

Combating Climate Change Through a Duty to Divest

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The movement for divestment from fossil fuels is building momentum, and pension funds, municipalities, and universities around the world are increasingly being pressured to eliminate their holdings in fossil fuel stocks in order to fight climate change. While the debate over whether divestment is in line with fiduciary duty continues, there is some consensus that divestment, in theory, is consistent with meeting fiduciary duty. Yet, in practice, institutions fear divesting due to a lack of clear law on the issue and fiduciary standards that discourage departure from the status quo. The relatively new movement has largely avoided the courts up to this point. However, in November 2014, a group of Harvard students paved the way with a lawsuit against Harvard alleging claims of (1) “mismanagement of charitable funds” and (2) “intentional investment in abnormally dangerous activities” for failing to divest from fossil fuel stocks. Previous literature on the subject has focused on legislative and regulatory solutions rather than looking at possible legal claims that could compel divestment under current laws. The Harvard suit suggests, however, that there is a role for courts to play; litigation might be the only viable solution as legislative and regulatory attempts are moving too slowly and ineffectively to deal with the pressing nature of climate change. This Note argues that courts should recognize the special threat posed by climate change to humanity as well as to portfolio risks and returns, take an expansive view of the special duties charitable institutions and public entities owe, and require charitable and public institutions to take into account the effects of climate change when making investment decisions.

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I. INTRODUCTION

In the fall of 2010, a group of students at Swarthmore College formed the group Swarthmore Mountain Justice and took the first steps towards mobilizing the fossil fuel divestment movement.¹ The students had travelled and witnessed first-hand the effects of mountaintop removal coal-mining² on the Appalachians and local communities and, as a result, launched the first campus divestment campaign in which they began petitioning Swarthmore University to divest its endowment resources from the 16 largest fossil fuel companies.³

In August 2015, President Obama stated “no challenge poses a greater threat to our future than climate change.”⁴ The divestment movement arises from recognition that climate change destroys global well-being and unjustly impacts already marginalized communities most severely. As Obama has explained:

Climate change is already disrupting our agriculture and ecosystems, our water and food supplies, our energy, our infrastructure, human health, human safety — now. Today. And climate change is a trend that affects all trends — economic trends, security trends. Everything will be impacted. And it becomes more dramatic with each passing year.⁵

If action is not taken, the chilling result is:

Submerged countries. Abandoned cities. Fields no longer growing. Indigenous peoples who can't carry out traditions that stretch back millennia. Entire industries of people who

1. Swarthmore Mountain Justice, *Campaign History*, SWARTHMORE MOUNTAIN JUSTICE, <http://swatmountainjustice.wordpress.com/ourcampaign/#campaignhistory> [http://perma.cc/6N96-69HS].

2. Mountaintop removal coal-mining involves clearing upper-elevation forests, using explosives to break up the rock and access coal, and then pushing the excess rock into valleys and filling streams. It is associated with a number of environmentally harmful effects including loss of forests, declines in biodiversity, and water and air pollution. See, e.g., M.A. Palmer et al., *Mountaintop Mining Consequences*, 327 *SCIENCE* 148 (2010).

3. Swarthmore Mountain Justice, *supra* note 1.

4. Barack Obama, Remarks by the President at National Clean Energy Summit (Aug. 25, 2015), <https://www.whitehouse.gov/the-press-office/2015/08/25/remarks-president-national-clean-energy-summit> [http://perma.cc/3UNR-DG33].

5. Barack Obama, Remarks by the President at the GLACIER Conference — Anchorage, AK (Sept. 1, 2015), <https://www.whitehouse.gov/the-press-office/2015/09/01/remarks-president-glacier-conference-anchorage-ak> [http://perma.cc/2247-69SM].

can't practice their livelihoods. Desperate refugees seeking the sanctuary of nations not their own. Political disruptions that could trigger multiple conflicts around the globe.⁶

Climate change is not just an environmental issue, but also a social justice concern.⁷ The United Nations Framework Convention on Climate Change (UNFCCC)⁸ has acknowledged: "Impacts of climate change, such as drought, floods, extreme weather events and reduced food and water security, affect women and men differently with the poorest being the most vulnerable. 70 per cent of the world's poor are women."⁹ Other groups disproportionately impacted include "children, older persons, indigenous peoples, minorities, migrants, rural workers, [and] persons with disabilities."¹⁰ The Office of the United Nations High Commissioner for Human Rights has emphasized that these "disproportionate impacts . . . raise concerns of climate justice, fairness, equity and access to remedy."¹¹

The divestment movement, fueled by this need for urgency, got its spark when in August 2012 *Rolling Stone Magazine* pub-

6. *Id.*

7. SWARTHMORE MOUNTAIN JUSTICE, INSTITUTIONAL MEMORY DOCUMENT 2011–2012 21–22 (2012), http://swatmountainjustice.files.wordpress.com/2012/12/mj_institutional_memory_2011-2012_final_draft.pdf [<http://perma.cc/UX7H-5WH7>] ("Issues of fossil fuel extraction/consumption and environmental degradation are inherently social justice issues. Environmental Justice challenges the ways in which the distribution of resources and the ramifications of environmental degradation disproportionately harm some individuals, social groups, and communities in ways that perpetuate the oppression of already marginalized communities in the interests of the owning class. Environmental hazards are disproportionately concentrated in communities of color and low-income communities.").

8. The UNFCCC is an international treaty signed in 1992 by countries pledging to work together to limit average global temperature increase and best deal with the inevitable climate change expected to occur. See UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE (1992), http://unfccc.int/files/essential_background/background_publications_htmlpdf/application/pdf/conveng.pdf [<http://perma.cc/H8VZ-N5ZF>].

9. *Gender and Climate Change*, UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE, http://unfccc.int/gender_and_climate_change/items/7516.php [<http://perma.cc/SL9Q-DYZ4>]. See also JOHN H. KNOX, UN SPECIAL RAPPORTEUR, MAPPING REPORT ON CLIMATE CHANGE AND HUMAN RIGHTS (2014), <http://srenvironment.org/wp-content/uploads/2014/08/Climate-Change-mapping-report-15-August-final.docx> [<http://perma.cc/54XK-YT67>].

10. SUBMISSION OF THE OFFICE OF THE HIGH COMMISSIONER FOR HUMAN RIGHTS TO THE 21ST CONFERENCE OF THE PARTIES TO THE UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE 2 (Nov. 26, 2015), http://www.ohchr.org/Documents/Issues/ClimateChange/KeyMessages_on_HR_CC.pdf [<https://perma.cc/683M-BH3T>].

11. *Id.* at 8.

lished a landmark article¹² by author Bill McKibben, founder of the organization 350.org.¹³ The article presented the following facts: two degrees Celsius is the maximum amount of temperature increase the planet can take before catastrophe occurs, 565 more gigatons of carbon is the most that can be released into the air before we exceed that point, and 2,795 gigatons is the amount of carbon deposits fossil fuel companies have in their reserves waiting to release.¹⁴ In November 2012, Bill McKibben and 350.org launched the “Do the Math” tour, traveling around the country and explaining the math behind climate change and carbon emissions.¹⁵ The tour led to the 350.org Fossil Free Divestment Movement, a network of independent campaigns petitioning institutions and investors to divest¹⁶ from fossil fuels.¹⁷ The Fossil Free campaigns are demanding that institutions (1) freeze

12. The article quickly went viral and now frequently appears on timelines of the divestment movement as a turning point. See Joe Romm, *McKibben Must-Read: ‘Global Warming’s Terrifying New Math’*, CLIMATE PROGRESS (July 23, 2012, 6:40 PM), <http://thinkprogress.org/climate/2012/07/23/565751/mckibben-must-read-global-warming039s-terrifying-new-math> [<http://perma.cc/56GP-DFAX>]; Michelle Y. Raji, *Timeline: Fossil Fuels Divestment*, THE HARVARD CRIMSON (Oct. 2, 2014), <http://www.thecrimson.com/article/2014/10/2/timeline-fossil-fuels-divestment> [<http://perma.cc/QHZ6-D3T9>].

13. Bill McKibben, *Global Warming’s Terrifying New Math*, ROLLING STONE (July 19, 2012), <http://www.rollingstone.com/politics/news/global-warmings-terrifying-new-math-20120719?page=4> [<http://perma.cc/K6SK-LCYX>].

14. *Id.*

15. DO THE MATH TOUR, <http://math.350.org> [<http://perma.cc/7WZL-L9MK>] (last visited Jan. 11, 2016).

16. Fossil Free defines divestment as “the opposite of an investment — it simply means getting rid of stocks, bonds, or investment funds that are unethical or morally ambiguous.” *What is Fossil Fuel Divestment?*, FOSSIL FREE, <http://gofossilfree.org/what-is-fossil-fuel-divestment> [<http://perma.cc/ST3C-K4EY>].

17. DO THE MATH TOUR, *supra* note 15. Activists claim divestment is necessary because “if it’s wrong to wreck the climate, it’s wrong to profit from that wreckage.” Bill McKibben, *The Case for Fossil-Fuel Divestment*, ROLLING STONE (Feb. 22, 2013), <http://www.rollingstone.com/politics/news/the-case-for-fossil-fuel-divestment-20130222> [<http://perma.cc/CAD5-UACQ>]. Fossil fuel companies spend hundreds of millions of dollars per year lobbying for industry-friendly policies that exacerbate the threat of climate change. Claire Moser & Matt Lee-Ashley, *The Fossil-Fuel Industry Spent Big to Set the Anti-Environment Agenda of the Next Congress*, CENTER FOR AMERICAN PROGRESS (Dec. 22, 2014), <https://www.americanprogress.org/issues/green/news/2014/12/22/103667/the-fossil-fuel-industry-spent-big-to-set-the-anti-environment-agenda-of-the-next-congress> [<http://perma.cc/M3C2-2TE9>]. Exxon has been accused of burying its own internal studies that confirmed the risk of climate change early on in the 1980s and instead going on to spend millions funding climate change denial. See Neela Banerjee et al., *Exxon’s Own Research Confirmed Fossil Fuels’ Role in Global Warming Decades Ago*, INSIDECLIMATE NEWS (Sept. 16, 2015), <http://insideclimatenews.org/news/15092015/Exxons-own-research-confirmed-fossil-fuels-role-in-global-warming> [<http://perma.cc/7JZZ-S3WD>]. These factors suggest that fossil fuel companies are interested only in selling their climate-devastating product and shoulder blame for the lack of action on climate change thus far.

new investments in fossil fuel companies immediately, and (2) divest from direct ownership and comingled funds that include fossil fuel equities and corporate bonds within 5 years.¹⁸ The movement saw its first major victory with Stanford University, which, in May 2014, agreed to divest its \$18.7 billion endowment from coal companies.¹⁹ The movement has only been intensifying since then; in September 2014, 181 institutions and 656 individuals with \$50 billion in assets had committed to divest, by September 2015, the number had grown to 436 institutions and 2,040 individuals with \$2.6 trillion in assets,²⁰ and by December 2015 the number had increased to 500 institutions representing \$3.4 trillion in assets.²¹

Divestment is a strategy that originally came to force to combat apartheid in South Africa when activists pressured funds to eliminate stock holdings of corporations that were engaged in business in South Africa.²² In the 1980s, the movement spread across college campuses as students petitioned universities to

18. *About Fossil Free*, FOSSIL FREE, <http://gofossilfree.org/about-fossil-free> [<http://perma.cc/E3NS-STND>].

19. Stanford University, *Stanford to Divest from Coal Companies*, STANFORD NEWS (May 6, 2014), <http://news.stanford.edu/news/2014/may/divest-coal-trustees-050714.html> [<http://perma.cc/N5C6-WN96>].

20. See ARABELLA ADVISORS, MEASURING THE GROWTH OF THE GLOBAL FOSSIL FUEL DIVESTMENT AND CLEAN ENERGY INVESTMENT MOVEMENT (Sept. 2015) at 1, <http://www.arabellaadvisors.com/wp-content/uploads/2015/09/Measuring-the-Growth-of-the-Divestment-Movement.pdf> [<http://perma.cc/6AF2-DJ5W>].

21. Melanie Mattauch, *In the space of just 10 weeks*, FOSSIL FREE (Dec. 2, 2015), <http://gofossilfree.org/in-the-space-of-just-10-weeks> [<http://perma.cc/DJ27-JV8T>]. These include, of note, University of California, Georgetown University, and Oxford University. Arabella Advisors, *supra* note 20 at 2.

22. There is still a debate over the extent to which the South African divestment movement had an impact on dismantling the Apartheid regime. The movement has widely been seen as successful. See, e.g., Desmond Tutu, *Divesting From Injustice*, HUFFINGTON POST: THE WORLD POST (May 25, 2011, 4:10 PM), http://www.huffingtonpost.com/desmond-tutu/divesting-from-injustice_b_534994.html [<http://perma.cc/H6V9-GMTJ>] (“In South Africa, we could not have achieved our freedom and just peace without the help of people around the world, who through the use of non-violent means, such as boycotts and divestment, encouraged their governments and other corporate actors to reverse decades-long support for the Apartheid regime.”); Eric Hende, *Does Divestment Work?*, HARVARD POLITICAL REVIEW (Oct. 2, 2012, 12:04 AM), <http://harvardpolitics.com/harvard/does-divestment-work> [<http://perma.cc/SC5H-T3BJ>] (“Divestment greatly increased public visibility surrounding the injustices of South Africa’s apartheid government. It is almost certain that worldwide popular opposition in the 1980s contributed to the decline of apartheid, and divestment was an important piece of this puzzle.”). However, a study by Siew Hong Teoh, Ivo Welch, and C. Paul Wazzan found that it had little to no financial impact on public market valuations. Siew Hong Teoh et al., *The Effect of Socially Activist Investment Policies on the Financial Markets: Evidence from the South African Boycott*, 72 THE J. OF BUS. 35 (1999).

divest their endowments of these holdings.²³ For example, the University of California divested \$3 billion from such companies.²⁴ In the 1990s, divestment was again used as a strategy, this time to pressure tobacco companies.²⁵ It has also been used as a tool to pressure gun manufacturers²⁶ and companies doing business in Israel²⁷ and Sudan,²⁸ among others.²⁹ These past movements brought to the forefront the role of social objectives in making investment decisions, and raised questions about whether considering social objectives was permissible under the fiduciary duties of fund managers.³⁰ These questions still linger in the current debate over divestment from fossil fuels.³¹

Divesting is a form of social investing, which one of the pioneers of the movement has defined as “the systematic incorpora-

23. Victor Luckerson, *How College Kids Helped Divest \$50 Billion from Fossil Fuels*, TIME (Sept. 22, 2014), <http://time.com/3419456/fossil-fuel-divestment-climate-change> [<http://perma.cc/VZK6-YCWD>].

24. *Id.*

25. See N. Wander & R.E. Malone, *Fiscal Versus Social Responsibility: How Philip Morris Shaped the Public Funds Divestment Debate*, 15 TOBACCO CONTROL 231, 238 (2006) (finding “[t]he 1990s tobacco stock divestment movement put pressure on the tobacco industry, and caused top PM executives to expend considerable time and resources defending against it. Divestment advocacy may have been of limited success in convincing public fund decisions-makers to withdraw their fund’s financial resources from the tobacco industry, but the states where divestment advocates succeeded in whole or in part were/are highly visible, often trendsetters in public health and social policymaking.”).

26. Katie Gilbert, *Balancing the Moral and Financial Sides of Gun Divestment*, INSTITUTIONAL INVESTOR (July 26, 2014), <http://www.institutionalinvestor.com/article/3365531/investors-pensions/balancing-the-moral-and-financial-sides-of-gun-divestment.html?eventlogin=Login&login=1&actionname=login&eid=E017#VQUCdmYhzOo> [<http://perma.cc/L32Q-P6AU>].

27. Zeina Azzam, *Israel Facing New Divestment Support in US*, AL JAZEERA (July 24, 2014, 7:10 AM), <http://www.aljazeera.com/indepth/features/2014/07/presbyterian-israel-facing-new-divestment-support-us-20147238133786329.html> [<http://perma.cc/5SKV-3AUA>].

28. See U.S. GOV’T ACCOUNTABILITY OFF., GAO-10-742, SUDAN DIVESTMENT: U.S. INVESTORS SOLD ASSETS BUT COULD BENEFIT FROM INCREASED DISCLOSURE REGARDING COMPANIES’ TIES TO SUDAN 2 (2010) (“Since 2006, U.S. state treasurers and public pension fund managers have divested or frozen about \$3.5 billion in assets primarily related to Sudan in response to their states’ laws and policies; U.S. investment companies, which also sold Sudan-related assets, most commonly cited normal business reasons for changes in their holdings. . . . Thirty-five U.S. states have enacted legislation or adopted policies affecting their investments related to Sudan, primarily in response to the Darfur crisis, as well as in response to Sudan’s designation by the U.S. government as a state sponsor of terrorism.”).

29. Luckerson, *supra* note 23.

30. Christof Heyns, *Divestment in the United States: Trust Law and the Law of Charities*, 23 COMP. & INT’L L.J. S. AFR. 34 (1990).

31. See generally Benjamin J. Richardson, *Do the Fiduciary Duties of Pension Funds Hinder Socially Responsible Investment?*, 22 BANKING & FIN. L. REV. 145 (2007), http://cmsdata.iucn.org/downloads/cel10_richardson.pdf [<http://perma.cc/VJ4L-9FGB>].

tion of ethical values and objectives in the investment decision-making process.”³² Social investing can take several forms, including ethical screens (excluding a certain class of assets from portfolios), “best in class” portfolios (including only those firms that are performing at a higher level than their peers on the relevant social and environmental issues), shareholder advocacy (using shareholder rights to sway firm behavior in a more ethical direction), and institutional support, such as banks giving beneficial terms to finance ethical and socially beneficial projects.³³ Screens can take several forms: passive screens, which follow an index that employs certain environmental, social, and governance (ESG) criteria; negative screens, which exclude companies that perform poorly on ESG benchmarks; and positive screens, which include companies only if they meet certain ESG criteria.³⁴ One of the major challenges with divestment is persuading institutions that divestment is not in conflict with their fiduciary duties.³⁵ Trustees and managers of funds are often thought to have a strict fiduciary duty to maximize financial benefit to the fund beneficiaries, with ESG criteria playing only a secondary role, if any role at all.³⁶ Thus many proponents of social investing have begun to make a “business case” for social investing, claiming the environmentally and socially responsible investment decisions are also the ones that will lead to the best returns.³⁷

Institutional investors have expressed unease at fossil fuel divestment, voicing concerns over the increased risk involved in a less diversified portfolio and the financial injury that may result from pulling out of historically high-performing fossil fuel

32. Lewis D. Solomon & Karen C. Coe, *Social Investments by Nonprofit Corporations and Charitable Trusts: A Legal and Business Primer for Foundation Managers and Other Nonprofit Fiduciaries*, 66 UMKC L. REV. 213, 214 (1997).

33. Benjamin J. Richardson, *Reforming Climate Finance through Investment Codes of Conduct*, 27 WIS. INT'L L.J. 483, 488 (2009).

34. FRESHFIELDS BRUCKHAUS DERINGER, A LEGAL FRAMEWORK FOR THE INTEGRATION OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE ISSUES INTO INSTITUTIONAL INVESTMENT 25 (2005), http://www.unepfi.org/fileadmin/documents/freshfields_legal_resp_20051123.pdf [<http://perma.cc/5B5Q-M9MA>].

35. See, e.g., Joakim Sandberg, *Socially Responsible Investment and Fiduciary Duty: Putting the Freshfields Report into Perspective*, 101 J. BUS. ETHICS 143, 146 (2011) (“In a recent survey among American pension fund trustees, for example, as many as 45% of respondents indicated that considerations of fiduciary duty were their main reason for not engaging more actively in SRI.”).

36. See, e.g., *id.* at 148 (“The current legal framework surrounding fiduciary duty dictates that the overriding goal of institutional investors should be to provide financial benefits for their beneficiaries.”).

37. Richardson, *supra* note 33, at 489.

stocks.³⁸ There are also those who argue that divestment is not a proven strategy,³⁹ that it has little to no effect on markets,⁴⁰ and that there are better strategies for putting pressure on fossil fuel companies, such as engaging in shareholder activism.⁴¹ On the other hand, proponents argue that complying with fiduciary duty *requires* divestment,⁴² as the carbon bubble is due to burst, making fossil fuel companies risky investments.⁴³ They also claim that divestment has been historically effective in past movements.⁴⁴

The divestment movement, since 2011, has largely stayed out of the courtroom. The first attempt to litigate for divestment comes from a group of Harvard students who, on November 19th, 2014, filed a complaint in Suffolk County Superior Court in Massachusetts against the president and fellows of Harvard Col-

38. See, e.g., Drew Faust, *Fossil Fuel Divestment Statement*, HARVARD UNIVERSITY (Oct. 3, 2013) <http://www.harvard.edu/president/fossil-fuels> [<http://perma.cc/ZY4P-2H9N>].

39. See, e.g., Ivo Welch, *Why Divestment Fails*, N.Y. TIMES (May 9, 2014), <http://www.nytimes.com/2014/05/10/opinion/why-divestment-fails.html> [<http://perma.cc/9KSV-S9FV>] (“Individual divestments, either as economic or symbolic pressure, have never succeeded in getting companies or countries to change.”); Teoh et al., *supra* note 22.

40. Daniel Fischel, *The Feel Good Folly of Fossil Fuel Divestment*, WALL ST. J. (Feb. 9, 2015), <http://www.wsj.com/articles/daniel-r-fischel-the-feel-good-folly-of-fossil-fuel-divestment-1423527484> [<http://perma.cc/RHP3-ECFZ>] (“Over the long run, stock prices are primarily driven by fundamentals, not the decisions of particular investors to hold or sell. Moreover, the vast majority of institutions currently attempting to implement fossil-fuel divestment policies hold a very small share of stock in the companies that are targets of the campaign. Divestment would have little or no effect on company share prices.”).

41. See, e.g., Anne Stausboll, *Selling Out of Fossil Fuels No Solution for Climate Change*, FINANCIAL TIMES (Mar. 22, 2015), <http://www.ft.com/cms/s/0/def47f8c-bb8d-11e4-b95c-00144feab7de.html#axzz3xQb1RVoR> [<http://perma.cc/42KP-SU6H>] (The chief executive officer for the California Public Employees’ Retirement System explains, “As a long-term investor, a seat at the table is the most effective way to shape how our investment capital gets put to use in a sustainable manner.”); Scott Wisor, *Why Climate Change Divestment Will Not Work*, ETHICS & INT’L AFFAIRS (Sept. 22, 2014), <http://www.ethicsandinternationalaffairs.org/2014/why-climate-change-divestment-will-not-work> [<http://perma.cc/GW7Y-YXG7>].

42. See, e.g., *Divesting from Fossil Fuels Will Soon be a Fiduciary Duty*, GREEN MARKET ORACLE (Oct. 2, 2014), <http://www.thegreenmarketoracle.com/2014/10/divesting-from-fossil-fuels-will-soon.html> [<http://perma.cc/9AQM-KEZM>].

43. See, e.g., Bevis Longstreth, *The Financial Case for Divestment of Fossil Fuel Companies by Endowment Fiduciaries*, HUFFINGTON POST: THE BLOG (Nov. 2, 2013, 2:52 PM), http://www.huffingtonpost.com/bevis-longstreth/the-financial-case-for-di_b_4203910.html [<http://perma.cc/AL25-ND95>].

44. See, e.g., Ning Ding et al., *When Does a Stock Boycott Work? Evidence From a Clinical Study of the Sudan Divestment Campaign* (2014), <http://ssrn.com/abstract=2469575> [<http://perma.cc/AM4A-QUJV>] (authors conduct an empirical examination of the impact of the Sudan divestment campaign and find that it decreased breadth of ownership and stock prices).

lege.⁴⁵ They alleged two claims: (1) “mismanagement of charitable funds” and (2) “intentional investment in abnormally dangerous activities.”⁴⁶ This lawsuit has shifted the debate to looking at whether public and charitable institutions owe their beneficiaries a duty beyond just maximizing financial benefits when making investment decisions. This Note looks at the role litigation could play in the divestment movement and argues that courts should mandate that public and charitable institutions consider the risk climate change poses to their portfolio and to human well-being and divest from companies whose business plans threaten the climate.

Part II of this Note discusses the current fiduciary duties applicable to various charitable institutions and public pension funds and views on their compatibility with divestment. Part III discusses the arguments for and against divestment and the role these arguments play in the discussion of fiduciary duty and whether institutions have to consider climate change impacts. Part IV looks at the major barriers to divestment and potential reforms that have been discussed. Finally, Part V argues that courts should consider expanding fiduciary duty to obligate charitable and public institutions to take into account climate change impacts when making investment decisions. It does so by examining how the Harvard lawsuit is changing the way divestment is framed, making a case for why public and charitable institutions owe a special duty to the public, and using the “atmosphere as public trust” theory of litigation as a model.

II. CURRENT FIDUCIARY DUTY LAW AND ITS RELATIONSHIP TO DIVESTMENT

This Part discusses the major fiduciary duties relevant to divestment and looks at the current view on whether divestment is legally compatible with those duties. It first discusses broadly the fiduciary duties that arise under trust law and corporate law, next examines the fiduciary duties of directors of charities and public pensions, and finally assesses in depth how specific fiduciary duties impact divestment decisions.

45. Complaint for Declaratory and Injunctive Relief, Harvard Climate Justice Coal. v. President and Fellows of Harvard Coll., 32 Mass. L. Rptr. 529 (Mass. Sup. Ct. 2015) (No. 14-3620).

46. *Id.*

A. FIDUCIARY DUTIES UNDER TRUST LAW AND CORPORATE LAW

Investment decisions made by institutional investors are regulated by fiduciary duties, which in the United States are set by trust law and corporate law, and vary according to the type of fund being managed.⁴⁷ Judge Cardozo described the duty of a fiduciary⁴⁸ as being a standard “stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is . . . the standard of behavior.”⁴⁹

Fiduciary duty from trust law imposes several duties on fiduciaries that are relevant in the divestment context, including a duty of prudence, duty of loyalty, and duty of impartiality. The adoption of the modern prudent investor rule for trusts is an important development in federal statutes, state statutes following uniform laws (such as the widely adopted Uniform Prudent Investor Act (UPIA)), and state common law.⁵⁰

The fiduciary standards applying to corporate directors are less stringent than those applied to trustees.⁵¹ Corporate law usually does not apply the modern prudent investor rule.⁵² Corporate law requires that corporate directors fulfill a duty of “undivided loyalty, requiring directors to make investment decisions only with reference to the organization’s purposes, and a duty of care, which means business care.”⁵³ In some cases corporate directors are given deference under the business judgment rule.⁵⁴

47. See Solomon & Coe, *supra* note 32 at 218–33 (summarizing laws governing investments by charitable trusts, nonprofit corporations, and private foundations in the United States).

48. A fiduciary relationship comes about “when one party (the ‘fiduciary’) acts on behalf of another party (the ‘beneficiary’) while exercising discretion with respect to critical resources belonging to the beneficiary.” Richardson, *supra* note 31, at 150.

49. *Meinhard v. Salmon*, 164 N.E. 545 (N.Y. 1928).

50. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 102–03.

51. Heyns, *supra* note 30, at 40.

52. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 104.

53. Heyns, *supra* note 30, at 40.

54. The business judgment rule presumes proper conduct as long as the directors had a rational basis for their decisions (and exercised reasonable care in the decision-making process) and acted in good faith. *Id.* at 40–41.

B. FIDUCIARY DUTIES APPLYING TO CHARITIES AND PENSION FUNDS

1. *Charities*

A charity can take the form of a charitable trust or a non-profit corporation (or a private foundation, which takes one of these forms but also has additional obligations under Internal Revenue Service (IRS) regulations).⁵⁵ Charitable trustees exercise their duties toward a “charitable purpose” and corporate directors owe their duty to the corporation.⁵⁶ Most universities in the United States are organized as charitable corporations, and many cite only “the pursuit of knowledge” as their institutionally recognized objective.⁵⁷ Divestment and social investing in general can be particularly appealing for fiduciaries of charities, because they can be one means to accomplish the charity’s goals.⁵⁸ Because fiduciaries of charities are not accountable to specific beneficiaries or shareholders, legislatures, attorneys general, and courts have traditionally monitored their investments decisions strictly; however, these institutions also are given greater discretion in making investments because their purposes are charitable.⁵⁹ While it may be undisputed that social investing related to the charitable purpose of the charity is proper,⁶⁰ some believe consideration of unrelated social factors when making investment decisions is still prohibited.⁶¹

55. Evelyn Brody, *Charity Governance: What’s Trust Law Got To Do With It?*, 80 CHIKENT L. REV. 641, 646 (2005).

56. *Id.* at 644.

57. Heyns, *supra* note 30, at 42.

58. See Solomon & Coe, *supra* note 32, at 215 (discussing the Noyes Foundation’s use of social and environmental screens representing its charitable values, using shareholder activism, and allocating 5% of its assets for capital investments in businesses that directly further its goals).

59. *Id.* at 217.

60. RESTATEMENT (THIRD) OF TRUSTS: P.I.R. § 227 (AM. LAW INST. 1992) (“[S]ocial considerations may be taken into account in investing the funds of charitable trusts to the extent the charitable purposes would justify an expenditure of trust funds for the social issue or cause in question or to the extent the investment decision can be justified on grounds of advancing, financially or operationally, a charitable activity conducted by the trust.”).

61. Brody, *supra* note 55, at 643 (“What the trust approach should not suggest, though, is that general societal interests, or charitable goals extraneous to the charity, override the fiduciaries’ good faith interpretation of the charity’s [SIC] mission.”).

The majority of states have adopted statutes based on the Uniform Prudent Management of Institutional Funds Act⁶² (UPMIFA).⁶³ UPMIFA sets the standard of conduct for directors of charitable corporations and for trustees of charitable trusts where the trustee is a charity.⁶⁴ Under UPMIFA, directors must take under consideration the charitable purposes of the fund, comply with a duty of loyalty, and act “in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.”⁶⁵ Investment costs can be incurred “only . . . [when] appropriate and reasonable.”⁶⁶ The act also emphasizes that investment decisions must be made in relation to the overall resources of the institution and its charitable purposes, rather than in isolation.⁶⁷ Other charitable trusts fall under the purview of the Uniform Prudent Investor Act (UPIA), which applies similar principles.⁶⁸

For private foundations, the corporate director standard applies.⁶⁹ Foundations must comply with three types of authorities when making investment decisions: (1) the written intent of the donor, (2) federal tax law, and (3) state laws regarding fiduciary duty.⁷⁰ Investing based on social missions rather than solely for financial returns is always allowed if the donor has stated that directors and trustees may take the foundation’s charitable mission into account when making investment decisions or that the foundation’s assets need not be preserved permanently.⁷¹ Additionally, under Section 4944 of the Internal Revenue Code, “jeopardy investments” that are found to be overly risky are not al-

62. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT (UNIF. LAW COMM’N 2006).

63. *Legislative Enactment Status, Prudent Management of Institutional Funds Act*, UNIF. LAW COMM’N, <http://uniformlaws.org/LegislativeMap.aspx?title=Prudent%20Management%20of%20Institutional%20Funds%20Act> [http://perma.cc/JMF7-QGSW] (last visited Nov. 28, 2015).

64. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 2 cmt. 4 (UNIF. LAW COMM’N 2006).

65. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3 (UNIF. LAW COMM’N 2006).

66. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3(e)(1) (UNIF. LAW COMM’N 2006).

67. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3(e)(1) (UNIF. LAW COMM’N 1994).

68. *See* UNIF. PRUDENT INV’R ACT § 2 (UNIF. LAW COMM’N 2006).

69. Heyns, *supra* note 30, at 48–49.

70. Mark Kramer & Anne Stetson, A BRIEF GUIDE TO THE LAW OF MISSION INVESTING FOR U.S. FOUNDATIONS 1 (2008), http://www.issueelab.org/click/download1/brief_guide_to_the_law_of_mission_investing_for_us_foundations.

71. *Id.* at 4.

lowed.⁷² Charitable trust and nonprofit corporation laws explicitly authorize consideration of the charitable purpose of the foundation when making investment decisions.⁷³

2. *Public Pension Funds*

Public pension funds are usually subject to state law, and often common law rules for trusts apply.⁷⁴ Most states have adopted UPIA to govern public pension funds, which uses the modern prudent investor rule.⁷⁵ They are not subject to ERISA.⁷⁶ Since pension funds involve the management of money to insure retirement income for the elderly, they might be even more carefully scrutinized if sacrificing returns for social impact. The case law supports the view that socially responsible investing is permissible.⁷⁷ It is best if the pension fund has an explicit mandate allowing the consideration of social factors.⁷⁸ However, even without this, social investing is usually permissible if:

the SRI policy is not predicted to unduly lower the expected return of the pension plan's assets; there is sufficient portfolio diversification; trustees have taken proper investment advice and have consulted with their fund membership; and, the policy can be implemented without burdensome and costly administrative procedures.⁷⁹

C. DIVESTMENT'S CONSISTENCY WITH FIDUCIARY DUTY

The Restatement (Third) of Trusts has defined the duty of prudence as a duty to:

invest and manage the funds of the trust as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the trust. This standard requires the exercise of reasonable care, skill, and

72. *Id.* at 7.

73. *Id.* at 13.

74. Heyns, *supra* note 30, at 51.

75. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 102.

76. *Id.*

77. Richardson, *supra* note 31, at 185.

78. *Id.*

79. *Id.*

caution, and is to be applied to investments not in isolation but in the context of the trust portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust. In making and implementing investment decisions, the trustee has a duty to diversify the investments of the trust unless, under the circumstances, it is prudent not to do so. . . .⁸⁰

UPIA, which UPMIFA tracks, follows the approach of the Restatement's prudent investor rule.⁸¹ The American Law Institute's (ALI) description of the prudent investor rule embraces modern portfolio theory, which looks at the portfolio as a whole rather than any particular investment decision in isolation.⁸² Modern portfolio theory is more flexible than historical fiduciary standards.⁸³ Thus, a single decision to divest from an otherwise high-performing fossil fuel stock, or investing in a riskier socially-beneficial stock, may not be seen as a breach of fiduciary duty.

However, divestment raises red flags in regards to the duty to diversify.⁸⁴ Some argue that social investing can result in under-diversification that increases risks and costs not compensated for by gains beneficiaries receive as a result of the social investment.⁸⁵ The Restatement allows for an exception to diversification if it is not prudent to do so, which may hold true for investing

80. RESTATEMENT (THIRD) OF TRUSTS § 90 (2007).

81. Its main objectives are setting the standard of prudence in the context of the portfolio rather than in isolation; placing central consideration on the tradeoff between risk and return; removing all categorical restrictions on types of investments; requiring diversification; and permitting delegation. UNIF. PRUDENT INV'R ACT prefatory note (UNIF. LAW COMM'N 2006).

82. See *id.*; Robert J. Aalberts & Percy S. Poon, *The New Prudent Investor Rule and the Modern Portfolio Theory: A New Direction for Fiduciaries*, 34 AM. BUS. L.J. 39, 48–49 (1996). See also FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 8.

83. Historical standards included those focusing on the performance of individual securities, requiring the use of “legal lists,” or requiring investment only in government-backed securities. Aalberts & Poon, *supra* note 82, at 48–50.

84. For a discussion on the duty to diversify, see John H. Langbein, *The Uniform Prudent Investor Act and the Future of Trust Investing*, 81 IOWA L. REV. 641, 646–49 (1996); see also Aalberts & Poon, *supra* note 82, at 57.

85. John Langbein & Richard Posner, *Social Investing and the Law of Trusts*, 79 MICH. L. REV. 72, 88–89 (1980); see also, Richardson, *supra* note 31, at 165 (“[E]nvironmental and social investment screens that constrict investment portfolios by excluding specific companies or economic sectors hamper true diversification. Also, diverse portfolios can lead to smaller holdings in any particular investment, thereby reducing trustees’ influence in individual companies.”) (footnotes omitted).

in the fossil fuel sector.⁸⁶ Additionally, in some cases the duty to diversify could support a decision to divest from some fossil fuel stocks and diversify stock holdings in the energy sector by investing in renewables.⁸⁷

Another potential obstacle to divestment arises under the duty of loyalty, which states that “[unless] otherwise provided in the terms of the trust, a trustee has a duty to administer the trust solely in the interest of the beneficiaries, or solely in furtherance of its charitable purpose.”⁸⁸ Further, “the trustee has a duty . . . not to be influenced by the interest of any third person or by motives other than the accomplishment of the purposes of the trust.”⁸⁹ Investing based on climate change might be impermissible because it is outside the scope of the purposes of the trust. Given the wide-ranging physical, social, and economic havoc that climate change will cause, it may be possible to argue that minimizing climate risk *is* related to the purposes of the trust and in the beneficiaries’ best interest. The answer also depends on the interpretation of the “interest” or “benefit” the fiduciary must prioritize for the beneficiary.⁹⁰ If the purpose of the fund is purely to generate financial returns, such as a pension fund, then the “benefit” the trustee is allowed to consider will likely be more strictly construed as only financial returns.⁹¹ Nevertheless, there is some

86. RESTATEMENT (THIRD) OF TRUSTS § 90(b) (2007) (“In making and implementing investment decisions, the trustee has a duty to diversify the investments of the trust unless, under the circumstances, it is prudent not to do so.”).

87. Benjamin J. Richardson, *supra* note 31 at 166.

88. RESTATEMENT (THIRD) OF TRUSTS § 78(1) (2007). *See also*, Sandberg, *supra* note 35, at 146. (“According to the classic and oft-cited commentary of the Chicago law professors Langbein and Posner, e.g., ‘[t]he duty of prudent investing . . . reinforces the duty of loyalty in forbidding the trustee to invest for any other object than the highest return consistent with the preferred level of portfolio risk’ and, were fiduciaries to take ESG considerations into account, ‘both the duty of loyalty and the prudent man rule would be violated.’”) (citation omitted). *See, e.g.*, Robert H. Jerry & O. Maurice Joy, *Social Investing and Lessons from South Africa Divestment: Rethinking the Limitations on Fiduciary Discretion*, 66 OR. L. REV. 685, 699 (1987) (“The proper balance of return and risk depends on many circumstances. Nevertheless, it is widely understood, despite some opinions to the contrary, that achieving the maximum rate of return and avoiding undue risk are the sole and exclusive objectives of the trustee.”) (footnotes omitted).

89. RESTATEMENT (THIRD) OF TRUSTS: P.I.R. § 170 cmt. q (1992). This duty has been read to prohibit a fiduciary from making an investment decision for their own benefit or for the benefit of third parties. Langbein & Posner, *supra* note 85, at 97; *see also* RESTATEMENT (THIRD) OF TRUSTS § 90 cmt. c (2007) (“The strict duty of loyalty . . . [prohibits] investing in a manner that is intended to serve interests other than those of the beneficiaries or the purposes of the settlor.”) (citation omitted).

90. Richardson, *supra* note 31, at 161.

91. *Id.*

discussion about whether the “benefits” considered can be non-financial benefits.⁹² For example, one commentator has interpreted Judge Cardozo’s famous words about holding a trustee to a higher standard than the “morals of the marketplace” as meaning a trustee should consider non-financial factors that affect the beneficiaries but may carry no price in the marketplace.⁹³ In that case, it is hard to argue there is a class of beneficiaries that is not benefited by divestment. Charities that are oriented towards a particular mission may make investment decisions based on that mission.⁹⁴ It has also been argued that fiduciaries in all cases should be allowed to consider non-financial factors with the beneficiaries’ consent.⁹⁵

Finally, under the duty of impartiality, the trustee has a duty to “act impartially and with due regard for the diverse beneficial

92. See, e.g., Solomon & Coe, *supra* note 32, at 220 (“Although the trust portfolio cannot be a means of expressing a trustee’s own social viewpoints, according to the Restatement, she is entitled to consider an investment’s social impact if such is appropriate to the purposes of the trust. The Restatement concludes: ‘[I]nvestment judgments may be affected by the fact that a special type of trust is involved, such as . . . charitable trusts.’”) (footnotes omitted). See also Richardson, *supra* note 31, at 161 (“If the trust is established to further some ethical, social, or charitable goal connected with broader society, then fiduciaries should act in accordance with those benefits.”); Adam Kanzer, *Divesting is an Exercise in Real Fiduciary Care*, PENSIONS & INV. (Feb. 18, 2013), <http://www.pionline.com/article/20130218/PRINT/302189995/divesting-is-an-exercise-in-real-fiduciary-care> [<http://perma.cc/L7BS-FLZC>] (“Newtown presents a very concrete example of what a violation of the duty of loyalty looks like. If you use my money to make a weapon that kills my child, don’t tell me that in 20 years I’ll retire with more money as a result. If you claim that decision was made in my best interest, you have no right to call yourself a fiduciary.”).

93. Kanzer, *supra* note 92 (“In the marketplace, everything has a price. The market has no use for irreplaceable things of infinite value. As a result, finance lacks clear imperatives to maximize life and the priceless things that sustain it, such as clean air and water. Finance knows no imperative to safeguard children. Fiduciaries, however, can check the more damaging aspects of finance through the process of prudent decision-making in conformance with a duty of loyalty — another priceless thing. ‘Price’ is not a fiduciary’s sole concern. If fiduciary duty meant ‘maximize returns,’ we’d have no need for fiduciary duty at all. We would merely need to set the incentives right and guard against embezzlement.”).

94. RESTATEMENT (THIRD) OF TRUSTS: P.I.R. § 227 cmt. c (1992) (“[S]ocial considerations may be taken into account in investing the funds of charitable trusts to the extent the charitable purposes would justify an expenditure of trust funds for the social issue or cause in question or to the extent the investment decision can be justified on grounds of advancing, financially or operationally, a charitable activity conducted by the trust.”) (citation omitted).

95. See, e.g., FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 12 (“Courts in the UK have recognised that trusts such as charities are entitled to exclude investments that conflict with their values and that the concept of beneficiaries’ ‘best interests’ under a general pension trust may extend beyond their financial interests to include their ‘views on moral and social matters’. In a similar way, US law permits investments to be excluded where the beneficiaries so consent.”) (footnote omitted).

interests created by the terms of the trust” and to “invest and administer the trust . . . that the trust estate will produce income that is reasonably appropriate to . . . the diverse present and future interests of its beneficiaries.”⁹⁶ Thus, the trustee must administer funds to protect all diverse beneficiaries and their interests equitably.⁹⁷ One can argue that fossil fuel investments impermissibly favor current beneficiaries at the expense of future beneficiaries who will suffer the severest effects of climate change, and thus breach this duty.

In the most obvious case, taking climate change factors into account for investment decisions is permissible when the environmental factors have a material bearing on financial returns in the short or long term.⁹⁸ However, two landmark cases suggest that there are other instances when non-financial factors can and should play a role in institutional investment decisions. In the case *Withers v. Teachers Retirement System*, trustees were able to buy \$860 million worth of highly speculative and risky city bonds, which had no promise of return, to prevent the city from going bankrupt; this occurred because of the relationship between the city and the fund where the city was the main contributor to the fund.⁹⁹ In *Board of Trustees of Employee Retirement System of*

96. RESTATEMENT (THIRD) OF TRUSTS § 79 (2007).

97. See FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 113 (“[A]n important consideration for investment decision-makers is the duty of impartiality between different beneficiaries, especially as it applies to different classes of beneficiaries over time. There is an argument, recognized in US case law, that this duty incorporates aspects of inter-generational fairness. . . . [A] Federal District Court held that a pension fund must be managed with a view to meeting future as well as present obligations.”) (footnotes omitted).

98. Richardson, *supra* note 31, at 188–89. For example, trustees could believe that divestment is in the best long-term interest of the beneficiary. *Divestment - Legality of Divestment Statutes - Court Upholds City Divestment Statutes Against Federal and State Constitutional Challenges. - Board of Trustees of the Employees' Retirement System v. Mayor of Baltimore City*, 317 Md. 72, 562 A.2d 720 (1989), 103 HARV. L. REV. 817, 819 (1990). It might also be permissible when such consideration has *no* bearing on financial returns or risk. See Jerry & Joy, *supra* note 88, at 704 (“If . . . social investing does not impair the interests of trust beneficiaries by either reducing the rate of return or increasing the risk of loss of the trust’s corpus, no justification exists for interpreting the duty of loyalty as absolutely proscribing a trustee from taking political and social values into account in investment decision making.”).

99. *Withers v. Teachers' Ret. Sys. of City of N.Y.*, 447 F. Supp. 1248 (S.D.N.Y. 1978), *aff'd mem.*, 595 F.2d 1210 (2d Cir. 1979). *But see* 1982 Idaho Op. Att’y Gen. 82 (1982) (“[N]either the protection of the jobs of the City’s teachers nor the general public welfare were factors which motivated the trustees in their investment decision. The extension of aid to the City was simply a means — the only means in their assessment — to the legitimate end of preventing the exhaustion of the assets of the [Teachers’ Retirement System] in the interest of all the beneficiaries.”) (quoting *Withers*, 447 F. Supp. at 1256, 1259).

Baltimore (City) v. Baltimore (City),¹⁰⁰ the court upheld city ordinances requiring four municipal pension funds to divest from companies engaged in business in South Africa and ruled that “if . . . social investment yields economically competitive returns at a comparable level of risk, the investment should not be deemed imprudent.”¹⁰¹ The statutes did not limit the investment universe to the extent that it was impossible for the trustees to make prudent investments and considering the social implications of an investment was not a breach of the duty of loyalty if “the costs of considering such consequences are *de minimis*.”¹⁰² The court stated that, “a trustee’s duty is not necessarily to maximize the return on investments but rather to secure a ‘just’ or ‘reasonable’ return while avoiding undue risk.”¹⁰³ In October 2015, a Department of Labor Interpretive Bulletin, clarifying the scope of ERISA (the federal statute regulating private pension funds), also stated that fiduciaries may consider collateral social benefits to choose an investment over another with similar risk-return characteristics.¹⁰⁴

In 2005, the United Nations Environment Programme’s Finance Initiative (UNEP FI) released a landmark report by law firm Freshfields Bruckhaus Deringer.¹⁰⁵ The report, commonly referred to as the Freshfields Report, found that fiduciary duties were compatible with social investing.¹⁰⁶ The report and its conclusion have been widely accepted and cited by social investing advocates.¹⁰⁷ It specified that when the primary purpose of the

100. 562 A.2d 720, 737 (Md. Ct. App. 1989), *cert. denied*, 493 U.S. 1093 (1990).

101. *Id.*

102. *Id.* at 738.

103. *Id.* at 737 (“As one commentator stated, a ‘trustee is under no duty to open a brothel in Nevada, where prostitution is legal, in order to maximize return to beneficiaries.’ . . . [If] social investment yields economically competitive returns at a comparable level of risk, the investment should not be deemed imprudent.”) (citation omitted).

104. Interpretive Bulletin Relating to the Fiduciary Standard Under ERISA in Considering Economically Targeted Investments, 29 C.F.R. § 2509.2015-01 (2015); *Trustees Grapple with Socially Responsible Investing*, BERMAN DEVALERIO, <http://www.bermandevalerio.com/news/firm-newsletter/70-trustees-grapple-with-socially-responsible-investing> [<http://perma.cc/Q96U-BQ2S>]; Tom Perez, Remarks by U.S. Secretary of Labor Tom Perez Press Conference Announcing New ERISA Guidance On Economically Targeted Investments (Oct. 22, 2015), http://www.dol.gov/_sec/media/speeches/20151022_Perez.htm [<http://perma.cc/JBF8-BMTT>].

105. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34.

106. *Id.*

107. Sandberg, *supra* note 35, at 147 (“With regards to the legislative side, there is really no end to the praise given to the Freshfields report in Fiduciary II; it is called ‘a landmark report’ and ‘[t]he single most effective document for promoting the integration of environmental, social and governance (ESG) issues into institutional investment’ Fur-

fund was to produce financial returns, such as with most pension funds, this objective must override all others.¹⁰⁸ However, it also specified three distinct scenarios finding: (1) if the beneficiaries reach a consensus¹⁰⁹ that the fiduciary should consider ESG factors, the fiduciary *must* consider them, (2) if deciding between two otherwise equal¹¹⁰ investments the fiduciary *may* take into account ESG factors, and (3) if the ESG criteria are likely to have a material impact¹¹¹ on the financial performance, the fiduciary *must* consider them.¹¹² The last point weighs heavily in favor of climate consideration and divestment in light of arguments that climate change often is a financially material consideration.¹¹³

thermore, the Freshfields report's 'clear conclusion' is claimed to be 'routinely cited by practitioners, academics and opinion formers worldwide' and is suggested to, together with some other 'ground-breaking reports' from UNEP FI, have 'created a near universally accepted platform in support of ESG integration on which many other initiatives were able to build.'" (citations omitted).

108. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 12.

109. Joakim Sandberg, however, argues that there will rarely be an easy way to determine consensus. Sandberg, *supra* note 35, at 153, 155 ("[T]here is simply no such thing as what 'typical' social investors care about or want. Thus, the idea that there could be certain ESG areas where there was a consensus among social investors about what to do or think seems extremely farfetched. . . . While there indeed are some fairly robust social conventions on some of these issues — there are, for instance, multiple international treaties on environmental protection and labour standards signed by an impressive amount of nations — there simply is a vast range of important issues where there are no clear conventions or treaties at all.") (footnote omitted).

110. See also Solomon & Coe, *supra* note 32, at 221 ("Social and moral considerations may be taken into account, even though they may not take precedence over total return. As long as one investment would produce roughly the same financial result as another, the charitable trustee may consider social and moral factors in deciding between the two.") (footnote omitted). Joakim Sandberg also argues that since, when comparing two assets, modern portfolio theory requires a complex analysis "not only of the expected return and variance of the two assets themselves, but also the covariance between those assets and the rest of the holdings within the portfolio," there will rarely be a situation where two assets are in all other respects equal. Sandberg, *supra* note 35, at 149.

111. Joakim Sandberg argues there are few instances where ESG factors will be material. Sandberg, *supra* note 35, at 150–51 ("Now curiously, the only real example of when ESG performance affects financial performance given in the Freshfields report is the case of climate change. . . . Similarly, none of the summaries published by UNEP FI itself have been able to show that there always — or even most often — is a connection between CSP and CFP over the long term; not even in the case of climate change.") (citation omitted).

112. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 14.

113. A CLIMATE FOR CHANGE: A TRUSTEE'S GUIDE TO UNDERSTANDING AND ADDRESSING CLIMATE RISK 19 (2005), http://www.iigcc.org/files/publication-files/A_climate_for_change_a_trustees_guide.pdf [<http://perma.cc/AWK5-EX6M>] ("The materiality of climate change as outlined in this document clearly shows that climate change risk could have the potential to impact a Fund's investments over the long term. In addition, we suspect climate change risk is neither fully known nor understood and that it is not yet properly managed by the various groups involved in the ongoing management of pension scheme assets."). *But see* ANNEX I — CRITIQUE OF THE CAMPAIGN FOR SUSTAINABILITY TO BECOME A FIDUCIARY CONSIDERATION 3, SUSTAINABLE RESOURCE INVESTMENT (Oct. 2013),

Thus, there is support for the view that divestment is in many instances compatible with meeting fiduciary duties.¹¹⁴

III. THE DIVESTMENT DEBATE

This Part will summarize the main arguments on both sides of the debate over divestment. In particular, arguments on the prudence, effectiveness, and challenges in implementing a divestment strategy play an important role in determining whether or not divestment is compatible with fiduciary duties.

The fossil fuel divestment movement aims to damage the reputation of fossil fuel businesses and put social and political pressure on them to leave their carbon reserves untouched.¹¹⁵ Divestment activists hope to send an important signal to politicians and create indirect impacts such as increased legislation for a transition to renewables from fossil fuels.¹¹⁶ This Part will discuss the controversy over divestment as a strategy, which centers on: (1) whether divestment is successful in achieving its goals, (2) whether shareholder advocacy is a better avenue for change, (3) the impacts on portfolio returns and risk, and (4) how to overcome the challenges in implementing a divestment strategy.

<http://www.srinvestment.net/wp-content/uploads/2014/02/Fiduciary-Duty-Mercer-Report-3.pdf> [<http://perma.cc/C92D-TUNN>] (arguing that climate change impacts are “inherently difficult to quantify” and that the fiduciary has discretion to determine whether climate change constitutes a risk and how to deal with the risk).

114. Solomon & Coe, *supra* note 32, at 220 (noting that “[o]ne of the most respected legal commentators on trusts and trust investments, Professor Austin Wakeman Scott” believed trustees could take into account societal welfare in investment decisions) (footnotes omitted).

115. See, e.g., *Why Divestment*, DIVEST HARVARD, <http://divestharvard.com/why-divestment> [<http://perma.cc/DJ9Y-UUCN>]; Marc Gunther, *Why the Fossil Fuel Divestment Movement May Ultimately Win*, YALE ENVIRONMENT 360 (July 27, 2015), http://e360.yale.edu/feature/why_the_fossil_fuel_divestment_movement_may_ultimately_win/2898 [<http://perma.cc/KZ2K-HEN8>] (“The divestment campaign aims, first, to build a bigger and stronger climate movement, and, second, to put the fossil fuel industry on the defensive by attacking its reputation and challenging the long-term viability of its business in a climate-constrained world”).

116. Atif Ansar et al., STRANDED ASSETS AND THE FOSSIL FUEL DIVESTMENT CAMPAIGN: WHAT DOES DIVESTMENT MEAN FOR THE VALUATION OF FOSSIL FUEL ASSETS?, 9–15 (2013), <http://www.smithschool.ox.ac.uk/research-programmes/stranded-assets/SAP-divestment-report-final.pdf> [<http://perma.cc/9AL6-DENM>].

A. EFFECTIVENESS OF THE DIVESTMENT CAMPAIGN

To assess whether the divestment movement can successfully help mitigate climate change, one must differentiate between the potential impacts that selling stock in a fossil fuel company can have. This Part will analyze not only whether the act of selling stock could lower stock prices to a degree that threatens the existence of fossil fuel companies, but also whether the campaign can succeed by triggering indirect impacts. Even if it has no direct financial impact, the mass sale of stock might send political and social signals that in turn lead to other political action and policies that put fossil fuels out of business.

First, those who argue that divestment is not an effective strategy claim that previous movements have demonstrated that shareholder divestment is not effective in exerting enough financial pressure on companies to put them out of business.¹¹⁷ A study on the impacts of the U.S. movement to divest from businesses operating in South Africa during the Apartheid found that anti-apartheid legislative and shareholder boycotts had no effect on the valuation of the banks and corporations operating in South Africa or on South African markets.¹¹⁸ This could suggest that the firms being divested from circumvented sanctions and continued to operate, or that the demand for stocks was elastic enough that shareholdings were merely redistributed from socially active investors to others.¹¹⁹

A report by the Stranded Asset Programme at Oxford University also found divestment unlikely to affect stock prices in the long term, since even were the movement successful in achieving a short-term decrease in stock price, neutral investors could research long-term earnings potential and choose to invest.¹²⁰ Previous divestment movements failed to harm the future net cash flows of the businesses they targeted and thus failed to impact their long-term earnings potential.¹²¹ The global market value of stock and bond holdings is \$212 trillion¹²² and combined university and public funds hold a total of \$12 trillion of that amount.¹²³

117. See, e.g., Teoh et al., *supra* note 22, at 62, 68–69.

118. *Id.* at 79–83.

119. *Id.* at 37.

120. Ansar et al., *supra* note 116, at 2, 30.

121. *Id.* at 60.

122. *Id.* at 54.

123. *Id.* at 57.

However, in previous divestment movements only a small portion of possible divestible funds actually divested.¹²⁴ As a result, the report concluded that there is likely to be only a negligible direct impact on the equity valuations of fossil fuel companies.¹²⁵ Withdrawal of debt financing from large banks would also not have a major impact on companies, because other sources of debt finance would arise as substitutes, unless borrowers were situated in countries with low financial depth.¹²⁶ For all major fossil fuel companies, however, the ability to undertake large capital expenditure projects in difficult technical or political environments would be impaired by divestment “due to a higher hurdle rate and reduced availability of debt financing.”¹²⁷ The report suggested that the best chance of a divestment movement depressing stock prices permanently would be if it triggered a change in market norms that restricted previously available funding.¹²⁸ For example, the report stated, “[c]ampaigners can . . . target large lending banks and pressure them to commit to a set of principles . . . that create obstacles for the debt financing of marginal fossil fuel projects.”¹²⁹ Finally, though oil and gas companies make up about 11% of the S&P 500, have a broad range of shareholders, and are highly liquid since they are publicly listed,¹³⁰ the coal mining industry is “much smaller and fragmented.”¹³¹ Thus, the coal industry is more likely to be directly impacted by divestment and less access to debt financing.¹³²

Supporters of divestment stress that the non-financial pressure created by divestment does achieve the aims of the movement.¹³³ For example, it has been argued that “pressure from

124. *Id.* at 60.

125. *Id.* at 61.

126. *Id.* at 33.

127. *Id.* at 62.

128. *Id.* at 32.

129. *Id.* at 18.

130. *Id.* at 53.

131. *Id.* at 54.

132. *Id.* at 63.

133. David Keith, *The Fossil Fuel Divestment Campaign Can Succeed Where Politics Failed*, BOSTON REV. (Dec. 23, 2006), <http://bostonreview.net/blog/david-keith-fossil-fuel-university-endowment-divestment> [<http://perma.cc/L4HH-J8PA>] (“My hope is that the divestment movement can, with other grassroots efforts, grow into a social movement capable of mobilizing a small but active minority to push climate policy at the ballot box.”). In fact, activists frequently state that they have no explicit aim to impact stock price. See, e.g., Francesca Rheannon, *Fossil Fuel Divestment as a Lever for Change: A Conversation with Bob Massie*, CSWWIRE TALKBACK (June 6, 2014), <http://www.csrwire.com/blog/posts/1377-fossil-fuel-divestment-as-a-lever-for-change-a-conversation-with-bob-massie>

divestiture created a political climate in which House and Senate Republicans and Democrats could join to pass legislation imposing sanctions on South Africa and then override President Ronald Reagan's veto of the bill."¹³⁴ Additionally, between 50% to 70% of a large company's value is considered intangible, and thus threatening the company's reputation can induce it to act more ethically in order to decrease these "reputational risks."¹³⁵ Indeed, the Stranded Assets Programme report found that stigmatizing the fossil fuel industry could lead to negative social and economic outcomes for it.¹³⁶

For divestment to impact the value of the targeted industry in the long term, neutral equity or debt investors would have to lower their expectations of the industry's net cash flows.¹³⁷ Stigmatization could achieve this by adding to the uncertainty surrounding the future of the industry.¹³⁸ Almost all previous divestment movements studied, including Darfur, Tobacco, and South Africa were successful in passing restrictive legislation.¹³⁹ Though the study found it unlikely the campaign would succeed in banning fossil fuel drilling entirely, it found that implementation of a carbon tax could have a significant stigmatization impact.¹⁴⁰ However, companies will also fight the stigma, diversify, and modify their behavior, and thus stigma is unlikely to threaten the survival of the firm directly without the broader political action the movement calls for.¹⁴¹

[<http://perma.cc/G4HS-XNRQ>] (Bob Massie states: "I have been studying [divestment] for more than 20 years and I have never encountered any advocate for divestment who believes it will affect the stock price.").

134. Imogen Rose-Smith, *Climate Change and the Fossil Fuel Divesture Movement*, INSTITUTIONAL INVESTOR (Apr. 15, 2014), <http://www.institutionalinvestor.com/Article/3330970/Investors-Endowments-and-Foundations/Climate-Change-and-the-Fossil-Fuel-Divestiture-Movement.html?ArticleId=3330970&single=true&login=1&eventlogin=Login&eid=E017&actionname=login#.VLayqSchyVC> [<http://perma.cc/6XPF-57NP>].

135. Benjamin J. Richardson, *Keeping Ethical Investment Ethical: Regulatory Issues for Investing for Sustainability*, *Journal of Business Ethics*, 87 J. BUS. ETHICS 555, 557 (2009).

136. Ansar et al., *supra* note 116, at 38.

137. *Id.*

138. *Id.* at 65.

139. *Id.* at 66.

140. *Id.* at 66–67.

141. *Id.* at 68–69.

B. SHAREHOLDER ADVOCACY

Additionally, there are those who argue that remaining a shareholder and using voting power and shareholder activism is a more practical and effective strategy to pressure fossil fuel companies to engage in more sustainable operations.¹⁴² For example, instead of divesting from coal companies, Stanford might have done better “buy[ing] up lots of energy stocks, concentrating its holdings and then using that position to press corporate boards to make changes.”¹⁴³ Yale University, after being petitioned by students, declined to divest but instead had its chief investment officer write a letter to its fund managers asking them to “discuss with company managements the financial risks of climate change and the financial implications of current and prospective government policies to reduce greenhouse gas emissions.”¹⁴⁴ There are two ways in which shareholders can engage with firms outside of divestment or employing screens: (1) through active filing of shareholder proposals¹⁴⁵ and (2) through forming joint groups to push for reforms and lobbying for regulatory changes.¹⁴⁶ Shareholders can at minimum be engaged as socially responsible owners through voting their proxies on social and environmental issues in an informed manner along a set of guidelines.¹⁴⁷

The Carbon Disclosure Project requests that corporations disclose information on their greenhouse gas emissions, their energy

142. Jeffrey Sachs & Lisa Sachs, *The Responsible Investor's Guide to Climate Change*, PROJECT SYNDICATE, <http://www.project-syndicate.org/commentary/fossil-fuels-divestment-renewables-by-jeffrey-d-sachs-and-lisa-sachs-2015-01#A8JATRhJqFWsfDy4.99> [http://perma.cc/2Y29-V7TC].

Jeffrey Sachs and Lisa Sachs suggest that shareholders ask whether a company has “subscribed to the internationally agreed goal of limiting global warming to 2° Celsius above pre-industrial levels” and corresponding emissions limits, whether the company will “pledge to leave business groups that lobby against effective climate policies,” whether the company will “agree to end any exploration and development of unconventional reserves,” and whether the company can show that it “remains a good investment, despite the transition to low-carbon energy sources and technologies.” They suggest that shareholders engage with companies that seem open to climate action and divest from those that deny climate change.

143. Welch, *supra* note 39.

144. Geraldine Fabrikant, *Yale Fund Takes Aim at Climate Change*, N.Y. TIMES (Sept. 7, 2014), http://www.nytimes.com/2014/09/08/business/yale-fund-takes-aim-at-climate-change.html?_r=0 [http://perma.cc/A85N-UFRT].

145. David Hess, *Public Pensions and the Promise of Shareholder Activism for the Next Frontier of Corporate Governance: Sustainable Economic Development*, ROSS SCH. OF BUS. 16 (Working Paper Series, Paper No. 1080, 2007), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=988792 [http://perma.cc/7GHT-N922].

146. *Id.* at 17.

147. *Id.* at 20.

use, and the risks and opportunities climate change poses for them on behalf of 822 institutional investors with \$95 trillion in assets.¹⁴⁸ The information that results from the disclosure can then be used by institutions to engage directly with the corporation and to better analyze the prudence of the investment.¹⁴⁹ Another influential group is the Investor Network on Climate Risk, a network of 110 institutional investors with more than \$13 trillion in assets with a “mission . . . to mobilize investor leaders to address climate and other key sustainability risks, while building low-carbon investment opportunities.”¹⁵⁰ Collaboration through such groups allows institutions to avoid duplicating costs, learn from one another’s experiences, and increase their influence.¹⁵¹

There is a history of shareholders mobilizing to pressure firms to change their social and political actions.¹⁵² Shareholder resolutions are one tool used by large, powerful shareholders to influence firm behavior.¹⁵³ They send a public message to the firm and non-shareholders who may still have a stake in the cause and thus serve as a “long-term change tactic.” While winning the vote is an uphill battle, the main goal is to open a dialogue and create transparency, supported with threats of divestment.¹⁵⁴ One study found that firms with climate change concerns or no climate change record were willing to engage with shareholder resolutions, and thus shareholder resolutions help monitor firms

148. *Climate Change Program*, CDP, <https://www.cdp.net/en-US/Programmes/Pages/CDP-Investors.aspx> [<http://perma.cc/ERQ2-8AR9>] (last visited Nov. 28, 2015).

149. Hess, *supra* note 145, at 36.

150. Investor Network on Climate Risk, *2012 Investor Action Plan on Climate Change Risks & Opportunities*, CERES, <http://www.ceres.org/investor-network/investor-summit/summit-files/2012-investor-action-plan> [<http://perma.cc/4PG4-KSY2>]. According to their 2012 Investor Action Plan on Climate Change Risks & Opportunities, main strategies include: 1. Incorporating climate change risks into their investment process and portfolios; 2. Integrating climate change risks into their external manager procurement and monitoring; 3. Investing in low-carbon solutions; 4. Integrating energy efficiency into the decision-making process; 5. Taking into consideration water risk posed by climate change into portfolios; 6. Encouraging companies to improve disclosure and governance and to engage with companies as shareholders that do not; 7. Supporting international, national, sector-specific, and sub-national policy action; and 8. Encouraging the SEC to require more climate change disclosure from companies. *Id.*

151. Hess, *supra* note 145, at 36.

152. Cynthia E. Clark & Elise Perrault Crawford, *Influencing Climate Change Policy: The Effect of Shareholder Pressure and Firm Environmental Performance*, 51 BUS. AND SOC’Y 148, 152 (2012), <http://bas.sagepub.com/content/51/1/148.abstract> [perma.cc/3TF2-XAUK].

153. *Id.* at 153.

154. *Id.* at 153–54.

and can increase transparency.¹⁵⁵ There are many examples of shareholder activism leading to changes in company policies and actions.¹⁵⁶

Proponents of this strategy argue that divestment turns over shares and voting power from socially activist investors who are willing to engage firms to those who are disinterested and who will not attempt to change firm behavior.¹⁵⁷ However, shareholder activism requires time to monitor and engage with investments, which can be costly, especially given the large number of equity holdings institutional investors usually have.¹⁵⁸ Supporters of divestment argue that only divestment creates the stigma necessary to revolutionize the system, and, furthermore, shareholder activism is not an effective tool to address climate change.¹⁵⁹ Shareholder activism has principally pursued firm disclosure, but addressing climate change will require fossil fuel companies to change their fundamental business plan. Under Security Exchange Commission (SEC) rules, however, shareholders cannot submit resolutions asking companies to forgo profits by not exploiting their fossil fuel assets.¹⁶⁰ Additionally, one fos-

155. *Id.* at 170.

156. Roy A. Schotland, *Divergent Investing for Pension Funds*, 36 FIN. ANALYSTS J. 29, 37 (1980).

157. Wisor, *supra* note 41. See also Schotland, *supra* note 156, at 37 (“Management need not adjust its policies to avoid a raid prompted by a desire to convert the company into a socially responsible one-social irresponsibility may well have caused higher profits and stock prices, hardly an atmosphere conducive to a raid . . . [S]elling stock in a company that discriminates against blacks might be good for the spirit, but it does not directly affect the company; rather it would place the stock in the hands of persons who either favor the policy, or at least are indifferent to it.”).

158. Schotland, *supra* note 156.

159. Cutler J. Cleveland & Richard Reibstein, *The Path to Fossil Fuel Divestment for Universities: Climate Responsible Investment* 41 (2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2565941 [<http://perma.cc/5SE7-ZQCV>] (“Asking the oil and coal companies to ‘green’ their supply chain will not solve the problem. We need to stop producing oil and coal. Shareholder advocacy, if it is to contribute to solutions, must be used to influence a company to transition to new business activities.”).

160. SEC regulations allow companies to exclude proposals “deal[ing] with a matter relating to the company’s ordinary business operations.” Shareholder Proposals, 17 C.F.R. 240.14a-8(i)(7). As Swarthmore Mountain Justice explains, “Shareholder resolutions are useful in cases where a company can reform its practices, principles, or procedures, but are virtually impossible when the reform undermines the economic purpose of the company in question. . . . Companies can (according to the US SEC), and frequently do, throw out shareholder resolutions that are ‘related to the company’s ordinary business operations.’” *Resources on Divestment*, SWARTHMORE MOUNTAIN JUSTICE, <http://swatmj.org/resources-on-divestment> [<http://perma.cc/EF6A-JJV7>]. See also *Debunking Myths about Fossil Fuel Divestment*, FOSSIL FREE, <http://gofossilfree.org/wp-content/uploads/2014/05/debunking-divestment-myths.pdf> [<http://perma.cc/T6PX-E66M>] (last visited Sept. 15, 2015).

oil corporation, Exxon Mobil, responded to shareholder requests for disclosure on their plan to manage climate change risks with two reports stating that (1) it did not think climate change or stranded assets (fossil fuel assets that cannot be utilized in order to prevent climate change) posed any threat and (2) that they were going to continue to search for and burn more oil and gas.¹⁶¹ This response displays the limits of shareholder engagement, after which the only action left to take is divestment.¹⁶²

C. DIVESTMENT'S IMPACT ON PORTFOLIO RISK AND RETURNS

Another controversy is whether divestment will increase risk and lower returns for funds. Since fiduciary duties usually require maximizing profits and minimizing risks to beneficiaries, determining divestment's actual impact on portfolio risks and returns plays an important role in deciding whether institutions can divest without breaching their duty. Those who claim divestment is too costly point to risks from decreased diversification and high transaction costs, including the brokerage fees to sell all current fossil fuel assets.¹⁶³ Some argue it is irresponsible for institutions such as pension funds to engage in social investing because it puts retirement security at risk if funds are not seeking only to maximize returns.¹⁶⁴ On the other hand, the "business case" for divestment has been picking up steam, and more and more supporters of divestment are arguing that it is the financially prudent decision to make.¹⁶⁵

Institutions fear divestment will hurt portfolio returns since stock in fossil fuel companies has historically been very high performing. A study sponsored by the American Petroleum Industry found that, over the last decade, U.S. colleges and universities saw the greatest returns in their portfolios from investments in

161. ExxonMobil, ENERGY AND CARBON — MANAGING THE RISKS, <http://cdn.exxonmobil.com/~media/global/files/energy-and-environment/report---energy-and-carbon---managing-the-risks.pdf>; Bill McKibben, *Exxon Mobil's Response to Climate Change is Consummate Arrogance*, GUARDIAN (Apr. 3 2014, 7:13 AM) <http://www.theguardian.com/environment/2014/apr/03/exxon-mobil-climate-change-oil-gas-fossil-fuels> [http://perma.cc/YC85-G2FN].

162. McKibben, *supra* note 161.

163. Heyns, *supra* note 30, at 37.

164. Schotland, *supra* note 156, at 34.

165. *See, e.g.*, Longstreth, *supra* note 43.

U.S. natural gas and oil companies.¹⁶⁶ From 2010–11, the study found that oil and natural gas company shares generated the highest returns of the year at 52.8 percent, compared to 19.2 percent for endowments overall and 30.7 percent for all U.S. equities.¹⁶⁷ A report by Bloomberg New Energy Finance also found, after analyzing seven alternative trillion-dollar sectors, that only shares in real estate firms have paid higher dividends in recent years than those in fossil fuel firms.¹⁶⁸

Investment decisions are normally made according to the prudent investor rule, which calls for maximizing expected returns and minimizing risk, and one method of minimizing risk is through diversification.¹⁶⁹ In fact, fiduciary duty, including the modern prudent investor rule, normally *requires* diversification.¹⁷⁰ Institutions fear that restricting the “investment universe” limits diversification opportunities.¹⁷¹ Harvard’s statement on divestment emphasized that “significantly constraining investment options risks significantly constraining investment returns . . . barring investments in a major, integral sector of the global economy would — especially for a large endowment reliant on sophisticated investment techniques, pooled funds, and broad diversification — come at a substantial economic cost.”¹⁷²

However, there have also been multiple studies showing that there is no significant impact on portfolio performance as a result of divesting.¹⁷³ A study analyzing portfolio risk when excluding all fossil fuel companies relative to a benchmark of the Russell

166. ROBERT J. SHAPIRO & NAM D. PHAM, THE FINANCIAL RETURNS FROM OIL AND NATURAL GAS COMPANY STOCKS HELD BY AMERICAN COLLEGE AND UNIVERSITY ENDOWMENTS (2012), *available at* <http://www.api.org/~media/files/news/2012/12-december/api-report-industry-returns-for-college-university-endowments.pdf> [<http://perma.cc/4FE7-CNTL>].

167. *Id.* at 18.

168. Simon Evans, *Why Fossil Fuel Divestment Won't be Easy*, CARBON BRIEF (Aug. 8, 2014, 3:45 PM), <http://www.carbonbrief.org/why-fossil-fuel-divestment-wont-be-easy/> [<http://perma.cc/Z4KF-DKG2>].

169. Heyns, *supra* note 30, at 38.

170. See RESTATEMENT (THIRD) OF TRUSTS § 90 (2007).

171. Alex Lenferna, *Fossil Fuel Divestment Report for the Seattle City Employees' Retirement System* 9 (Oct. 2014), https://www.academia.edu/8651774/Fossil_Fuel_Divestment_Report_for_the_Seattle_City_Employees_Retirement_System [<http://perma.cc/ZZ25-3DTS>].

172. Faust, *supra* note 38.

173. See, e.g., Jerry & Joy, *supra* note 88, at 727 (“Thus, the Grossman and Sharpe results refute the claim that South Africa-free stocks have been inferior performers compared to the rest of the market in recent years. More important, their results support the proposition that a South Africa-free portfolio can be managed to achieve competitive rates of return without unacceptable risk levels.”).

3000 showed that there *was* an increased portfolio risk, but it was of a nearly negligible value of 0.0101% with a theoretical return penalty of only 0.0034%.¹⁷⁴ Apex conducted a similar study analyzing the volatility¹⁷⁵ and tracking error¹⁷⁶ of fossil free portfolios.¹⁷⁷ The study examined four different investment strategies that screened out carbon at various levels and found that removing the fossil fuel sector entirely and replacing it with “fossil free” portfolios of energy efficiency, renewable energy, and other alternative energy stocks would improve the MSCI World Index, with a small positive impact on returns (0.5% annually) and only a modest increase in tracking error of 1.6% a year from 2006 to 2013.¹⁷⁸ Additionally, commentators have acknowledged that the modern prudent investor rule allows for flexibility.¹⁷⁹ One commentator noted that the Restatement (Third) of Trusts does not define to what extent the portfolio must be diversified, so the diversification strategy is left to the discretion of the fund manager.¹⁸⁰

There are also financial risks associated with not divesting from fossil fuel stocks. In 2010, the SEC published interpretive guidance acknowledging that the risk posed by climate change could be financially material enough to require disclosure.¹⁸¹ The guidance notes the following developments could significantly impact business and trigger disclosure requirements: climate-related legislation and regulation; international accords or trea-

174. Aperio Group, DO THE INVESTMENT MATH: BUILDING A CARBON FREE PORTFOLIO, https://gofossilfree.org/se/wp-content/uploads/sites/13/2014/07/building_a_carbon_free_portfolio.pdf [http://perma.cc/V9HS-VHQ5]. Aperio Group has also published an update finding a tracking error of only 0.77% when excluding fossil fuel companies from the Russell 3000. Aperio Group, BUILDING A CARBON-FREE EQUITY PORTFOLIO (2015), <https://www.aperiogroup.com/resources-insights/topic/carbon-divestment/building-carbon-free-equity-portfolio-updated> [http://perma.cc/AE7U-U5TF].

175. Volatility refers to how much a stock’s price varies over time.

176. Tracking error is a measure of the difference between a particular portfolio’s returns against the fund it is benchmarked against.

177. *Beyond Fossil Fuels: The Investment Case for Fossil Fuel Divestment*, IMPAX ASSET MGMT. 1, <http://www.impaxam.com/sites/default/files/20130704%20Impax%20White%20Paper%20fossil%20fuel%20divestment%20FINAL.pdf> [http://perma.cc/6NDQ-CJ5M].

178. *Id.* at 5.

179. Aalberts & Poon, *supra* note 82, at 49–50.

180. *Id.* at 51. *See also* Jerry & Joy, *supra* note 88, at 747 (analyzing the South African divestment movement’s effects on portfolio returns and risk: “[o]ur analysis shows that systematic exclusion of a large part of the investment universe *can* be accomplished without sacrificing return and without increasing risk.”).

181. SEC, Commission Guidance Regarding Disclosure Related to Climate Change, 75 Fed. Reg. 6290 (Feb. 8, 2010).

ties on climate change;¹⁸² business trends arising from legal, technical, and political developments that could, for example, decrease demand for certain products; and physical impacts of climate change that could affect business operations.¹⁸³

The United Nations Environment Programme report “Show Me the Money” analyzed the materiality of ESG factors to company profitability in eight industry sectors and found that:

- 1) ESG issues are material — there is robust evidence that ESG issues affect shareholder value in both the short and long term.
- 2) The impact of ESG issues on share price can be valued and quantified.
- 3) Key material ESG issues are becoming apparent, and their importance can vary between sectors.¹⁸⁴

Thus, as an independent review of the UNEP report found, a “clear case is emerging” for investors to consider environmental and climate change issues as material to their portfolio value.¹⁸⁵ The World Resources Institute and the UNEP FI have even released a comprehensive framework for investors to identify and

182. For example, the Paris Agreement adopted at the UNFCCC Conference of Parties in December 2015 may be one such treaty that could affect businesses. U.S. Secretary of State John Kerry stated that through the agreement “[w]e are sending literally a critical message to the global marketplace. Many of us here know that it won’t be governments that actually make the decision or find the product, the new technology, the saving grace of this challenge. . . . It will be business unleashed because of 186 nations saying to global business in one loud voice: We need to move in this direction. And that will move investment.” John Kerry, Remarks at COP21 Plenary (Dec. 12, 2015) (transcript available at <http://www.state.gov/secretary/remarks/2015/12/250584.htm> [<http://perma.cc/RRS9-UEYC>]).

183. Commission Guidance Regarding Disclosure Related to Climate Change, *supra* note 181. See also A CLIMATE FOR CHANGE: A TRUSTEE’S GUIDE TO UNDERSTANDING AND ADDRESSING CLIMATE RISK, *supra* note 113 (analyzing climate risks to businesses that could impact portfolio risks and returns).

184. UNEP FIN. INITIATIVE ASSET MGMT. WORKING GRP., SHOW ME THE MONEY: LINKING ENVIRONMENTAL, SOCIAL AND GOVERNANCE FACTORS TO COMPANY VALUE 11 (2006), http://www.unepfi.org/fileadmin/documents/show_me_the_money.pdf [<http://perma.cc/3JBS-DEEH>].

185. *Id.* at 53. See also Richardson, *supra* note 31, at 167–68 (refuting the idea that active consideration of ESG criteria is unnecessary because the market already reflects all material information in a company’s stock price because “sometimes there is a delay between a company’s financially relevant environmental record and the reaction of the ‘efficient market’ to that information” and, further, “investors who engage in corporate governance (e.g., filing shareholder resolutions and asking questions to company management) outperform their peers on measures such as return on investments”).

manage the climate risk in their portfolios, presenting divestment as a tool to avoid this risk.¹⁸⁶

One major potential risk is the carbon bubble — the term given to describe the concept of carbon asset risk.¹⁸⁷ This risk is that current fossil fuel reserves far exceed the quantity it would take to surpass a two degrees Celsius temperature increase, which is what nations have agreed to limit warming to.¹⁸⁸ Thus, companies currently hold more carbon assets than they can actually utilize or monetize, creating “stranded assets.”¹⁸⁹ Since fossil fuel companies’ valuation is based on their current assets and fossil fuel reserves, the argument is that they are currently vastly overvalued.¹⁹⁰ Because fossil fuel companies are also still expending resources searching for new fossil fuels, there could be over \$6 trillion wasted on new potentially stranded fossil fuels.¹⁹¹ By one calculation, the market value of current stranded assets is \$22 trillion.¹⁹² The reality of carbon asset risk depends on market efficiency; in an efficient market, the market would account for this risk in the stock price.¹⁹³ Unfortunately, fossil fuel companies’ stock prices are not currently capturing this risk.¹⁹⁴ Increasing developments in renewables also jeopardize the future monetization of fossil fuels.¹⁹⁵

186. WRI & UNEP FI, CARBON ASSET RISK: DISCUSSION FRAMEWORK (2015), <http://www.wri.org/publication/carbon-asset-risk-discussion-framework> [<https://perma.cc/RVT8-7J87>].

187. Lenferna, *supra* note 171, at 4.

188. *Id.* at 1.

189. *Id.* at 4.

190. *Id.*

191. *Id.*

192. *Id.* at 4–5.

193. Heyns, *supra* note 30, at 39.

194. CARBON TRACKER INITIATIVE, UNBURNABLE CARBON 28 (2011), <http://www.carbontracker.org/wp-content/uploads/2014/09/Unburnable-Carbon-Full-rev2-1.pdf> [<http://perma.cc/68BC-44MQ>] (“Our report shows that fossil fuels appear to be over-capitalised. The capital markets have financed future fossil fuel development based on a false assumption: that what the corporate sector have asked investors to finance can actually be burnt. We believe this poses a large and currently unappreciated risk for the capital markets.”). One of the problems implicated here is corporations not adequately disclosing their climate risk and thus obstructing the market from proper functioning. Clearly, work must be done to increase transparency of this risk to shareholders and the market. In 2014, Ceres published a report on S&P 500 companies and their compliance with SEC-required reporting on climate risks. It found “the vast majority of financial reporting on climate change does not meet SEC requirements.” Jim Coburn & Jackie Cook, *Cool Response: the SEC & Corporate Climate Change Reporting*, CERES 5 (2014), <http://www.ceres.org/resources/reports/cool-response-the-sec-corporate-climate-change-reporting/view> [<http://perma.cc/EYN8-AJDQ>].

195. Longstreth, *supra* note 43.

Finally, recently, oil prices have been falling, which has also led to a resulting downturn of energy stocks.¹⁹⁶ There was a 60% drop in oil prices between June 2014 and January 2015.¹⁹⁷ The U.S. Energy Information Administration has analyzed the growing volatility and price uncertainty of crude oil, expecting oil prices to remain low through 2016 and 2017.¹⁹⁸

D. IMPLEMENTATION CHALLENGES

In addition to transaction costs, such as brokerage fees, that can conflict with the duty to minimize costs,¹⁹⁹ there are implementation challenges involved in divestment, such as identifying which stocks to divest from and which new investments to make in their place.²⁰⁰ Institutions are worried about passing judgment on what constitutes an ethical investment, which can be seen as a subjective decision.²⁰¹ Ethical investing could lead to “acrimonious and irresolvable debates about the correct ethical course.”²⁰² However, many universities did join the South Africa divestment movement and did not fall down this “slippery slope” demonstrating this is a debate universities are capable of handling. Additionally, since climate change represents the greatest existential threat humans face today, if any issue merits divesting for, it would arguably be climate change. Another challenge is deciding where to invest the money taken out of fossil fuel companies, as

196. Larry Milstein, *Falling Oil Prices May Recast Divestment Debate*, YALE DAILY NEWS (Jan. 20, 2015), <http://yaledailynews.com/blog/2015/01/20/falling-oil-prices-recast-divestment-debate/> [<http://perma.cc/X5N2-7MKT>].

197. *Id.*

198. *Short-Term Energy Outlook*, U.S. ENERGY INFO. ADMIN. (Jan. 12, 2016), <http://www.eia.gov/forecasts/steo> [<http://perma.cc/D72A-446Z>].

199. RESTATEMENT (THIRD) OF TRUSTS § 88 (2007) (“A trustee can properly incur and pay expenses that are reasonable in amount and appropriate to the purposes and circumstances of the trust and to the experience, skills, responsibilities, and other circumstances of the trustee.”).

200. See DANIEL R. FISCHER, FOSSIL FUEL DIVESTMENT: A COSTLY AND INEFFECTIVE INVESTMENT STRATEGY 3 (2015), http://divestmentfacts.com/pdf/Fischel_Report.pdf [<http://perma.cc/Z3RS-NX6U>].

201. Richardson, *supra* note 135, at 560. See also Schotland, *supra* note 156, at 31 (“Furthermore, who decides what the goals and priorities of the divergent portfolio should be? Divergence involves the participants and their trustees in a decision process that will be political at best or subjective and divisive at worst. John Petersen has put it most pointedly: ‘One man’s ‘socially useful’ investment is another man’s ‘do-gooder boondoggle.’ In any event, the decisions are likely to be unacceptable unless they result from a truly political process.”).

202. Richardson, *supra* note 33, at 487.

currently clean energy firms are not big enough to take in the \$5 trillion currently invested in oil and gas firms.²⁰³

IV. LEGAL INERTIA AS A BARRIER TO DIVESTMENT AND SUGGESTED REFORMS

Many commentators have noted the reluctance of institutional investors to embrace social investing and suggested reforms and legislation to make social investing more accessible and utilized. However, few have looked specifically at climate change and argued that considering climate change impacts should be a requirement to meet fiduciary duty under existing law. This Part will raise some of the concerns and solutions commentators have discussed.

As mentioned earlier, there is growing support for the idea that climate change is a material financial concern.²⁰⁴ Climate change is expected to have a damaging impact on economic markets.²⁰⁵ Others argue “there is no inherent conflict between pension funds’ fiduciary duty and the consideration of climate change as a risk or opportunity, in circumstances where climate change is likely to have a demonstrable financial impact over the long term.”²⁰⁶ The problem preventing institutional investors from

203. Evans, *supra* note 168. Naomi Klein has suggested divested funds be used as a climate justice tool and reinvested to help grassroots groups set up clean energy projects in their local communities. Grist Staff, *Naomi Klein on the power of fossil fuel divestment*, GRIST (Feb. 11, 2015), <http://grist.org/climate-energy/naomi-klein-on-the-power-of-fossil-fuel-divestment> [<http://perma.cc/FL3S-LN52>].

204. See FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34.

205. See STERN REVIEW: THE ECONOMICS OF CLIMATE CHANGE ii. (“The evidence shows that ignoring climate change will eventually damage economic growth. . . . The earlier effective action is taken, the less costly it will be.”). The Stern report found that with no action on climate change, the effects would cause costs from 5% to 20% of global GDP per year, whereas the costs of reducing greenhouse gases to avoid the most catastrophic impacts would take only 1% of world GDP per year. *Id.* at vi. Stern eventually updated his report to suggest spending 2% of world GDP. Juliette Jowit & Patrick Wintour, *Cost of Tackling Global Climate Change Has Doubled, Warns Stern*, GUARDIAN (June 24, 2008, 7:01 PM), <http://www.theguardian.com/environment/2008/jun/26/climatechange.scienceofclimatechange> [<http://perma.cc/DMZ3-GT7P>]. See also U.S. GLOBAL CHANGE RESEARCH PROGRAM, CLIMATE CHANGE IMPACTS IN THE UNITED STATES: THE THIRD NATIONAL CLIMATE ASSESSMENT (Jerry M. Melillo, Terese (T.C.) Richmond, and Gary W. Yohe eds., 2014) 131, nca2014.globalchange.gov [<http://perma.cc/5QEU-EVR3>] (explaining, for example: “The U.S. economy depends on the personal and freight mobility provided by the country’s transportation system. . . . The national transportation system is composed of four main components that are increasingly vulnerable to climate change impacts[.]”).

206. Claire Woods, *Funding Climate Change: How Pension Fund Fiduciary Duty Masks Trustee Inertia and Short-Termism*, in *Corporate Governance Failures* 264 (2011).

taking into account climate change impacts arises from lingering confusion over fiduciary duty and legal interpretations of fiduciary duty that encourage investors to continue with the status quo.

Fiduciary duty law in this area is unclear because there is scant current case law and legislative commentary.²⁰⁷ Though fiduciary duty has the ability to change over time (and has changed significantly over time) to keep up with changing social conditions,²⁰⁸ the change is incremental and slow.²⁰⁹ While in theory, even under a strict interpretation of fiduciary duty, managers should be able to take into account climate change when making investment decisions, in practice inertia and uncertainty prevents this from happening.²¹⁰ Some have linked this “legal inertia” to the prudent man standard.²¹¹ Because the standard compares actions to that of a prudent man, investors typically look to their peers to assess what kind of investment behavior is acceptable, which makes any kind of innovation or deviation from current prevailing standards difficult.²¹² Since pension funds are preoccupied with short-term benefits, this can unfortunately come at the cost of long-term value.²¹³

This problem is especially pronounced when it comes to tackling climate change, because “[t]he incrementalism central to the maturation of fiduciary duty in the past cannot facilitate the urgent action required by climate change.”²¹⁴ One potential solution involves (1) legislation to clarify climate change considera-

207. *Id.* at 272.

208. *See also* Richardson, *supra* note 31, at 188 (“Fiduciary duties are not static, and have evolved to reflect changing social norms and values. Over fifty years ago, for instance, fiduciary duties were held by British courts to preclude municipal authorities from applying a standard minimum wage for adult men and women and providing subsidized public transport.”).

209. Woods, *supra* note 206, at 268.

210. *Id.* at 277. *See also* Sandberg, *supra* note 35, at 146 (“In a recent survey among American pension fund trustees, for example, as many as 45% of respondents indicated that considerations of fiduciary duty were their main reason for not engaging more actively in SRI.”).

211. Woods, *supra* note 206, at 268.

212. Woods, *supra* note 206, at 269. *See also* Hess, *supra* note 145, at 30 (“For example, in the UK, 63 percent of pension fund trustees indicated that in making investment decisions their fund ‘sticks as closely as possible to the accepted practice in the industry.’”); Keith L. Johnson & Frank Jan de Graaf, *Modernizing Pension Fund Legal Standards for the Twenty-First Century*, 2 *ROTMAN INT’L J. PENSION MGMT.* 44, 45 (2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1408691 [<http://perma.cc/U4GR-E9VP>].

213. Hess, *supra* note 145, at 45.

214. Woods, *supra* note 206, at 271.

tions are compatible with fiduciary duty requirements and (2) reconsideration of pension funds' investment practices and an adoption of best-practice governance measures to aid this process.²¹⁵

These measures are similar to reforms others have advocated. For example, it has been suggested that state laws should include greater lawsuit protection for fund managers who divest in order to comply with state laws.²¹⁶ Another suggestion includes (1) having government policies set a value on carbon emissions (in order for the "business case" to carry any weight)²¹⁷ and (2) focusing on the ethical and social values behind taking into account climate change impacts which could be done by (a) requiring fiduciaries to be accountable for the social and environmental costs they create,²¹⁸ and (b) giving more voice in investment decision-making to ordinary fund members and affected third-parties.²¹⁹ Some have also considered (1) expressly authorizing fiduciaries to, at their discretion, consider social and environmental factors they consider material,²²⁰ (2) legislation that requires procedures to improve the likelihood these factors are taken under consideration,²²¹ and (3) mandating that a fiduciary take into account sustainability factors.²²² Others advocate for legislative clarification that would explicitly authorize "constrained social investing."²²³ These advocates argue that not only should legislatures specify divestment can be appropriate in certain situations, but they

215. *Id.* at 278.

216. Salar Ghahramani, *Protecting Public Pension Funds from Divestment-Related Lawsuits: Exploring the State Laws of the United States*, 16 PENSIONS 212 (2011), available at <http://www.palgrave-journals.com/pm/journal/v16/n3/full/pm201117a.html> [<http://perma.cc/D999-7PMG>].

217. Richardson, *supra* note 135, at 510.

218. *Id.* at 513.

219. *Id.* at 514.

220. Benjamin J. Richardson, *Putting Ethics into Environmental Law: Fiduciary Duties for Ethical Investment*, 46 OSGOODE HALL L.J. 243, 277 (2008), <http://digitalcommons.osgoode.yorku.ca/cgi/viewcontent.cgi?article=1195&context=ohlj> [perma.cc/GD2C-6ZVW].

221. *Id.* at 279.

222. *Id.* at 282.

223. Jerry & Joy, *supra* note 88, at 748. The authors argued in favor of "constrained social investing" after analyzing portfolio risk and returns after divestment from South African stocks and finding that divestment could be done with no effect on those factors. Therefore, the authors concluded that social investing should be allowed where it has no effect on portfolios. They also argued that their position in favor of constrained social investing needs legislative clarification. *Id.*

should also set threshold standards that would give a presumption of validity to social investing.²²⁴

Many codes of conduct for fiduciaries do require a look at factors beyond short-term value. The CFA Institute advises that pension fund governing boards must consider “all relevant risk and value factors . . . [which] may include environmental, social, and corporate governance issues.”²²⁵ It acknowledges a trustee’s need to incorporate a level of risk that will generate high returns for future beneficiaries while not jeopardizing payments to current ones.²²⁶ Thus, it seems the solution to this problem cannot be solved by “best practices” codes alone.

The business case argument for divestment, where divestment is motivated only by financial prudence, carries its own set of problems.²²⁷ Though many of the reforms explored in this Note would authorize investors to consider social and environmental factors they view as materially relevant to financial performance,²²⁸ this still would not establish an affirmative duty to consider those factors.²²⁹ The “business case” for divestment frames problems such as sea level rise, hurricanes, drought, and famine in terms of their financial rather than ethical or moral dimensions, and limits consideration to only those impacts that are “material” to financial management.²³⁰ This is problematic because the perceived harmony between environmental protection and doing what’s best for business “can be a pretext for the per-

224. *Id.* at 750–51 (“Thus, a legislature might enact a statute that declares presumptively valid any social investing plan that excludes no more than forty percent of the New York Stock Exchange or S&P 500 by market capitalization and otherwise satisfies important financial qualifiers. . . . The statute could then place the burden on the person challenging the social investing strategy to show by clear and convincing evidence that the particular divestment’s unique circumstances will impair portfolio performance relative to other investment strategies not similarly constrained.”).

225. CFA INSTITUTE, CODE OF CONDUCT FOR MEMBERS OF A PENSION SCHEME GOVERNING BODY 3 (2015), <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2008.n3.1> [<http://perma.cc/GYP5-X72J>].

226. *Id.* at 3.

227. This view has been endorsed by UNEP. Benjamin J. Richardson, *supra* note 135, at 557.

228. *Id.* at 565.

229. *Id.*

230. Benjamin J. Richardson, *Climate Finance and its Governance: Moving to a Low Carbon Economy Through Socially Responsible Financing?*, 58 THE INT’L AND COMP. LAW QUARTERLY 597, 608 (2009); *see also id.* at 606 (“[T]he SRI movement has increasingly disavowed ethical arguments in favour of a business case for social investment. By tying social and environmental activism to furthering the ‘bottom line’, SRI has diminished its pretences to stand for change. . . .”).

petuation of business-as-usual.”²³¹ The business cost-benefit analysis has yet to adequately value environmental ideals and the economy has yet to become “ecologically sustainable.”²³² Business reasons favoring the environmentally destructive activity often exist.²³³

As an example, one critic has refuted arguments that climate change is indisputably a fiduciary concern saying “[t]he potential impacts of climate change are inherently difficult to quantify” and “[t]he determination of whether such impacts constitute a risk for investment purposes is a subjective matter.”²³⁴ The “business case” alone does not support the drastic, preemptive action that must be taken to stop climate change. Climate change is unlike other threats in that it will take global, collective action to address. As Jeffrey Sachs has said:

[F]ossil-fuel use is a social dilemma: it makes sense for the individual but not for the society as a whole. . . . Indeed, for the society as a whole, the prevailing way of using fossil fuels is ruinous, already claiming lives of the poor abroad through droughts, floods, and extreme tropical cyclones; and threatening our very survival in the future.²³⁵

In the macro view it is easy to see how Bill McKibben’s math spells doom if shareholders continue to try and profit off fossil fuels, but, for the individual shareholder, it is easier to argue that their investment is safe or that their divestment will have no impact. Fiduciary duty law must recognize this paradox, remove the subjectivity of the decision, and hold that fiduciaries should always consider climate risk to be material.

231. *Id.* at 609.

232. *Id.* (“Investment analysts often perceive social or environmental values as too nebulous for workable financial quantification.”).

233. *Id.* (“The continuing investment in Canada’s oil sands is one controversial example. Without additional ethical motivations, financiers may lack the incentive to take actions beyond those prescribed by a business case.”).

234. *Annex I — Critique of the Campaign for Sustainability to Become a Fiduciary Consideration*, *supra* note 113, at 3.

235. Jeffrey Sachs, Speech at Columbia University: What is a Moral University in the 21st Century? (Mar. 30, 2015) (transcript available at <http://jeffsachs.org/2015/04/2748> [<http://perma.cc/VZ3Y-GTF4>]).

V. DIVESTMENT LITIGATION

Part IV discussed various obstacles preventing institutions from divesting despite a strong moral and financial case to do so, and this Part will discuss how litigation may offer a solution by calling upon courts to require fund managers to consider climate change impacts as part of their fiduciary duties. A group of students at Harvard, after spending years trying to convince Harvard to divest to no avail, and “with the clock ticking on the climate crisis,” are spearheading divestment litigation taking the debate “to a forum more amenable to fair and open argumentation: the courts.”²³⁶ This Part will analyze the Harvard lawsuit, consider the special case of public pension funds and charitable institutions, which arguably owe a special duty to consider climate change impacts in their investment decisions, and, finally, justify this new role for the courts by building upon atmosphere as public trust litigation.

A. THE HARVARD LAWSUIT

On November 19, 2014, a group of undergraduate, graduate, and law students at Harvard filed a lawsuit against the president and fellows of Harvard College and the Massachusetts Attorney General, in her capacity as regulator of charitable corporations, over Harvard University’s endowment containing fossil fuel investments.²³⁷ The complaint accuses Harvard of “mismanagement of charitable funds” and “intentional investment in abnormally dangerous activities.”²³⁸ The complaint lists “Future Generations, individuals not yet born or too young to assert their rights but whose future health, safety, and welfare depends on

236. Alice Cherry, Ted Hamilton, and Kelsey Skaggs, *Opinion: Litigation Could be the Newest Tool for the Divestment Movement*, DAILY CLIMATE (Apr. 9, 2015), <http://www.dailyclimate.org/tdc-newsroom/2015/04/divestment-harvard-universities-fossil-fuels-coal> [<http://perma.cc/C7ZA-4ELM>].

237. Complaint for Declaratory and Injunctive Relief, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (No. 14-3620); John Schwartz, *Harvard Students Move Fossil Fuel Stock Fight to Court*, N.Y. TIMES (Nov. 19, 2014), <http://www.nytimes.com/2014/11/20/us/harvard-students-move-fossil-fuel-divestment-fight-to-court.html> [<http://perma.cc/CTJ2-2GSS>].

238. Complaint for Declaratory and Injunctive Relief at 6–11, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (No. 14-3620).

current efforts to slow the pace of climate change” as a plaintiff in the suit.²³⁹

The complaint states that, under the constitution of Massachusetts, Harvard University has a unique duty to the public.²⁴⁰ The students claim this requires Harvard to “act[] in the public interest, further[] the education and welfare of students, and refrain[] from actions known to cause harm to the public and students.”²⁴¹ Under Harvard’s charter, the university also has a mission to act for “the advancement and education of youth’ and to maintain its physical campus for the wellbeing of its students.”²⁴² They say that investment in fossil fuel companies contributes to “sea level rise and increased storm activity” that will lead to future damage to the campus and, since the plaintiffs are studying at Harvard to enter into various environmental careers, fossil fuel companies spreading climate denial research harm their education.²⁴³ Thus, by not divesting, Harvard is allegedly in violation of this mission and its duties.²⁴⁴

The lawsuit was dismissed by the court that found the students lacked standing to bring these claims.²⁴⁵ Under Massachusetts’s law, only the Attorney General can enforce proper management of charitable funds, aside from an exception for plaintiffs with a special interest apart from that of the general public.²⁴⁶ The court denied the students special interest standing²⁴⁷ and failed to recognize their novel claim of intentional investment in abnormally dangerous activities.²⁴⁸ The case has been appealed.²⁴⁹

239. *Id.*

240. *Id.* at 4. The Massachusetts constitution gives the state legislature authority to “mak[e] such alterations in the government of the said university, as shall be conducive to its advantage and the interest of the republic of letters,” and prescribes a duty to “legislatures and magistrates” to ensure the charitable operation of schools, especially Harvard. *Id.* at 4–5.

241. *Id.*

242. *Id.* at 6.

243. *Id.* at 8.

244. *Id.* at 6–7.

245. Harvard Climate Justice Coal. v. President and Fellows of Harvard Coll., 32 Mass. L. Rptr. 529 (Mass. Sup. Ct. 2015).

246. *Id.* at 3.

247. *Id.* at 8.

248. *Id.* at 8–9.

249. Appellants’ Application for Direct Appellate Review, Harvard Climate Justice Coal. v. President and Fellows of Harvard Coll., *appeal docketed*, No. 2015-P-0905 (Mass. App. Ct. Mar. 17, 2015).

Though standing presents one major obstacle to divestment litigation, this lawsuit demonstrates what divestment litigation can look like. First, while two NGOs, ClientEarth and the Asset Owner's Disclosure Project, have threatened legal action against pension funds invested in assets that carry material financial risks posed by climate change,²⁵⁰ the Harvard lawsuit demonstrates that legal hooks for such cases extend beyond financial harm. With a tort claim alleging violation of a "duty of care" to future generations, though not successfully recognized by the court, the students link investing in fossil fuels to risking the *physical* safety of future beneficiaries and their property.²⁵¹ Second, the plaintiffs accused Harvard of breaching duties it was bound to in its charter, including "the advancement and education of youth."²⁵² This suggests that legal suits may be tailored to individual institutions and their particular missions, especially for nonprofit corporations and public charities.

It is worth noting that Harvard's president, while explaining Harvard's decision *not* to divest, stated the endowment funds were entrusted solely "to advance academic aims, not to serve other purposes, however worthy."²⁵³ Here, the Harvard plaintiffs show how divestment furthers those very academic aims because investment in fossil fuel companies supports the spread of false science and climate denial, impedes academic research into climate change solutions, and thus diminishes their educations.²⁵⁴

Another question is what potential remedies might look like. The plaintiffs in the Harvard lawsuit asked for injunctive relief and not damages, asking Harvard withdraw direct holdings in fossil fuel companies and take immediate steps to withdraw indi-

250. Media Release, Asset Owners Disclosure Project, NGOs Challenge Pension Funds to Fulfill Legal Duties on Climate Risk (Apr. 27, 2015), <http://aodproject.net/news/84-ngos-challenge-pension-funds.html> [<http://perma.cc/D5BJ-AAWH>]; Michael J. Casey, *On 'Global Divestment Day,' Some Climate Activists Look to Courts*, WALL ST. J.: MONEYBEAT (Feb. 13, 2014, 10:34 AM), <http://blogs.wsj.com/moneybeat/2015/02/13/on-global-divestment-day-some-climate-activists-look-to-courts> [<http://perma.cc/GN3H-FPGN>].

251. Plaintiffs' Memorandum in Opposition to the Harvard Defendants' Motion to Dismiss at 16, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (Jan. 6, 2015) (No. 14-3620H).

252. Complaint for Declaratory and Injunctive Relief at 6, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (Nov. 19, 2014) (No. 14-3620).

253. Faust, *supra* note 38.

254. Complaint for Declaratory and Injunctive Relief at 8–9, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (Nov. 19, 2014) (No. 14-3620). However, if there were a duty to fulfill some other mission (as the students claim there is), the fiduciaries should work towards fulfilling that cause. Richardson, *supra* note 31, at 161.

rect holdings.²⁵⁵ The Judge, however, took issue with a supposed lack of limiting principle that could lead to a torrent of lawsuits on divestment for all other issues. The decision stated: “If Plaintiffs can bring this lawsuit, nothing would prevent other students from seeking court orders that Harvard — or any other charitable organization — take other actions to deal with the ‘exceptional risks’ posed by whatever danger to Future Generations those other students fear above all others.”²⁵⁶ However, the Harvard students have rightfully refuted this argument by pointing out that the “broad scientific agreement” that climate change “poses an existential threat to human civilization,” differentiates this cause.²⁵⁷

B. SPECIAL DUTIES OF CHARITABLE AND PUBLIC FUNDS

As the Harvard lawsuit demonstrates, if there is a case to be made for mandating that certain institutional investors take into account the social and environmental impacts related to climate change in their portfolios,²⁵⁸ it is especially compelling for public and charitable institutions. Stanford University has acknowledged that it has “stewardship responsibilities which attend the ownership of endowment assets . . . [and] that there is no practical way for the University to avoid having an effect on the outcome of issues involving corporations in which it has invested.”²⁵⁹ The F.B. Heron Foundation has also acknowledged it has a “duty of obedience to a larger public purpose” beyond its own mission that obligates the foundation to review its portfolio “on an ongo-

255. Complaint for Declaratory and Injunctive Relief at 11, *Harvard Climate Justice Coal.*, 32 Mass. L. Rptr. 529 (Nov. 19, 2015) (No. 14-3620).

256. *Harvard Climate Justice Coal. v. President and Fellows of Harvard Coll.*, 32 Mass. L. Rptr. 529, 2015 WL 1519036, at *9 (Mass. Sup. Ct. 2015).

257. Appellant’s Brief at 7, *Harvard Climate Justice Coal. v. President and Fellows of Harvard Coll.*, *appeal docketed*, No. 2015-P-0905 (Mass. App. Ct. Mar. 17, 2015). An article summarizing the science on climate change’s impacts concluded “[c]ontinuation of high fossil fuel emissions, given current knowledge of the consequences, would be an act of extraordinary witting intergenerational injustice.” James Hansen et al., *Assessing “Dangerous Climate Change”: Required Reduction of Carbon Emissions to Protect Young People, Future Generations and Nature*, 8 PLOS ONE 1 (Dec. 2013).

258. See, e.g., *Divesting from Fossil Fuels Will Soon Be a Fiduciary Duty*, GREEN MARKET ORACLE (Oct. 2, 2014), <http://www.thegreenmarketoracle.com/2014/10/divesting-from-fossil-fuels-will-soon.html> [<http://perma.cc/9KTK-YX3H>]. See also Kanzer, *supra* note 92.

259. *Stanford University’s Statement on Investment Responsibility*, STANFORD UNIV. (June 2015), <http://irsr.stanford.edu/documents/Stanford%20University%20Statement%20on%20Investment%20Responsibility.pdf> [<http://perma.cc/AJ9E-RDU5>].

ing basis to identify holdings that may unintentionally do harm to our missions or to the broader shared interests of society.”²⁶⁰ Since charities and public entities often have charters and statutes governing their mission and imposing a duty to the public, it makes sense to ask them to take into account the wider impact of their investment decisions on the broader public interest.²⁶¹

Others have spoken to the unique and special role pension funds hold in society, stating, “[p]ension trusts, especially large ones, are very much quasi-public entities, tightly woven into the fabric of society. It is hardly dramatic to suggest that they should be invested to obtain, in part, a benefit for persons other than the direct trust beneficiaries.”²⁶² Additionally, since they “hold a broad portfolio of stocks and other assets, they are inherently biased towards the health and long-term sustainability of the entire economy” and “[g]iven the ubiquity of pension fund membership, the interests of members should be broadly consistent with those of the society in which members live.”²⁶³

Charitable trusts may also owe a financial debt to the public because of the privileges they enjoy from being tax exempt.²⁶⁴ As proved to be an obstacle in the Harvard lawsuit, in most states only the state attorney general and sometimes “parties with a ‘special interest’” have standing to bring a lawsuit to enforce the

260. ALL INVESTING IS IMPACT INVESTING: PREFACE TO HERON’S INVESTMENT POLICY AND PRINCIPLES 2 (2014), <https://www.missioninvestors.org/system/files/tools/Heron-Investment-Policy-Statement-and-Preface-2014.pdf> [<http://perma.cc/Q3XG-RZBM>].

261. FRESHFIELDS BRUCKHAUS DERINGER, *supra* note 34, at 113 (citing the “leading US trusts treatise, *Scott on Trusts*” as supporting the view that trustees may consider ethical principles in investment decisions). Additionally, in the comments to RESTATEMENT (THIRD) OF TRUSTS: P.I.R. § 227 (1992) it is noted that “social considerations may be taken into account in investing the funds of charitable trusts to the extent the charitable purposes would justify an expenditure of trust funds for the social issue or cause in question or to the extent the investment decision can be justified on grounds of advancing, financially or operationally, a charitable activity conducted by the trust.”

262. Joel C. Dobris, *Arguments in Favor of Fiduciary Divestment of “South African” Securities*, 65 NEB. L. REV. 209, 229 (1986), <http://digitalcommons.unl.edu/nlr/vol65/iss2/2> [<http://perma.cc/7QTB-JTM9>].

263. Richardson, *supra* note 31, at 169–70. Richardson also notes that it is “a zero-sum game for an investor to favour a profitable but polluting fossil fuel business if it created risks and costs for other economic sectors the investor has a stake in.” *Id.* at 164. Additionally, “if the environmental cost is externalised onto the taxpayer (i.e., to clean up a toxic waste site), those taxpayers will most likely also be members of the fund. Thus, in theory, pension funds should be particularly attentive to the social and environmental performance of their investee companies, even if it means that a particular company must be divested from the fund’s portfolio.” *Id.* at 170.

264. Ilana H. Eisenstein, *Keeping Charity in Charitable Trust Law: The Barnes Foundation and the Case for Consideration of Public Interest in Administration of Charitable Trusts*, 151 U. PA. L. REV. 1747, 1760 (2003).

fiduciary duty of a charitable trustee.²⁶⁵ This is costly on society, considering the limited resources of state attorneys general.²⁶⁶ It is justified, however, because the attorney general “acts under the *parens patriae* power” to protect the public interest signaling that “the public is the ultimate beneficiary of all charities, notwithstanding the specific nature of the bequest.”²⁶⁷ This further supports why a duty to consider climate impacts might be imposed on charitable trusts.

In certain cases, it seems antithetical to the mission of the institution for it to be invested in fossil fuel companies and may even create a conflict of interest. For example, while governors in Oregon and Washington have been voicing opposition to the building of coal export stations in their states, the Oregon Investment Council and the Washington State Investment Board have investments financing the very projects being opposed by other governmental branches.²⁶⁸ Health organizations, such as the British Medical Association, which previously divested from tobacco companies,²⁶⁹ stand out as organizations that should not be invested in companies directly contributing to a public health hazard. One report has proclaimed “[i]t is arguably both immoral and inconsistent for the health sector to continue to invest in industries known to harm health, given its clear responsibility to protect health.”²⁷⁰ Finally, activists have been especially pointed about arguing that universities have a special stake in the effort

265. *Id.* at 1765.

266. *Id.* at 1767.

267. *Id.* at 1766.

268. Eric de Place & Nick Abraham, *How State Public Money Pays for Coal Exports and Oil Trains*, SIGHTLINE DAILY (Sept. 17, 2014, 6:30 AM), <http://daily.sightline.org/2014/09/17/how-state-public-money-pays-for-coal-exports-and-oil-trains> [<http://perma.cc/V4R8-GYUH>].

269. ALISTAIR WARDROPE & ISOBEL BRAITHWAITE, UNHEALTHY INVESTMENTS: FOSSIL FUEL INVESTMENT AND THE UK HEALTH COMMUNITY 5 (2015), <http://www.medact.org/wp-content/uploads/2015/02/UnhealthyInvestments-Spreads-Final-Version.pdf> [<http://perma.cc/MTN4-YPCJ>].

270. *Id.* They argue that there is a social contract between the health community and society and that health professionals should consider how their actions, even outside of the clinic, impact the public health. *Id.* at 12. In 1986, the American Medical Association wrote to every medical school in America asking for divestment from tobacco. *Id.* Because of the wide-ranging impacts on health from climate change, fossil fuel divestment has been compared to the tobacco divestment movement. *See, e.g.*, Jesse Rieseborough & Thomas Biesheuvel, *Coal Seen as New Tobacco Sparking Investor Backlash: Commodities*, BLOOMBERG BUS., (Nov. 20, 2013, 11:23 AM) <http://www.bloomberg.com/news/articles/2013-11-20/coal-seen-as-new-tobacco-sparking-investor-backlash-commodities> [<http://perma.cc/GZF4-MM4J>].

to divest from fossil fuels because they are the research centers leading the world forward on climate science.²⁷¹

C. APPLYING THE ATMOSPHERE AS PUBLIC TRUST THEORY TO THE DIVESTMENT CONTEXT

A useful framework that courts can follow to impose this fiduciary duty is the atmosphere as public trust theory developed by Mary Woods. Wood's theory starts with the well-developed public trust doctrine.²⁷² The public trust doctrine holds that "the public holds a perpetual common property interest in crucial natural resources . . . [and] [g]overnment, as trustee, must act in a fiduciary capacity to protect such natural assets for the beneficiaries of the trust, which include both present and future generations of citizens."²⁷³ Under the overarching public trust doctrine, the trustee has an affirmative duty to protect the asset including an "active duty of vigilance to 'prevent decay or waste' to the asset."²⁷⁴ Importantly, the trustee must protect assets not just for current beneficiaries, but also for future generations.²⁷⁵ This doctrine has traditionally been applied to water-based resources, and Wood has argued that it should be extended to the atmosphere.²⁷⁶ The argument has had limited success in courts. The Washington State Superior Court found that climate change affected the state's navigable waters, a public trust resource that the state had a duty to protect²⁷⁷ and the New Mexico State Court of Appeals found that the atmosphere was a public trust resource,²⁷⁸

271. McKibben, *supra* note 17 ("Universities need to lead because they are where we first found out about climate change. It was in physics labs and on university supercomputers that the realization we were in trouble first dawned a generation ago.")

272. Mary Christina Wood, *Atmospheric Trust Litigation Around the World, in FIDUCIARY DUTY AND THE ATMOSPHERIC TRUST* 99, 106 (Ken Coghill et al., eds., 2012), http://ourchildrenstrust.org/sites/default/files/ATLAcrossTheWorld_0.pdf [<http://perma.cc/2EZ8-CEUJ>] (last visited Sept. 14, 2015). For more on the public trust doctrine, see, e.g., *Ill. Cent. R.R. v. Illinois*, 146 U.S. 387 (1892).

273. *Id.* at 106.

274. *Id.* at 110.

275. *Id.* at 111.

276. *Id.* at 114 ("[W]hile air has not yet been the subject of trust litigation, modern courts have a solid legal rationale from which to draw in designating the atmosphere as a public trust asset.")

277. *Foster v. Wash. Dep't of Ecology*, 362 P.3d 959 (Wash. 2015) (en banc).

278. *Sanders-Reed ex rel. Sanders-Reed v. Martinez*, 350 P.3d 1221, 1227 (N.M. Ct. App. 2015).

though both declined to order the state to regulate greenhouse gases through a process other than what it already had in place.

Wood's theory is revolutionary because it envisions courts, not agencies or legislators, as drivers of climate policy. In this model, the judiciary can "compel the political branches to meet their fiduciary obligation through whatever measures and policies they choose, as long as such measures sufficiently reduce carbon emissions within the required time frame."²⁷⁹ This role is justified because the threat of climate change is so dire²⁸⁰ and because traditional political and legislative processes are failing.²⁸¹ The trust approach creates an all-encompassing "macro level legal strategy"²⁸² and is a solution that is protected from the political pressure stalling climate change action in Congress and that can be molded to address the crises.²⁸³ As Wood articulates, action on climate change requires lawyers to move beyond relying on existing environmental statutes, which are "a product of an altogether different era, formulated to respond to circumstances far less urgent, less dangerous, and less pervasive than those now confronting society."²⁸⁴

Given the massive political tension in the debate over divestment, similar arguments can be made to support a common law expansion of fiduciary duty to require consideration of climate impacts. Courts could recognize not only (1) the increasing materiality of climate change to portfolio performance, but also (2) the special duties public and charitable institutions owe to the public

279. Wood, *supra* note 272, at 126. Wood relies on the same math that McKibben does in attempting to persuade courts and judges to enforce mandatory, quantitative limits on carbon emissions. *Id.* Wood takes a global temperature increase of 1.5 degrees Celsius as the limit in order to avoid "dangerous anthropogenic heating." *Id.* at 128. Scientists have determined that in order to achieve this limit atmospheric concentrations of carbon must be kept below 350 parts per million, and this is the fiduciary obligation Wood says courts should impose on fiduciaries. *Id.* at 128.

280. Mary Christina Wood, *Atmospheric Trust Litigation*, in *CLIMATE CHANGE READER 2* (W.H. Rodgers, Jr. & M. Robinson-Dorn, eds., 2011) ("Should Business as Usual continue even for a few more years, our children and their descendants — future Humanity for untold generations — will be pummeled by floods, hurricanes, heat waves, fires, disease, crop losses, food shortages, and droughts as part of a hellish struggle to survive within a deadly greenhouse of our own making.").

281. *Id.* at 3 ("The scope and pervasiveness of carbon pollution is so vast that it slips through established legal paradigms. The time lag inherent in the future infliction of cruelty, deprivation, and death through pollution unleashed today defies causal linkages familiar to the law. Yet, law is a creative institution and, to be of any use at all, must mold to new and urgent circumstances.").

282. *Id.* at 21.

283. *Id.* at 22.

284. *Id.* at 58.

interest, to find that these institutions must consider the climate change impacts on and of their portfolios. The public trust doctrine further supports the idea that public entities should not have financial policies that contribute to climate change. In the case of investing in fossil fuel companies whose business plans are fundamentally incompatible with action on climate change, the mandate should be divestment. An alternative solution might be to merely require these institutions to take into account the climate change impacts of their investments, and to consider alternative investment decisions.²⁸⁵

VI. CONCLUSION

As Christiana Figueres, Executive Secretary of the UNFCCC, has stated, “fiduciary responsibility needs to grasp the intergenerational reality: namely that unchecked climate change has the potential to impact and eventually devastate the lives, livelihoods and savings of many, now and well into the future.”²⁸⁶ Climate change’s impacts will be felt around the globe and shatter people’s lives, with the least privileged feeling the greatest burden. Action must be taken immediately in order to prevent the worst impacts, and yet the U.S. and global political systems have failed to effectuate rapid mitigation.

Divestment offers a powerful tool to mobilize support and send a clear signal to politicians and those in power that action must be taken on this issue, and that legislation restricting carbon emissions must be passed. Fiduciary duties are entirely compatible with making the decision to divest, especially given the risk involved in holding fossil fuel stocks and their stranded assets. Yet, overcoming the institutional inertia and its tendency to resist change has proven to be a struggle. Charities and public institutions should not be invested in, and profiting off of, activities that are harmful to the very public and beneficiaries they exist to

285. Richardson, *supra* note 31, at 187–88 (“SRI-based regulation should probably aim (at least for the moment) to promote informational, incentive and other procedural mechanisms to nurture the conditions for SRI among pension funds and other investors. However, if the gravity of our social and environmental problems worsens, more interventionist reforms to promote SRI may be viable.”).

286. *Press Release: Safeguarding Future Retirement Funds — Time for Investors to Move Out of High-Carbon Assets Says UN’s Top Climate Official*, UNITED NATIONS CLIMATE CHANGE SECRETARIAT (Jan. 15, 2014), https://unfccc.int/files/press/press_releases_advisories/application/pdf/pr20140115_ceres_final1.pdf [http://perma.cc/X87W-8GKP].

serve. Through lawsuits like the one brought against Harvard, and innovative legal theories that advocate for preserving resources for the public, there is a chance to compel these institutions to live up to their duty and divest for the public interest. Eventually, the movement might achieve its aims of building political support for climate action and ultimately preventing the burning of fossil fuels.