[188] It also maintains an internal committee to oversee bank processes related to consumer protection.[189] Banco Ciudad collects city taxes, fees, and contributions, invests in local infrastructure, and more.[190] Its

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182. *See* Douglas Singleterry & Zenon Christodoulou, *Public Banks Help Communities Thrive. Why Aren't There More?*, HILL (Jan. 26, 2017, 7:00 PM), https://thehill.com/blogs/pundits-blog/finance/316403-public-banks-help-communities-thrive-why-arent-there-more [https://perma.cc/H2R7-LEKB]; Paige Curtis, *Public Banks Can Help Make Real Climate Progress. Why is There Only One in the U.S.?*, GRIST (May 23, 2022), https://grist.org/fix/opinion/nonprofit-state-owned-public-banks-climate-progress/ [https://perma.cc/3EE2-86R9].

183. *See* CYRUS A. VANCE CTR. FOR INT'L JUST., PUBLIC BANKING AROUND THE WORLD: A COMPARATIVE SURVEY OF SEVEN MODELS 5 (2021) https://www.vancecenter.org/wp-content/uploads/2021/10/Public-Banking-Around-the-World-A-Comparative-Survey-of-Seven-Models.pdf [https://perma.cc/D4B5-8PAJ].

184. *Id.*

185. *Id.*

186. *Id.*

187. *Id.*

188. *Id.*

189. CYRUS A. VANCE CTR. FOR INT'L JUST., *supra* note 183.

190. *Id.* at 7.

additional responsibilities include banking unbanked populations,[191] offering credit to small businesses, and promoting regional exports.[192]

In Canada, ATB Financial is a wholly-owned state bank that sustains itself with its profits.[193] Unlike Banco Ciudad, ATB enjoys a unique regulatory scheme, which includes rules in addition to the standard Alberta Treasury Branch regulations and the province's specific financial products regulations.[194] Its subsidiaries are subject to separate oversight.[195] ATB has a legislative mandate to provide the Province of Alberta with access to banking services, enhance competition in the financial services market, and provide returns comparable to those of similar financial institutions.[196]

German Savings Banks ("Sparkassen") are established by city or district authorities, but are fully independent of the government in their day-to-day operations.[197] Sparkassen are subject to specific regulations governing formation, contracting obligations, public mission, disclosures, and more.[198] They are also subject to regional ordinances.[199] They are not, however, subject to all of the same regulations as other EU banks; for instance, they are not overseen by the European Central Bank.[200] Sparkassen engage in retail and institutional banking, meeting mandates to keep profit-making secondary to the common good.[201] For example, while private banks supply products to small businesses on purely economic bases, Sparkassen must employ a more holistic approach.[202] Revenues sponsor a number of public interest initiatives, from the sciences to the arts.[203]

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191. *Id.* Notably, Banco Ciudad has opened many branches in local shantytowns where no other financial services exist, highlighting the importance of the public "gap-filling" discussed above. *Id.*

192. *Id.*

193. *Id.*

194. *Id.*

195. CYRUS A. VANCE CTR. FOR INT'L JUST., *supra* note 183.

196. *Id.* at 11.

197. *Id.* at 14.

198. *Id.* at 14.

199. *Id.*

200. *See* Nicolas Véron, *Banking Regulation in the Euro Area: Germany is Different*, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS (May 11, 2020, 5:45 AM), https://www.piie.com/blogs/realtime-economic-issues-watch/banking-regulation-euro-area-germany-different [https://perma.cc/KQ6Z-A4G7].

201. *Id.*

202. *Id.*

203. *Id.* at 15.

Public banks, no matter their stripes, are fairly scrutinized for falling prey to political influence.[204] One survey of Spanish public savings banks found a positive relationship between regional political influence and ex-ante risk taking, as well as ex-post loan defaults.[205] A study of Italian public banks showed that these banks charged lower interest rates to firms politically connected to the bank.[206] And one global survey suggests that greater government ownership of banks is associated with slower financial system development,[207] favoring the position that government involvement can lead to a political allocation of resources.[208] These conclusions may seem grim, but they are no worse than what is true of general corruptive influence in private banks. For instance, researchers have found state-level public corruption in the United States that influences local private bank lending activity.[209] In general, private banks can and do already engage in a unique, subtle form of political corruption—regulatory capture vis-à-vis lobbying or high-level bribery—that enables them to mold political and legal institutions for their benefit.[210] Public and private banks alike face pressures. The difference is merely in how obvious these pressures are.[211]

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204. In this context, "political influence" does not refer to the political determination of bank resources to particular lending initiatives, which is an integral element of public banks. Rather, it refers to undue political gamesmanship; for example, lending more during election years to further entrench the power of political incumbents.

205. Manuel Illueca et al., *Liberalization and Risk-Taking: Evidence from Government-Controlled Banks*, 18 R. FIN. 1217, 1217 (2014).

206. Paola Sapienza, *The Effects of Government Ownership on Bank Lending*, 72 J. FIN. ECON. 357, 357 (2004).

207. Financial system development occurs when "financial instruments, markets, and intermediaries ease the effects of information, enforcement, and transaction costs, and therefore do a correspondingly better job at providing the key functions of the financial sector in the economy." *Background of the Global Financial Development Report*, THE WORLD BANK, https://www.worldbank.org/en/publication/gfdr/gfdr-2016/background/financial-development [https://perma.cc/2FJ4-G8YQ].

208. *See, e.g.*, Rafael La Porta et al., *Government Ownership of Banks*, 57 J. FIN. 265, 266–68 (2002).

209. *See* Theodora Bermpei et al., *Local Public Corruption and Bank Lending Activity in the United States*, 171 J. BUS. ETHICS 73, 95–96 (2021).

210. *See* Daniel Kaufmann, *Corruption and the Global Financial Crisis*, BROOKINGS (2009), https://www.brookings.edu/opinions/corruption-and-the-global-financial-crisis [https://perma.cc/7Z7C-H8JL] (explaining the private corruption within American institutions that contributed to the Financial Crisis); Annalise Riles, *Managing Regulatory Arbitrage: A Conflict of Laws Approach*, 47 CORNELL INT'L L. J. 63 (2014) at 65–66 (lamenting private banks' persistent regulatory arbitrage).

211. *See supra* notes 204–208.

Some public banks have successfully guarded against improper political influence,[212] suggesting that certain system controls can, in fact, be built into a public bank model and that external institutions may also prevent political influence.[213] A hypercompetitive economy, for instance, may constrain politicians from pursuing their political agendas by way of a public bank.[214] This has been observed in East Asia, where government-owned banks performed poorly relative to the private sector from 1997–2000, but then started performing on par with private banks from 2001–2004 once regional financial services became more globalized.[215] A highly-developed financial services market may also play a role in mitigating the principal-agent problem by allowing public managers to mimic private counterparts, and by offering high standards for employees, supervision, regulation, and operation.[216] Indeed, empirical review of government-owned banks shows that the negative impact of government ownership depends largely on the degree of the nation's financial development, such that in highly-developed systems, there is little negative impact.[217] Finally, robust political institutions may help create public banks that are, at a minimum, generally transparent and institutionalized in the sociopolitical fabric.[218] Importantly, the United States has all of these characteristics—a hypercompetitive economy, highly-developed financial services market, and robust, well-developed political institutions—making it less likely domestic public banks will succumb to undue political influence. By the same token, it is also possible, and even likely, that domestic public banks can perform on par with comparable private financial institutions.

As evidenced by the discussion in this section, there is no "one size fits all" model for the regulation or operation of public banks. One could ostensibly cherry pick from existing models,

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212. *See, e.g.*, discussion on the Bank of North Dakota and the Territorial Bank of American Samoa, *infra* Part III.C.

213. *See, e.g.*, discussion on the Territorial Bank of American Samoa, *infra* Part III.C.

214. Yueh-Ping Yang, *Government Ownership of Banks: A Curse or a Blessing for the United States?*, 10 WM. & MARY BUS. L. REV. 667, 667 (2019).

215. Marcia Million Cornett et al., *The Impact of State Ownership on Performance Differences in Privately-Owned versus State-Owned Banks: An International Comparison*, 19 J. OF FIN. INTERMEDIATION 74, 79 (2010).

216. Yang, *supra* note 214, at 705.

217. Tobias Körner & Isabel Schnabel, *Public Ownership of Banks and Economic Growth: The Impact of Country Heterogeneity*, 19 ECON. TRANSITION 407, 434–35 (2011).

218. Yang, *supra* note 214, at 676.

conservatively or liberally, to create an entirely new model catering to regional needs. This Note argues for a model in which the public bank acts as a depository for government tax money, enabling governments to finance their projects at a significantly cheaper rate.[219] It does not argue, however, for a model accepting retail deposits from individuals, which would put a public bank in direct competition with private banks. Instead, this Note supports a model that only accepts deposits from city or state governments and works with private-sector partners to deliver additional services to communities at the city and state levels. Though this author believes that legislators should aspire to a fully public option for retail banking (due to the potential competitive benefits), taking into account the contemporary political ecosystem, this Note ultimately posits that private-sector support is invaluable for the promulgation of public banks and their many resulting benefits.[220] Moreover, private partnership in this non-retail public banking model would likely have the unique benefit of improving profit margins for private community banks, better enabling them to compete with multinational financial institutions.

C. PUBLIC BANKS IN THE UNITED STATES

This Note supports a public bank model drawing from the Bank of North Dakota (BND). While the BND is undoubtedly the paramount example of a U.S. public bank, it is far from the country's first. The Colonial Era saw the popularity of "land-banks," public lending institutions operated by colonial governments.[221] When money was scarce, the banks would inject liquidity into the system through cash loans to farmers in the hopes of promoting commerce.[222] The system performed poorly in New England, but was quite successful in the Middle Colonies—so successful, in fact, that it earned the staunch support of Benjamin

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219. *See, e.g.*, Michael Brennan & Macabe Keliher, *Public Banks*, DEMOCRACY POL'Y NETWORK, https://democracypolicy.network/agenda/open-country/open-economy/public-banks [https://perma.cc/P9XS-5M8Z] (noting that, by acting as public depositories and public lenders for the government, public banks obviate the need for the private market's financing at potentially higher rates).

220. *See infra* Part III.F.

221. Theodore Thayer, *The Land-Bank System in the American Colonies*, 13 J. ECON. HIST. 145, 145 (1953).

222. *Id.*

Franklin, Adam Smith, and the sizable number of English merchants who interacted with it.[223]

Public banks operated for some time even after American Independence. Each state had some financial institution that was wholly or partially public, integral to the state's early economic success, and at least somewhat regulated by the state's legislature.[224] Massachusetts, for example, invested significant capital into the Union and Boston Banks.[225] The banks' early successes allowed the state to drop its traditional poll and property taxes for a time.[226] New York used its state bank to underwrite local private bank operations and increase these banks' bottom lines.[227] Delaware became a large shareholder of the Bank of Pennsylvania and the Bank of Delaware, which enabled bank revenues to constitute seventy percent of the state's income by the 1840s.[228] And Virginia's state bank stocks paid for the state's schools and assorted public works projects, like canals.[229]

At the federal level, a national bank—the First Bank of the United States—was chartered in 1791.[230] Jointly funded by the U.S. government and wealthy, private stockholders, the bank operated as a regular commercial bank and competed with state and private banks.[231] Though the bank eventually lost its charter in 1811, the War of 1812 prompted the creation of a similar bank,

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223. *Id.* at 147–48.

224. Richard Sylla et al., *Banks and State Public Finance in the New Republic: The United States, 1790–1860*, 47 J. ECON. HIST. 391, 392–93 (1987) ("We here review how and to what extent each of the thirteen original states and also Maine and Vermont turned state-chartered banks into integral components of their public finances between 1790 and 1860. . . . Early American states turned the banks they chartered into instruments of state finance in two broad ways—by investing in banks and by chartering them. . . . State investment in banks could take the standard form of purchasing shares. . . . A few banks were wholly owned and operated by some states. Others chartered banks with the stipulation that shares be reserved for state purchase at later dates. . . .").

225. *Id.* at 393.

226. The bank taxes provided at least half of all state revenue from 1820 to 1860, enabling the state to drop its traditional property and poll taxes from 1826–1830, 1832–1834, and 1846–1853. *Id.* at 394.

227. *Id.* at 396.

228. *Id.* at 396–97.

229. *Id.* at 398.

230. James Wettereau, *New Light on the First Bank of the United States*, 61 PENN. MAG. HIST. AND BIOGRAPHY 263, 263 (1937).

231. *Id.* at 269–71. *See also The First Bank of the United States*, FED. RSRV. (Dec. 4, 2015), https://www.federalreservehistory.org/essays/first-bank-of-the-us [https://perma.cc/9YK3-KKVE].

the Second Bank of the United States.[232] This bank, in addition to competing with other banks in commercial activity, also acted as a depository for the U.S. government's dollars, making it the frequent subject of political attacks.[233] When the bank's charter did not renew in 1836, federal dollars were deposited into state-chartered banks.[234]

Later deregulation and the expansion of private finance eventually led many states to liquidate their states' bank shares in spite of their initial successes.[235] At the turn of the twentieth century, however, increasing industrialization, monopolization of grain elevators, and anti-bank sentiment led U.S. farmers to revisit public finance as a tool for conducting business.[236] BND was founded in 1919 with the mission of "promot[ing] agriculture, commerce, and industry" in North Dakota.[237] Its operations from its inception through today provide a fascinating case study in the impact and potential benefits a public bank can have in a given region.[238] Although data is scarce, research shows that BND has turned a profit every year since 1971.[239] In addition, these studies show that BND's lending and investments[240] have been more

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232. *The Second Bank of the United States*, FED. RSRV. (Dec. 5, 2015), https://www.federalreservehistory.org/essays/second-bank-of-the-us [https://perma.cc/33XQ-93V6].

233. Opponents claimed, for example, that the bank impeded on states' rights, put too much power in the hands of a few private citizens, and was far too removed from the oversight of the president, Congress, and voters. *Id.*

234. *Id.*

235. Harry Scheiber, *The Pet Banks in Jacksonian Politics and Finance*, *1833–1841*, 23 J. ECON. HIST. 197, 210–14 (1963).

236. Alvin Tostlebe, The Bank of North Dakota: An Experiment in Agrarian Banking 21, 32–35, 37–39 (1924) (Ph.D. dissertation, Columbia University) (on file with author); Elizabeth Laughlin, *The Rise of American Industrial and Financial Corporations*, 6 GETTYSBURG ECON. REV. 42, 49 (2012) ("It is clear to see the influence that the railroads had. . . . Investment quickly became the driving force of economic expansion."); KODRZYCKI & ELMATAD, *supra* note 173, at 5.

237. Tostlebe, *supra* note 236, at 7; *Mission, Vision, Core Values*, BANK OF N.D. (2021), https://bnd.nd.gov/mission/ [https://perma.cc/G5BQ-ZGZB].

238. *See generally* KODRZYCKI & ELMATAD, *supra* note 173 (drawing from Bank of North Dakota case studies to consider potential benefits and disadvantages of a public bank in Massachusetts).

239. *Id.* at 8.

240. Many public banking advocates push for public banks that will not invest in fossil fuels, or that will otherwise be limited to particular ESG investments. They nevertheless champion BND, which has long invested in oil and gas, as a model of what public banking may look like in the United States. These potentially contradictory views may be reconciled as follows: (1) As the oldest existing public bank in the United States, BND is the best case study for public banking's *other* prosocial benefits beyond environmental good (*see* discussion in Part IV.B), (2) BND simultaneously engages in sustainable ventures, and (3) community-driven operation is a core element of public banking. A public bank's

successful than those of similarly sized private banks.[241] Through a large average transfer of profits to the state government, BND has helped North Dakota balance its state budget during times of economic downturn.[242] For instance, during the Financial Crisis, BND increased its loans and letters of credit to the state's banks that needed to develop liquidity plans.[243] In addition, "[s]ince the initial investment of $2 million . . . BND has returned more than $1 billion to the state through the general fund, infrastructure, disaster relief, and other special programs."[244] BND is also responsible for administering a number of state programs, including the Guaranteed Student Loan Program (administering the state's low-interest student loans), the Community Water Facility Loan Fund (financing projects that conserve, control, treat, and distribute water, especially in rural areas), and the Beginning Farmer Loan Program (extending loans to farmers or ranchers for purchase of farmland).[245]

Five years prior to BND's founding, the U.S. Navy established the public Bank of American Samoa (BAS) to overcome the obstacles relating to the territory's scarce banking services.[246] BAS was the territory's sole bank for decades, and operated as a public bank[247] until it was purchased by the private Bank of Hawaii in

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investment criteria should be determined in part by local residents if they are part owners of the bank. One may accordingly view BND's investments as an exercise of North Dakotans' choice. But BND's history of fossil fuel investment does not in any way preclude other public banks from foregoing such investment in favor of ESG investments. KODRZYCKI & ELMATAD, *supra* note 173, at 3–4; Emily Erickson, Investing in Our Future: A Comparison of Strategies 24–25 (June 2019) (B.A. thesis, University of Oregon, Clark Honors College), https://scholarsbank.uoregon.edu/xmlui/bitstream/handle/1794/25016/Final_Thesis-Erickson.pdf?sequence=1&isAllowed=y [https://perma.cc/HMJ6-BC2T]; Emily Windjue, *Project Tundra Receives $100 Million Loan From State of North Dakota*, MINNKOTA CURRENT (May 24, 2022), https://news.minnkota.com/post/project-tundra-receives-100-million-loan-state-of-north-dakota [https://perma.cc/ZYK5-KDZ5] (announcing BND's $100 million loan to Project Tundra, an initiative to build the world's largest carbon capture facility).

241. KODRZYCKI & ELMATAD, *supra* note 173, at 8.

242. *Id.* at 4.

243. *Id.*

244. Felix Lessambo, *Public Bank—Bank of North Dakota*, *in* THE U.S. BANKING SYSTEM 139 (2019).

245. *Id.* at 140.

246. Julie Andersen Hill, *Opening a Federal Reserve Account*, 40 YALE J. ON REGUL. (forthcoming) (manuscript at 133), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4048081 [https://perma.cc/9YVB-JAJE] (noting that the Bank of American Samoa opened in 1914).

247. BAS was regulated only by the government of American Samoa, and these government officials also effectively ran the bank. *Id.* at 133.

1969.[248] By 2000, an additional private depository institution, ANZ Amerika Samoa Bank, had entered the market. ANZ was plagued with administrative inefficiencies—a check deposited in American Samoa could take up to three weeks to withdraw in the mainland United States—thus making the Bank of Hawaii the territory's primary financial institution in practice.[249] One can imagine American Samoa's devastation, then, when the Bank of Hawaii announced it would exit the market in 2012.[250] Following the announcement, a delegation implored other Hawaiian banks to open branches in the territory, to no avail.[251] The territorial government of American Samoa was forced to temporarily move its accounts to a private Utah bank that had no intention of starting a branch in the territory.[252] Finally, with no other options and a desperate need to connect to U.S. payment systems, American Samoa turned to public banking. In 2015, the Territorial Bank of American Samoa (TBAS) was chartered.[253]

The American Samoa story is a notable example of the private sector's total failure to provide essential financial services in a region. It is doubly significant as a real-time case study in the challenges and successes of forming a public bank within the U.S. financial system today. In 2016, for example, TBAS opened with a "packed" ceremony.[254] But it had failed to first obtain either a routing number or a Federal Reserve ("Fed") account, preventing it from connecting to the broader U.S. payments system.[255] In turn, TBAS was unable to offer customers checking services.[256] It courted the Federal Reserve as deposits rose.[257] In so doing, it was required to address several questions from the Fed's General Counsel, including whether TBAS was eligible for a Fed account and why, how it would protect itself from government pressures, and how the Office of Financial Services could supervise the

248. *Id.*
249. *Id.*
250. *Id.*
251. *Id.*
252. Hill, *supra* note 246, at 133.
253. *Id.* at 134.
254. Rob Blackwell, *How Far Does American Samoa Have to Go to Get a Bank?*, Am. Banker Mag. (July 31, 2017), https://www.americanbanker.com/news/how-far-does-american-samoa-have-to-go-to-get-a-bank [https://perma.cc/62YM-R643].
255. Hill, *supra* note 246, at 134–35.
256. *Id.* at 135.
257. *Id.* at 135.

bank.[258] Organizers emphasized TBAS' prosocial benefits and the Community Reinvestment Act's requirement that the Fed consider local credit needs.[259] In 2018 the Fed granted TBAS an account, a decision the former TBAS CEO attributes to the Fed's appreciation for the bank's community benefits rather than its risk profile.[260]

TBAS and BND remain the only two public banks in the United States as of 2023.[261] The current limited number of U.S. public banks can likely be explained by a few factors. First, the unique complexity of the U.S. financial system renders it opaque to most people. Many people (including lay citizens, financiers, policymakers, etc.) are unfamiliar with the country's history of public finance,[262] and with so many systemic actors, rules, and regulations to account for, it can be difficult to conceptualize new financial entities like public banks. Likewise, lawmakers and their staff are rarely experts in finance,[263] making it particularly challenging for these elected representatives to address the necessary structural and operational questions for public banking through legislation. Second, the U.S. political tradition invites exaggerated skepticism of public interventions.[264] Concerns that

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258. *Id.* at 135.
259. *Id.* at 135.
260. *Id.* at 136.
261. Nevertheless, the United States has had several quasi-public financial institutions for some time. For example, in the 1980s, a government bailout for the Continental Illinois Corporation, then the nation's seventh largest bank, gave the FDIC majority ownership of the bank. *See* Yang, *supra* note 214, at 683–85. Government ownership of financial institutions famously came to a head during the Financial Crisis, when a federal bailout for troubled firms came vis-à-vis $205 billion in equity purchases by the Treasury. *Id.* at 685. Additionally, several states have state infrastructure banks to capitalize infrastructure projects, or green banks to fund clean energy. *State Infrastructure Banks*, U.S. DEP'T OF TRANSP., https://www.transportation.gov/buildamerica/sibs [https://perma.cc/DJ3N-KF4C]; Ella Nilson, *The Smartest Way to Finance Clean Energy That You've Never Heard Of*, VOX (June 1, 2021 10:00 AM), https://www.vox.com/2021/6/1/22454779/green-banks-biden-american-jobs-plan [https://perma.cc/DX93-Q3U3].
262. This is extrapolation based on the fact that most Americans do not know basic U.S. history. *See, e.g.*, Saba Naseem, *How Much U.S. History Do Americans Actually Know? Less Than You Think*, SMITHSONIAN MAG. (May 28, 2015), https://www.smithsonianmag.com/history/how-much-us-history-do-americans-actually-know-less-you-think-180955431/ [https://perma.cc/CRC2-4TTP].
263. Lee Drutman & Steven M. Teles, *Why Congress Relies on Lobbyists Instead of Thinking for Itself*, ATLANTIC (Mar. 10, 2015), https://www.theatlantic.com/politics/archive/2015/03/when-congress-cant-think-for-itself-it-turns-to-lobbyists/387295/ [https://perma.cc/44R2-SX6Z] (noting that lawmakers face increasing difficulty understanding complex policy issues, often relying on staffers who in turn are often generalists as opposed to specialists).
264. Jedediah Britton-Purdy et al., *Building a Law-and-Political-Economy Framework: Beyond the Twentieth-Century Synthesis*, 129 YALE L.J. 1784, 1795–96 (2020) (noting contemporary law and economics represents the ideal of "autonomy of the economy"—an

undue political influence may impact public bank operations, or that public management will lead to insufficient performance, tend to dominate the nation's public banking discourse,[265] whether fairly or not. Third, and perhaps most importantly, the country's private banking lobby exerts considerable influence on the general public and in Congress.[266] Private banks, understandably, feel threatened by public banks, seeing their proliferation as adverse to their bottom lines by increasing competition for the retail deposits and loans that make them money.[267] Consequently, they frequently and loudly oppose any efforts to create these institutions.[268]

Despite these obstacles, however, grassroots movements around the country are gathering support for public banks and bringing discussions about government-owned banking models to

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idea building off traditional laissez-faire, which posits that markets should be free of state coercion, to conclude the political must necessarily be subordinate to the economic).

265. *See, e.g.*, Rob Nichols, Opinion, *A Public Bank is Risky Business*, HILL (Oct. 19, 2018 4:00 PM), https://thehill.com/opinion/finance/412278-a-public-bank-is-risky-business/ [https://perma.cc/B47U-7G5A] (discussing concerns about political influence and inefficiency); George Joseph, *'Public Bank' Bill Blocked From State Senate Vote After Industry Pushback*, CITY (May 18, 2022), https://www.thecity.nyc/2022/5/18/23125953/public-bank-bill-blocked-new-york-senate [https://perma.cc/DT99-GTZC] (discussing a memo from the Independent Bankers Association to the New York State Legislature in opposition to public banking legislation, which argued public banks would burden taxpayers due to excessive risk and the likelihood of poor performance).

266. *See, e.g.*, Deniz Igan & Thomas Lambert, *Bank Lobbying: Regulatory Capture and Beyond* 5–17 (IMF Working Paper 19/171, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3772463 [https://perma.cc/94ZQ-SVLW] ("Regulatory capture arises when banks exert excessive influence on the regulators such that regulators act primarily in the interests of the industry they regulate rather than in the public interest. . . . [Findings from various scholarship on the American ecosystem] seems consistent with the theory of regulatory capture."). *See also* Jeff Stein, *As Bank Profits Soar, Wall Street's Political Spending Hits New High*, WASH. POST (Apr. 30, 2019 8:00 AM), https://www.washingtonpost.com/business/2019/04/30/bank-profits-soar-wall-streets-political-spending-hits-new-high/ [https://perma.cc/8TJK-VS36].

267. *See, e.g.*, *Our Position: State-Owned Public Banks*, INDEP. CMTY. BANKERS OF AM., https://www.icba.org/our-positions-a-z/state-owned-public-banks [https://perma.cc/Q6UW-29Y3] (statement opposing public banks partially on the grounds that they would directly or indirectly compete with private community banks).

268. *See, e.g.*, Aaron Stetter, *The Problem with Public Banking*, INDEP. CMTY. BANKERS OF AM., https://www.icba.org/newsroom/blogs/main-street-matters/2021/05/13/the-problem-with-public-banking [https://perma.cc/EA6G-GDXJ] ("While community banks have again proven their importance to local communities . . . public banking proponents in some states and municipalities threaten to undermine this system and its benefits to consumers."); *see also* Joseph, *supra* note 265 (in addition to the opposition memo from the Independent Bankers Association, the article also notes major banks like JP Morgan and Capital One have hired lobbying firms to do direct lobbying on bills, including public banking measures); discussion *infra* Part III.F.

the mainstream.[269] In 2020, U.S. Representatives Rashida Tlaib and Alexandria Ocasio-Cortez introduced the Public Banking Act to create a Public Bank Grant program administered by the Federal Reserve and U.S. Treasury.[270] If enacted,[271] the Act would also enable the Federal Reserve to charter and grant program membership to public banks, allow the FDIC to insure public bank deposits, and direct other financial regulators like the Securities and Exchange Commission to create additional regulatory frameworks covering public banks.[272] In 2021, Los Angeles and San Francisco took concrete steps to create their own municipal banks, voting to study the viability of a local public bank and creating a municipal bank business plan, respectively.[273] Activists in several other cities and states are educating the public about financing possibilities and lobbying legislators for new banks.[274]

269. *See, e.g.*, Steve Dubb, *Public Bank Movement Gains Ground in Cities and States Across the US*, NONPROFIT Q. (Jan. 2, 2018), https://nonprofitquarterly.org/public-bank-movement-gains-ground-cities-states-across-us/ [https://perma.cc/9BXY-Y6Y6] (noting how several cities around the country have campaigns to launch local public banks); Syris Valentine, *How Activists Are Trying to Change the Way Banking Gets Done*, YES! MAG. (Nov. 9, 2022), https://www.yesmagazine.org/economy/2022/11/09/public-community-banking-land [https://perma.cc/HCD6-WA9N] (highlighting how New York community organizations have built a coalition for public banking and are pushing for pertinent legislation at various levels of government).

270. H.R. 8721, 116th Cong. (2020).

271. While many local, state, and federal public banking legislation is either waiting to be passed or is otherwise very incremental in its approach, one paper finds that this phased approach to public banking legislation gives lawmakers more time to run educational campaigns and conduct research, and thus increases the likelihood that a public bank will be created. SEBASTIAN LEDER MACEK, NORTHEAST-MIDWEST INST., WHITE PAPER: PUBLIC BANKING IN THE NORTHEAST AND MIDWESTERN STATES 41–42 (2019), https://www.nemw.org/wp-content/uploads/2019/09/Public-Banking-White-Paper.pdf [https://perma.cc/MSK7-8PVY].

272. *See* Stewart, *supra* note 12.

273. *See* Julia Wick, *LA Takes a Step Toward Launching a City-Owned Bank*, L.A. TIMES (Oct. 5, 2021 6:10 PM), https://www.latimes.com/california/story/2021-10-05/la-takes-step-toward-launching-city-owned-bank [https://perma.cc/QJ82-XUB5]; *SF Supes Approve Plan to Create First Public Bank In U.S.*, CBS BAY AREA (June 15, 2021 5:41 PM), https://www.cbsnews.com/sanfrancisco/news/sf-supes-approve-plan-to-create-first-public-bank-in-u-s/ [https://perma.cc/EX7A-ABST]; Christin Evans, *Working Group Write Business Plan for San Francisco Public Bank*, HAIGHT ASHBURY NEIGHBORHOOD COUNCIL (Dec. 4, 2022), https://www.hanc-sf.org/24-home/739-working-group-writes-business-plan-for-san-francisco-public-bank [https://perma.cc/43W2-YFGD].

274. *See, e.g.*, the Ohio Public Banking Coalition, a 501(c)(4) organization advocating for public banks to "[increase] equity in the financial system by ensuring all individuals are given the financial tools they need to succeed." OHIO PUB. BANKING COAL., https://www.ohiopublicbanking.org/ [https://perma.cc/2Q9F-76PF]. *See also* the Philadelphia Public Banking Coalition, a campaign of "nonpartisan volunteer citizens . . . to achieve the creation of a public bank in Philadelphia." *About*, PHILA. PUB. BANKING COAL., https://philapublicbanking.org/?page_id=14 [https://perma.cc/FGL9-RKCY]. *See also* Jeremy Nobile, *Could the Public Banking Movement Take Root in Cleveland?*, CRAINS

The time is ripe for considering new ways to leverage public banks to fight systemic problems.[275]

D. A LONG-TERM INVESTMENT

Public banks can be sound, long-term investments for pensions. Internationally, they tend to be less efficient than their private counterparts[276] but are nevertheless capable of generating positive financial returns to benefit pensioners.[277] For instance, state-owned banks charge lower interest rates than privately-owned banks.[278] The competitive interest rates in turn mean more

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CLEVELAND (Oct. 31, 2021), https://www.crainscleveland.com/finance/could-public-banking-movement-take-root-cleveland [https://perma.cc/Z4US-Z4FH] and Geeta Minocha and Ricardo Williams, Guest Commentary, *It's Expensive to be Poor. Publicly Owned Banks May Help*, ORLANDO SENTINEL (Mar. 21, 2021), https://www.orlandosentinel.com/opinion/guest-commentary/os-op-public-banks-20210312-qj6akuf4ezboppeal3rtbnstq4-story.html [https://perma.cc/6KCU-9DK8] for local commentaries on public banking efforts.

275. Indeed, one author posits that public banks will have "a materially significant place in the future of global finance for sustainable development." THOMAS MAROIS, PUBLIC BANKS: DECARBONISATION, DEFINANCIALISATION AND DEMOCRATISATION 5 (2021).

276. One influential study finds that prior to a crisis, there is no material difference in nonperforming loans between private banks and state-owned banks in countries with significant government involvement in the financial sector; however, during a crisis, nonperforming loans from state-owned banks increase rapidly. Cornett et al., *supra* note 215, at 87–88. A possible explanation is that state-owned banks always have more unbooked nonperforming loans, but that these loans can no longer be covered up during a crisis. Post-crisis, however, state-owned banks are able to strongly overcome this gap in nonperforming loans. This same paper finds that, from 1993–2004, state-owned banks enjoyed less operational efficiency compared to private banks, calculated using a ratio of personnel expenses to total loans. *Id.* at 77, 88. Moreover, during this period, state-owned banks had greater allowance for loan losses. *Id.* at 87. Finally, in general, state-owned banks appear to provide more financing to the government than private banks. *Id.* at 77. Another review comparing foreign-owned, state-owned, and private banks in Pakistan shows that Pakistani public banks were overall less efficient than both foreign-owned and private banks across various metrics. Abid Burki & G.S.K. Niazi, *Impact of Financial Reforms on Efficiency of State-Owned, Private, and Foreign Banks in Pakistan*, 42 APPLIED ECON. 3147 (2010). The authors attribute the differences in part to flexible, market-oriented policies, young, energetic managers, political independence, urban networks, and fewer administrative expenses on the private side. *Id.* at 3156. Public banks are the least technically efficient banks in the Turkish market. Elmira Partovi & Roman Matousek, *Bank Efficiency and Non-Performing Loans: Evidence from Turkey*, 48 RSCH. INT. BUS. & FIN. 287, 295 (2019). Similarly, public banks are the least technically efficient banks in the Chinese market. Tai Hsin-Huang et al., *Evaluating Efficiencies of Chinese Commercial Banks in the Context of Stochastic Multistage Technologies*, 41 PACIFIC-BASIN FIN. 93, 95 (2017). It is possible, however, that a public bank may guard against these inefficiencies using specific structural methods that would promote energetic management, political independence, performance transparency, rapid technological adoption, and more. *See also* discussion *supra* Part III.B.

277. *See infra* Part III.E for additional discussion about the possible financial upside to be reaped from public banks.

278. Sapienza, *supra* note 206, at 2.

businesses will flock to take out loans.[279] Abroad, a few public banks have done quite well for investors.[280] Collectively, however, it may be true that public banks will offer less robust direct returns than private banks. But, for the reasons stated below, it is worthwhile for pensions to forego short-term financial gains in exchange for the valuable economic and prosocial gains that public banks may catalyze in the long-term.

Public banks can generate positive externalities which may improve society at large and offer beneficiaries both financial and nonfinancial value. The relationship between public ownership of banks and GDP depends on a country's conditions at the time state ownership is assumed.[281] Thus, for nations with high financial development and institutional quality, like the United States, the impacts of public ownership are neutral to positive.[282] And cross-country evidence from 1995 to 2007 shows that government ownership of banks has been "robustly" associated with higher long-run economic growth.[283]

To understand why government ownership of banks may positively impact an economy, consider Person P, an underbanked individual in City C with no access to credit besides loans from family or friends. P would like to start a business but has been deemed uncreditworthy by traditional financial institutions and cannot obtain the necessary start-up capital. Meanwhile, a local teachers' pension has purchased shares of the Public Bank of C (PBC). PBC uses some of its capital, including money from the teachers' pension, to partially fund P's loan thanks to a partnership with C's private banks, in which PBC partially funds loans for individuals the private entities deem risky. When P's

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279. RICHARD CARNELL ET AL., *Banks: Fundamental Concepts*, *in* THE LAW OF FINANCIAL INSTITUTIONS (7th ed. 2021).

280. *See, e.g.*, Wesen Legessa Tekatel & Beyene Yosef Nurebo, *Comparing Financial Performance of State Owned Commercial Bank with Privately Owned Commercial Banks in Ethiopia*, 5 EUR. J. BUS. SCI. & TECH. 200 (2019). This recent study of Ethiopian public banks showed that they offer a greater return on equity compared to the nation's private banks, implying that public bank shareholders earn more per dollar of equity they own. *Id.* at 209. *See also* Tobias Körner & Isabel Schnabel, *supra* note 217.

281. Körner & Schnabel, *supra* note 217. *But see* Rafael La Porta et al., *Government Ownership of Banks*, 57 J. FIN. 265 (2002) for an influential paper arguing that public ownership of banks is associated with lower GDP. Körner and Schnabel effectively debunk this.

282. *See* Körner & Schnabel, *supra* note 217, at 435.

283. Svetlana Andrianova et al., *Is Government Ownership of Banks Really Harmful to Growth?* 3 (DIW Berlin, Discussion Paper No. 987, 2010), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1633841, [https://perma.cc/8VJ6-BUMA].

business eventually turns a profit,[284] P decides to franchise it. It grows, and eventually becomes a healthy investment for PBC itself. Consequently, the teachers' pension has not only obtained a sound investment in PBC, but has also reaped tangible benefits from PBC's investment in Person P via higher returns. Perhaps the pension later invests in P's business too.

This scenario is, of course, an extreme example of public banking's "trickle-up" potential. More likely, the investment in Person P will yield dividends through more subtle avenues, such as increasing P's spending power. But the former result is not an impossibility, and even the latter result could generate crucial regional growth in the long-term. Remember, P's individual impact should be multiplied by the community's unbanked or underbanked population. Today, approximately twenty-five percent of Americans fall into these categories.[285]

Investment in individuals is paramount, but public banks also have a mandate to invest in broader, profitable social goals that benefit individuals through externalities.[286] Fighting climate change is an obvious example, but the possibilities are endless. A community may choose to charter a bank to account for any number of causes particularly salient to it, such as a future Bank of Cleveland investing in lead-safe infrastructure[287] or a future Bank of Florida investing in plant breeding.[288] Accomplishing

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284. Traditional banks may sometimes turn down seemingly profitable small businesses simply because a small business loan may not make financial sense for the bank; these accrue fewer profits than large business loans. *See, e.g.*, *Why Banks Don't Lend to Small Businesses*, W. PHILA. FIN. SERVS. INST. (Mar. 9, 2017), https://wpfsi.com/banks-dont-lend-small-businesses/ [https://perma.cc/9RGC-FCAH].

285. Emily Guy Birken, *The Costs of Being Unbanked or Underbanked*, FORBES (July 28, 2020), https://www.forbes.com/advisor/banking/costs-of-being-unbanked-or-underbanked/ [https://perma.cc/26A6-J8M2].

286. *See, e.g.*, Joshua Bosshardt & Eugenio Cerutti, *Why Did Public Banks Lend More During the Global Financial Crisis?* 3–4 (Int'l Monetary Fund, Working Paper No. 20, 2020), https://www.imf.org/en/Publications/WP/Issues/2020/06/05/Why-Did-Public-Banks-Lend-More-During-the-Global-Financial-Crisis-49470 [https://perma.cc/U2A7-JUJC] ("Public banks can . . . support projects with positive externalities. . . . We find evidence that public banks lent more [during the Financial Crisis] because they pursued an objective of helping to stabilize the economy. . . .").

287. Twenty-five percent of children in Cleveland, Ohio are exposed to significant amounts of lead by the time they start kindergarten. *See* Hannah Catlett, *Lead Poisoning Concerns Brought to Cleveland City Council in 1st Public Comment Session*, CLEVELAND 19 NEWS (Oct. 5, 2021), https://www.cleveland19.com/2021/10/06/lead-poisoning-concerns-brought-cleveland-city-council-1st-public-comment-session/?outputType=apps [https://perma.cc/7NPP-RY3T].

288. Climate change has been decimating Florida's agricultural sector, but plant breeding may lead to more resilient crops. *See* J. Scott Angle, Opinion, *Florida Is Finding*

these social goals creates additional "trickle-up" effects that will positively impact the finances of public banks and the pensions that invest in them.[289] It has been documented, for example, that large-scale nature restoration efforts can create as many as thirty-three jobs per $1 million invested.[290] Assuming this trend would not suffer from diminishing returns, PBC, in concert with other public banks, could help create up to 395 million jobs by 2030 by aggressively directing capital towards such efforts in a way that private banks cannot.[291] Members of the teachers' pension who value low unemployment or a "green" economy would benefit. Meanwhile, the 395 million jobs created from a "green" transition would contribute to economic growth and likely increase the pension's returns from other investments, conferring a benefit to even those pensioners who do not prioritize social causes. Thus, by addressing individual and societal needs, public banks may indirectly offer pensioners significant financial *and* nonfinancial value, making them worthy of large-scale investment from pensions.

E. OVERCOMING REGULATORY AND INSTITUTIONAL HURDLES

Once the financial and nonfinancial value of public banks is established, it becomes easier to understand how investing in them can overcome the fiduciary obstacles presented by ERISA, the

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Answers to Farmers' Challenges, TAMPA BAY TIMES (Sept. 7, 2021), https://www.tampabay.com/opinion/2021/09/07/florida-is-finding-answers-to-farmers-challenges-column/ [https://perma.cc/3RX8-9QQW].

289. *See, e.g.*, Joshua D. Margolis et al., Does It Pay to Be Good . . . and Does It Matter? A Meta-Analysis of the Relationship Between Corporate Social and Financial Performance 25–27 (Mar. 1, 2009) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1866371 [https://perma.cc/8LH3-TDQX] ("The overall effect [of companies acting in the social good] is positive. . . ."); Francesco Gangi et al., *The Impact of Corporate Social Responsibility (CSR) Knowledge on Corporate Financial Performance: Evidence from the European Banking Industry*, 23 J. KNOWLEDGE MGMT. 110, 127 (2019) ("The more a bank invests in CSR, the more it can benefit from internal and external trust relationships that may support knowledge sharing within and outside of the organization."); Silvana Secinaro et al., *Impact of Climate Change Mitigation Policies on Corporate Financial Performance: Evidence-Based On European Publicly Listed Firms*, 27 CORP. SOC. RESP. ENV'T MGMT. 2491, 2491 (2020) ("A financial statement analysis of European publicly traded firms with high environmental performance shows that they register high corporate financial performance.").

290. Todd BenDor et al., *Estimating the Size and Impact of the Ecological Restoration Economy*, PLOS ONE, June 17, 2015, at 3.

291. *See generally* WORLD ECONOMIC FORUM, THE FUTURE OF NATURE AND BUSINESS (2020), https://www3.weforum.org/docs/WEF_The_Future_Of_Nature_And_Business_2020.pdf [https://perma.cc/E7MQ-BYW9].

Freshfields report, the Department of Labor, and jurisprudence. Accordingly, ERISA's mandate of prudence is met because it is comfortably argued that a prudent investor in like circumstances would invest in public banks. Critics may note that public banks have not been "tested" enough, thus making the prudence claim a tenuous one. This proposition, however, fails on two grounds: (1) it ignores important case studies from wholly or partially public banks from around the world, and (2) it forgets the key diversification tenet of MPT.

It is true that there are only two domestic public banks,[292] which can make it hard to predict how additional U.S. public banks may function if capitalized. But existing public banks are still useful case studies—informing the charters, operations, and regulations of new public banks. Public banks in Costa Rica, Canada, and Malaysia are regularly audited and release financial statements.[293] Closer to home, the United States' own BND has enjoyed A ratings from Standard & Poor's, with the state government likewise obtaining top marks for financial transparency from the watchdog organization Truth In Accounting.[294] The totality of evidence, including the recent case study of TBAS, suggests new public banks may be regulated just like any other financial institution, which ought to quell concerns of mismanagement.

Again, it is true that in the aggregate, public banks have historically underperformed the private sector,[295] but using this point as a justification to oppose public banks in the United States ignores the research indicating that a country's development status and institutional quality can be important variables in a public bank's financial performance.[296] In Indonesia, a G20 member nation, state-owned banks were shown to have equivalent statistics to private banks for ratios of net interest margin, non-

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292. *See supra* Part III.C.

293. CYRUS A. VANCE CTR. FOR INT'L JUST., *supra* note 183.

294. *North Dakota Gets Top Marks in Financial Transparency*, BISMARCK TRIB. (Nov. 19, 2019), https://bismarcktribune.com/news/local/govt-and-politics/north-dakota-gets-top-marks-in-financial-transparency/article_26b5439b-bc28-58e4-8384-59e4e2496d18.html [https://perma.cc/4JSE-WSMH].

295. *See* MARK ADAMS ET AL., INT'L MONETARY FUND, REGULATING, SUPERVISING, AND HANDLING DISTRESS IN PUBLIC BANKS 1 (2022), https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2022/04/28/Regulating-Supervising-and-Handling-Distress-in-Public-Banks-511609 [https://perma.cc/VV8N-562F].

296. Körner & Schnabel, *supra* note 217, at 408–10.

performing loans, and operating expenses to operating income.[297] Meanwhile, public banks in Pakistan, a rapidly-growing but middle-income economy, showed greater return on assets, though private banks outperformed public banks along other metrics.[298] In the United States, the BND is the default depository for all state tax collections and fees, creating a "captive" deposit base and ensuring consistent financing for its activities.[299] But even if all public banks are less efficient, evidence indicates a public bank's stock value can remain high despite subpar performance because of public confidence in the bank[300]—a prudent financial reason for pensions to invest.

Public bank investment also aligns with MPT, which is codified in ERISA's definition of prudence in § 1104(a)(1).[301] Per the theory, an investment portfolio should be as diversified as possible, spanning a variety of businesses and industries; thus, public banks present a critical diversification opportunity. Indeed, using public banks to increase portfolio diversification would neatly match the Supreme Court's interpretation of § 1104(a)(1) in *Fifth Third* (which prioritizes prudence over other plan goals),[302] as well as the Urwin analysis that emphasizes the benefit of diversifying investments into ESG[303] and other recent interpretations which note that "the inherent long-term investment horizon and the diversified portfolio structure are two of the principal enablers of ESG in pension funds."[304]

Some academics have built on MPT by suggesting that minimizing risk is best done by diversifying in *similar*

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297. Desi Susilawati & Siwi Setya Dewi, *A Comparative Analysis of State-Owned and National Private Banks' Financial Performance*, 201 ADVANCES IN ECON., BUS., & MGMT. RSCH. 133, 136 (2021). Note that the World Bank classifies Indonesia as "one of East Asia's most vibrant democracies, emerging as a confident middle-income country." *The World Bank in Indonesia*, WORLD BANK (2022), https://www.worldbank.org/en/country/indonesia/overview#1 [https://perma.cc/M2NU-BQWP].

298. Ahmad Waleed et al., *Comparison of Private and Public Banks Performance*, 17 IOSR J. BUS. & MGMT. 32, at 37 (2015); *Data for Lower Middle Income, Pakistan*, WORLD BANK (2022), https://data.worldbank.org/?locations=XN-PK [https://perma.cc/5URH-Q8HK].

299. Josh Harkinson, *How the Nation's Only State Owned Bank Became the Envy of Wall Street*, MOTHER JONES (Mar. 27, 2009), https://www.motherjones.com/politics/2009/03/how-nations-only-state-owned-bank-became-envy-wall-street/ [https://perma.cc/24SR-6MU2].

300. Nur Eny, *Financial Performance and Share Prices of Banks of State-Owned Enterprises in Indonesia*, 9 J. ILMIAH ILMU ADMINISTRASI PUBLIK 315, 315 (2019).

301. 29 U.S.C. § 1104(a)(1).

302. Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409, 421 (2014).

303. Urwin, *supra* note 65, at 29.

304. Lachance & Stroehle, *supra* note 47, at 28.

companies.[305] Even through this narrower interpretation of MPT, a prudent pension fiduciary should be inclined to invest in public banks because pensions already invest large amounts into other financial institutions.[306] Thus, in light of the fact that public banks are meant to supplement the work of private banks,[307] it behooves investors to add these banks to their portfolios.

The ERISA duty of loyalty is just as easily met because a fiduciary would be acting in the pensioners' best interests when investing in public banks. As discussed previously, investment in public banks and subsequent benefits to pensioners may be linked.[308] While the chain of impact from public banks to pensioner benefits may seem attenuated,[309] academics have argued before that attenuated benefits like job creation for plan participants are consistent with the duty of loyalty.[310] At least two courts have arrived at the same conclusion.[311] Consequently, investing in institutions that are meant to encourage economic growth in the way that public banks do ought not to violate the duty of loyalty. At an even simpler baseline, public banks worldwide have shown enough financial wherewithal that investors are plainly acting in pensioners' economic interest by choosing to invest in them.

Particularly austere interpretations of the duty of loyalty may cause some to posit that, despite the financial pragmatism behind investing in public banks, fiduciaries who do so violate the duty because they are presumably factoring in their own ethics when

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305. Michael Lubatkin & Sayan Chatterjee, *Extending Modern Portfolio Theory into the Domain of Corporate Diversification: Does It Apply?*, 37 ACAD. MGMT. J. 109, 130 (1994).

306. *See, e.g.*, CALIF. PUB. EMPS. RET. SYS., 2019–2020 ANNUAL INVESTMENT REPORT 127, 133, 137 (2020), https://www.calpers.ca.gov/docs/forms-publications/annual-investment-report-2020.pdf [https://perma.cc/K95B-9BVN] (showing the pension holds approximately 50,000 shares of Amerant Bancorp, 150,000 in BlackRock Capital Investment, and 6000 in Century BanCorp).

307. Josh Hardmeyer, *How the Nation's Only State-Owned Bank Became the Envy of Wall Street*, MOTHER JONES (Mar. 28, 2009), https://www.motherjones.com/politics/2009/03/how-nations-only-state-owned-bank-became-envy-wall-street/ [https://perma.cc/R5Y3-9X6H] ("[The BND] was designed to partner with [private banks] and not compete with them. So most of the lending we do is participatory in nature.").

308. *See* discussion *supra* Part III.D.

309. *Id.*

310. Letter from David Webber, Professor of Law, B.U. Sch. of L., to Dep't of Labor (Dec. 13, 2021) (on file with author).

311. Brock v. Walton, 794 F.2d 586, 587 (11th Cir. 1986) (ruling that trustees did not violate the duty of loyalty by establishing a discount mortgage loan to provide nonretirement benefits in the form of subsidized housing); Bandt v. Bd. of Ret., San Diego Cnty. Emps. Ret. Sys. Ass'n, 38 Cal. Rptr. 3d 544 (Cal. Ct. App. 2006) (ruling that reducing employer contribution on the basis of preserving 1500 jobs did not breach the duty of loyalty).

making the investment.[312] But this interpretation of the duty is too narrow to hold: it is not true that an investment can only provide *either* positive returns for beneficiaries *or* social benefit. A Maryland court has emphasized this point, for instance, noting that a duty of loyalty[313] has been met so long as consideration of an investment's social consequences is "*de minimis*."[314] This ruling was included in the Freshfields report as "the closest authority on point" for the notion that positive financial returns and ESG investing need not be mutually exclusive.[315] The prudent elements of an investment in public banks—their possible financial returns and utility as a tool for added portfolio diversification—indeed makes their likely prosocial benefits *de minimis* by comparison.

Because investing in public banks meets the ERISA duties of prudence and loyalty, most of the other obstacles discussed in Part II *supra* become largely irrelevant. After all, the Freshfields report and the DOL only offer additional guidance for applying the fiduciary duties—they are meant to *follow* an ERISA analysis if necessary, but not supplant it.[316] The Freshfields stipulations[317] are nonetheless achieved with public banks, as their likelihood of financial benefit enables pension managers to keep beneficiary upside the top priority in the investment process. Because of this upside, an investor faced with a choice between public banks and an equivalent financial investment with lesser social impact is able to pick the former.[318] But the recent rule proposed by President Biden's DOL[319] would seem to offer American investors even more flexibility, such that an investor faced with a choice between public banks and a slightly better financial investment with lesser social impact is probably still able to pick the former. Managers could defend this investment on the grounds that they were accounting for the banks' prosocial impacts *in addition* to their returns, in accordance with DOL guidelines.

Public bank investment similarly comports with *Fifth Third*, *Jander*, and *Thole*, as these decisions have together safeguarded

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312. Schanzenbach & Sitkoff, *supra* note 125, at 388.

313. The court did not consider ERISA directly, but rather assessed a substantially similar Baltimore code. *See* Bd. of Trustees v. Mayor of Baltimore City, 562 A.2d 720, 735 (Md. 1989).

314. *Id.* at 108.

315. FRESHFIELDS, *supra* note 69, at 111.

316. *See supra* Part II.A pp. 22–24; *supra* notes 131–46 and accompanying text.

317. *See supra* Part II.A pp. 22–23; *supra* notes 132–42 and accompanying text.

318. *See supra* Part II.A p. 23; *supra* notes 136–37 and accompanying text.

319. *See supra* Part II.A p. 24; *supra* note 146 and accompanying text.

pension trustees so extensively that they could easily invest in public banks without concern for legal pushback from beneficiaries.[320] In their discussion of how to best utilize pension capital for ESG, pensioners' reduced capacity to hold fiduciaries accountable and give the current fiduciary standards a public forum for debate becomes inconsequential.[321] On this issue, public banks shift significant burdens from pensions and their beneficiaries. Pensions may maintain their status quo, including their regulations, institutional inertia, and varied ESG understanding.[322] Likewise, beneficiaries may not need to scrutinize their pensions' ESG processes, so their reduced information rights from *Thole* become less important.[323] By investing in public banks, pensions effectively outsource ESG considerations.

To understand how this outsourcing may work, consider once more City C and its teachers' pension. C offers three investment opportunities for the pension: the Public Bank of C (PBC), a coal company, and a fashion company. Because of their fiduciary duties, the pension managers are unable to justify screening for ESG as part of their investing process. In fact, MPT dictates the managers should invest in all three opportunities, and they do so. PBC, upon receiving a fresh injection of capital from the pension, begins lending it out to local entrepreneurs. As part of its chartered mandate, PBC prioritizes loans for renewable energy entrepreneurs who can transition the city to a "green" economy. Thus, by directing one-third of its investment capital to the PBC, the pension successfully allowed that capital to be used in support of ESG goals.

State Anti-ESG laws present surmountable hurdles in the vast majority of present cases. In states with No Social Investment laws, public pensions will likely be unable to invest in public banks or any other ESG vehicle, but as of Spring 2023, only ten states have considered or passed such laws.[324] Public banks may circumvent state Boycott Bills, the most prevalent kind of Anti-ESG Bills. For instance, a bank mirroring BND may choose to

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320. *See supra* Part I.D.
321. *See supra* Part I.D pp. 18, 20; *supra* notes 111 and 123 and accompanying text.
322. *See supra* Part I.B pp. 9–10, Part II.A p. 21, and Part II.C pp. 27–29; *supra* notes 53–59, 123–30, and 160–71 and accompanying text.
323. *See supra* Part I.D pp. 19–20; *supra* notes 117–21 and accompanying text.
324. DEBEVOISE & PLIMPTON, *supra* note 155.

invest aggressively in green energy while simultaneously investing in fossil fuels. As long as an institution does not discriminate against a protected industry, it is free to support other ESG endeavors. Accordingly, a prosocial public bank-pension relationship is still viable in much of the country despite Anti-ESG Bills.

As a practical matter, it seems unlikely that state Anti-ESG Bills will survive for long; in fact, "states that pledged to bar their retirement funds from ESG-focused investment firms have thus far not put that policy into practice."[325] Globally, the private market seems to be moving towards ESG practices,[326] making it improbable that many states can afford to completely divest from entities implicated in the bills.[327] Moreover, only a few state pensions have the capital to make a material impact on the corporations they invest in, and these tend to exist in liberal-leaning states that support ESG.[328] At the same time, smaller state pensions are probably especially likely to need the returns from firms that, again, seem to be engaging in ESG at greater rates.[329] These are legitimate reasons to assume Anti-ESG Bills

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325. Karin Rives, *State Pension Funds Remain Insulated From GOP Crackdown on ESG*, S&P GLOBAL (Oct. 13, 2022), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/state-pension-funds-remain-insulated-from-gop-crackdown-on-esg-72459960 [https://perma.cc/QS8N-9GKB].

326. Lucy Pérez et al., *Does ESG Really Matter—and Why?*, MCKINSEY Q. (Aug. 22, 2022) https://www.mckinsey.com/capabilities/sustainability/our-insights/does-esg-really-matter-and-why [https://perma.cc/NK6Z-7WMU] ("Across industries, geographies, and company sizes, organizations have been allocating more resources toward improving ESG.").

327. Georgia, Colorado, and other states created comparable state statutory schemes in the late-aughts in response to international affairs. Salar Ghahramani, *Public Pensions, International Affairs and Divestment Regulations*, 17 PENSIONS 80, 83 (2012), https://link.springer.com/article/10.1057/pm.2012.6 [https://perma.cc/8RN8-EPB9]. In these states, public pension funds were barred from investing in companies that did business with Cuba, Syria, Iran, and Sudan, countries listed as state sponsors of terrorism. *Id.* at 80. The public funds themselves were generally responsible for bearing costs of divestment. *Id.* at 65. While it did eventually move forward with the legislation, the Georgia legislature noted "serious concerns regarding the efficacy of requiring the divestment of Georgia's divestment from large companies with fiscally sound histories and enviable histories of returns, and whether any effect on world-wide business activities might be too insubstantial as to warrant the cost to the state. . . . Further, [this body is concerned] with the cost of compliance. . . ." *Id.* at 83 (citing Ga. Code Ann. § 47-20-83.1; 2008 Ga. Laws Act 761, §§ 1–2).

328. For instance, in January 2022, Utah pulled $100 million from a BlackRock money market fund, but "such state efforts have not made a dent in the company's overall business." Rives, *supra* note 325.

329. Josh Lichtenstein, partner and head of ERISA Fiduciary Practice at Ropes & Gray, notes that ESG prohibitions could increase litigation risk for states and increase their vulnerability to breach of fiduciary duty claims. Noah Zuss, *ESG Bluster Leads to No Effect*

will eventually fall out of favor with states, clearing the way for pensions to form relationships with public banks.

Two things should now be noted: First, each public bank's charter will be a little different to reflect the unique community considerations and goals. But all public banks, no matter the location or the scale, ultimately operate with some prosocial mandate. Second, even with public banks, not all pension capital will be used in accordance with ESG. After all, in the above example, the teachers' pension is still invested in the coal company! At the same time, these banks can enable at least some of pensions' significant capital to be used in a way that is both financially *and* socially productive, making the public bank solution better than the current landscape by leaps and bounds.

F. CAPITALIZING PUBLIC BANKS

Because so few currently exist in the United States, public banks will require significant initial investment. Great opportunity cost certainly comes with choosing to build a new system versus simply identifying existing investments that may align with ESG and returns goals. Clear benefits, however, would accompany establishing these new institutions with long-term horizons and extensive prosocial benefits.

Pension funds must first enable the creation of new public banks through intangible and tangible support. Intangible support refers to endorsements of public banking, while tangible support refers to financial investments to capitalize the new public banks. Then, pensions must invest in the resulting public bank stock. These stock purchases will allow the banks to efficiently funnel the money to productive, prosocial causes.

Institutional investors regularly flex their capital to produce change. For instance, "[i]nvestor coalitions representing trillions of dollars' worth of investment have already supported carbon taxation and the Paris Climate Agreement."[330] Likewise, scholars regularly theorize new ways these investors can catalyze reforms. They have urged pensions to leverage their considerable influence to try to change the regulatory pressures that encourage short-

for Three States' Retirement Systems, PLANSPONSOR (Oct. 13, 2022), https://www.plansponsor.com/in-depth/esg-bluster-leads-no-effect-three-states-retirement-systems/ [https://perma.cc/V8S7-UTPT].

330. Quigley, *supra* note 64, at 15.

termism,[331] or to engage with other financial actors to encourage them to incorporate ESG into their methodologies.[332] Thus, the notion that intangible support from pensions makes a difference is an extremely practical one.

To this end, the private sector's response to public banking has been cautious at best and outwardly hostile at worst. The private banking industry, unsurprisingly, fancies itself the best-equipped to offer banking services of any kind, and frequently warns against public options. For example, the American Bankers Association's official position is that public banks would be not only "redundant in the current marketplace, where financial offerings are already efficiently meeting consumer needs, but potentially dangerous—placing taxpayer funds in institutions that may not have deposit insurance and whose business decisions will be driven by political priorities instead of sound risk management."[333]

This statement includes many inaccuracies, from the claim that the existing marketplace is already efficient (traditional financial institutions regularly come under fire for discriminatory lending campaigns)[334] to the notion that the private sector has an unblemished record of sound risk management (the present uncertainty about the survival of the American pension fund system alone provides a strong argument to the contrary).[335]

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331. Urwin, *supra* note 65, at 29, 31 ("short-termism" here refers to short-term return targets).

332. UNEP FINANCE INITIATIVE, UNIVERSAL OWNERSHIP: WHY ENVIRONMENTAL EXTERNALITIES MATTER TO INSTITUTIONAL INVESTORS 5 (2011), https://www.unepfi.org/fileadmin/documents/universal_ownership_full.pdf [https://perma.cc/QMR2-C7FA].

333. AM. BANKERS ASS'N, PUBLIC BANKS: ABA POSITION (2021), https://www.aba.com/advocacy/our-issues/public-banks [https://perma.cc/HJJ4-6BKY].

334. *See, e.g.*, Tamaryn Waters, *Wells Fargo Sued for Race Discrimination in Mortgage Lending Practices*, USA TODAY (Apr. 26, 2022), https://www.usatoday.com/story/money/2022/04/26/wells-fargo-being-sued-discriminating-against-black-borrowers/7451521001/ [https://perma.cc/W9JQ-4Q4K].

335. *See, e.g.*, Grant Suneson, *Retirement Warning Signs? Pension Crisis Hits States. Here's the Biggest, Smallest Funding Shortfalls*, USA TODAY (Dec. 11, 2020), https://www.usatoday.com/story/money/2020/12/11/every-states-pension-crisis-ranked/115099952/ [https://perma.cc/6WYR-MVQC] ("[N]early every state is facing a pension shortfall."); David Eifrig, *The Great American Pension Crisis*, STANSBERRY INVESTOR (June 29, 2021), https://stansberryresearch.com/articles/the-great-american-pension-crisis [https://perma.cc/U54V-ZHEH] ("Public pensions nationwide are crumbling. . . . If you're currently retired, the coming American pension crisis could mean the elimination of cost-of-living adjustments, higher health care premiums, or even cuts to your base pension check."); Monique Morrissey, *The State of American Retirement Savings*, ECON. POL'Y INST. (Mar. 3, 2016), https://www.epi.org/publication/the-state-of-american-retirement-savings/ [https://perma.cc/ACC4-3SDZ] ("Retirement wealth has not grown fast enough to keep pace with an aging population and other changes . . . .").

Unfortunately, such claims can and do hold weight with laypersons and policymakers alike.[336] If pension funds—as prominent stakeholders within the financial sector—offer endorsements of public banks, it may temper private-sector concerns. Because the sector remains a powerful political lobby, assuaging its fears could go a long way in hastening the creation of public banks[337]—indeed, the success of the BND is due in no small measure to the consistent endorsement from the state's Bankers Association.[338] Alternatively, pensions may be important enough on their own that, if they advocate for public banks, lawmakers will be driven to consider their arguments.[339]

In addition to endorsing public banking as an idea, pensions ought to endorse related actions, organizations, and movements. Many governments create research bodies to study the impacts of potential policies. San Francisco, for instance, created the Municipal Banking Feasibility Task Force in 2017,[340] and the group's final report culminated in eventual legislation approving a public bank for the city.[341] Public banking advocates in other regions are pushing for similar exploratory bodies because of the

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336. *See, e.g.*, John Fullerton, *Is There a Case for Public Banking in America?*, CAP. INST. (Apr. 30, 2012), https://capitalinstitute.org/blog/case-public-banking-america/ [https://perma.cc/XF9V-B2KS] (self-professed nonexpert writing "I'm not ready to embrace a call for state-owned banks quite yet, and there [is] a . . . challenging question . . . of whether government or the private banking system should control credit creation"). *See also Our Position: State-Owned Public Banks*, *supra* note 267 (Independent Bankers Association memo leading to the blockage of public banking legislation in New York).

337. *See, e.g.*, Raghuram G. Rajan & Luigi Zingales, *The Great Reversals: The Politics of Financial Development in the Twentieth Century*, 69 J. FIN. ECON. 5, 19 (2003). Rajan and Zingales posit that incumbents in financial markets will oppose financial development because it will generate competition, explaining why most countries were more financially developed in 1913 than in 1980, and have only recently surpassed their 1913 levels. *Id.* at 5, 7, 19. If indeed true, it is essential to minimize opposition from incumbents in the American financial system in order to promote new innovations like public banks.

338. Deborah M. Figart & Mariam Majd, *The Public Bank Movement: A Response to Local Economic Development and Infrastructure Needs in Three U.S. States*, 59 CHALLENGE 461, 464 (2016).

339. *See, e.g.*, Natascha van der Zwan, *Financialisation and the Pension System: Lessons from the United States and the Netherlands*, 15 J. MOD. EUR. HIST. 554, 578 (2017) ("[P]ension funds have become more assertive in leveraging their assets and demanding political reform which are in the interest of the financial industries.").

340. JOSÉ CISNEROS, MUNICIPAL BANK FEASIBILITY TASK FORCE REPORT 11 (2019) https://sftreasurer.org/files/2019-08/2.%20Municipal%20Bank%20Report_FINAL_03-01-19.pdf [https://perma.cc/T5LK-WYH3].

341. Laura Wenus, *Group of Experts Devising Business Plan for SF Public Bank*, S.F. PUB. PRESS (Aug. 5, 2021), https://www.sfpublicpress.org/group-of-experts-devising-business-plan-for-sf-public-bank/ [https://perma.cc/F3NY-WJ6E].

San Francisco task force's success.[342] Thus, one powerful form of intangible support would be the endorsement of such exploratory initiatives around the nation, a conservative and non-threatening means of raising awareness around the policy. Otherwise, pensions may directly call for such initiatives themselves.

Capitalizing public banks—pensions' "tangible" support—will require region-specific research on required funding and how different stakeholders should split initial costs. Massachusetts activists, for instance, are pushing for $50 million per year for four years, to be largely obtained from the state's Municipal Depository Trust.[343] Meanwhile, one major public banking activist believes Philadelphia need only allocate five to ten percent of its pension assets to capitalize a municipal bank.[344] Pensions are ill-suited to conduct this research, of course, but their intangible support of public banking should catalyze significant progress in this area. Once newly capitalized public banks have adequately proliferated, they may then sell shares to investors, including pensions. With these liquidity injections, the banks can embark on expansive, prosocial campaigns to generate considerable value for investors and society.

CONCLUSION

In his classic *The Concept of the Corporation* and *The Practice of Management*, corporate theorist Peter Drucker opined that all business organizations have obligations to contribute to society and to enable individuals to realize the promises of American society.[345] While acknowledging that such organizations are often by themselves unequipped to do so, Drucker believed managers

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342. *See, e.g.*, Vince Grzegorek, *Local Officials, Candidates, and Organizations Join in Calling for Cleveland Municipal Bank Exploratory Committee*, CLEVELAND SCENE (Aug. 30, 2021), https://www.clevescene.com/news/local-officials-candidates-and-organizations-join-in-calling-for-cleveland-municipal-bank-exploratory-committee-36613785 [https://perma.cc/3DWL-X4BF].

343. *What Is A Public Bank?*, MASS. PUB. BANKING (2022), https://masspublicbanking.org/learn-more-about-public-banking/#.Yfhnp_XMLvU [https://perma.cc/PZR2-EBVB].

344. Scott Baker, Senior Advisor to Pub. Banking Inst., Presentation at the Philadelphia Public Bank Summit: On Monetizing the Philadelphia Public Bank (2021), https://www.slideshare.net/ScottOnTheSpot/philly-public-bank-and-cafr-presentation [https://perma.cc/GLS9-Z4BG].

345. *See* PETER DRUCKER, THE CONCEPT OF THE CORPORATION (1946); Peter Drucker, THE PRACTICE OF MANAGEMENT (1954); *see also* Marcia Kurzynski, *Peter Drucker: Modern Day Aristotle for the Business Community*, 18 J. MGMT. HIST. 6, 9–10 (2012).

should be stewards of the business as a social entity, promoting the public good, advancing society's core beliefs, and contributing to societal harmony.[346] Over six decades later, it is clear that the nation still lacks an institutionalized pension structure that enables managers to pursue both positive financial returns *and* prosocial action. Perhaps, then, the solution is not to restructure what already exists, but to build something entirely new.

The stories of public banks—past and present—offer compelling evidence that such banks can generate positive returns for shareholders, thereby eliminating fiduciary hurdles for investors. Accordingly, by directing some of their funds toward these banks, pensions may effectively forego their ESG burdens and leave such considerations to democratically-administered vehicles. So, if indeed the time has come to build anew, adding public banks may be just the approach. Pensions, with their enormous capital and industry relevance, occupy a unique position to hasten their creation. With their help, the nation may finally assemble the necessary, modern financial system—a system not weighed down by the greed and myopia that often accompanies pure pecuniary interest, but rather one nurtured and elevated by the positive externalities and hyperopia accompanying a more altruistic framework infused with the public interest.

346. DRUCKER, *supra* note 345, at 388.