


MEMORANDUM

October 21, 2016

TO: County Council

FROM: Robert H. Drummer, Senior Legislative Attorney 

SUBJECT: **Introduction:** Bill 44-16, Retirement – Fossil Fuel Investments – Restrictions

Bill 44-16, Retirement – Fossil Fuel Investments - Restrictions, sponsored by Lead Sponsors Council Vice President Berliner and Councilmember Navarro and Co-Sponsor Councilmember Elrich, is scheduled to be introduced on October 25, 2016. A public hearing is tentatively scheduled for November 22 at 1:30 p.m.

Bill 44-16 would restrict the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board of Trustees from investing in certain businesses holding the largest amount of fossil fuel reserves under certain circumstances. The Bill would also require both Boards to research and adopt a socially responsible policy for investing.

Background

The Board of Investment Trustees (BIT) manages prudent investment programs for the trust fund established to pay retirement benefits guaranteed under the Employees' Retirement Plans. The Consolidated Retiree Health Benefits Trust Board of Trustees (CRHBT) Board is responsible for investing the funds designated to pay for all or a portion of benefits provided under the County retiree benefit plans or a County-funded agency retiree benefit plan, such as retiree health insurance.

Bill 44-16 would be the third time the County enacted a law requiring the BIT to sell certain types of investments to further important government objectives. In 1986, the Council, in Bill 23-86, restricted certain investments in companies doing business in the Republic of South Africa or Namibia due to the racial segregation or apartheid laws in those nations. This restriction was repealed when those nations repealed their apartheid laws. The Maryland Court of Appeals upheld a similar restriction on investments in companies doing business in the Republic of South Africa and Namibia in *Board of Trustees v. Mayor & City Council of Baltimore City*, 317 Md. 72 (1989).

In 2008, the Council, in Bill 3-08, restricted certain investments in companies doing business in Sudan in order to influence the Government of Sudan to end the atrocities in Darfur. State and local laws requiring the divestment of holdings in companies doing business in Sudan or other nations had been challenged in court on the basis of Federal preemption. The Supreme Court struck down a Massachusetts statute that required the state to boycott certain companies doing business with or in Burma in *Crosby v. National Foreign Trade Council*, 530 US 363 (2000). The Supreme Court struck down the state law, holding that it was preempted by federal statutes imposing sanctions on Burma and therefore violated the Supremacy Clause of the U.S. Constitution. Similarly, the U.S. District Court in Illinois issued an injunction against the Illinois Sudan Act in *National Foreign Trade Council v. Giannoulis*, 523

F.Supp.2d 731 (N.D. Ill. 2007). The Illinois statute in question prohibited the state from depositing funds in any financial institution unless it could certify that it did not loan money to the government of Sudan or certain companies doing business in Sudan and also prohibited state and local pension funds from investing in certain companies doing business in Sudan. The Court held that this statute violated the Supremacy Clause and the Foreign Commerce Clause of the U.S. Constitution.

In response to these decisions, Congress enacted the Sudan Accountability and Divestment Act of 2007. The President signed this Act into law on December 31, 2007. The Act expressly authorizes state and local governments to divest in companies doing business in Sudan and grants investment managers who implement these laws immunity from suit under certain circumstances. The Act establishes guidelines for the state or local government to follow in taking these divestment actions. The Act also requires a state or local government to submit written notice describing a Sudan divestment law to the Attorney General of the United States within 30 days after the enactment of the law. Bill 3-08 was consistent with the guidelines for divestment laws authorized by the Sudan Accountability and Divestment Act of 2007.

Both the BIT and the CRHBT Board hire professional investment managers to buy and sell securities. Bill 44-16 would limit the restriction to actively managed separate accounts and would exclude investments in an index fund, private equity fund, real estate fund, mutual fund, or other commingled or passively managed fund. The Bill would define a fossil fuel company as:

... a company listed in the 200 publicly traded coal, oil, and gas companies that hold reported fossil fuels reserves with the largest potential carbon emissions, as ranked in the Fossil Free Indexes US (FFIUS) published by Fossil Free Indexes LLC or a successor index, as updated annually.

The Bill would also require the Boards to divest in these companies gradually over the next 5 years and would permit the Boards to delay the sale of any individual security if necessary due to its fiduciary duty.

The Lead Sponsors, Council Vice President Berliner and Councilmember Navarro explained their reasons for introducing Bill 44-16 in ©8-9.

This packet contains:	<u>Circle #</u>
Bill 44-16	1
Legislative Request Report	7
Berliner and Navarro Memorandum	8

Bill No. 44-16
Concerning: Retirement – Fossil Fuel
Investments - Restrictions
Revised: October 21, 2016 Draft No. 5
Introduced: October 25, 2016
Enacted: April 25, 2018
Executive: _____
Effective: _____
Sunset Date: _____
Ch. _____, Laws of Mont. Co. _____

COUNTY COUNCIL FOR MONTGOMERY COUNTY, MARYLAND

Lead Sponsors: Council Vice President Berliner and Councilmember Navarro
Co-sponsor: Councilmember Elrich

AN ACT to:

- (1) prohibit the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board of Trustees from investing in certain businesses holding certain amounts of fossil fuel reserves under certain circumstances;
- (2) require the Boards to research and adopt a socially responsible investing policy; and
- (3) generally amend the law governing the investment of funds held in trust for the employees' retirement system and the consolidated retiree health benefits trust.

By adding

Montgomery County Code
Chapter 33, Personnel and Human Resources
Section 33-60C

By amending

Montgomery County Code
Chapter 33, Personnel and Human Resources
Sections 33-61A and 33-165

Boldface

Underlining

[Single boldface brackets]

Double underlining

[[Double boldface brackets]]

* * *

Heading or defined term.

Added to existing law by original bill.

Deleted from existing law by original bill.

Added by amendment.

Deleted from existing law or the bill by amendment.

Existing law unaffected by bill.

The County Council for Montgomery County, Maryland approves the following Act:

1 **Sec. 1. Section 33-60C is added and Sections 33-61A and 33-165 are**
 2 **amended as follows:**

3 **33-60C. Fossil Fuel Investments – Restrictions**

4 (a) Definitions. In this Section, the following words have the meanings
 5 indicated:

6 Actively managed separate account means assets held in a separate
 7 account by an investment manager hired by the Boards. Actively
 8 managed separate account does not include an index fund, private equity
 9 fund, real estate fund, mutual fund, or other commingled or passively
 10 managed fund.

11 Boards means the Board of Investment Trustees established by Section
 12 33-59 and the Consolidated Retiree Health Benefits Trust Board of
 13 Trustees established by Section 33-160.

14 Company means any sole proprietorship, organization, association,
 15 corporation, partnership, joint venture, limited partnership, limited
 16 liability partnership, limited liability company, or other entity or business
 17 association, including any wholly-owned subsidiary, majority-owned
 18 subsidiary, and parent company of any of them, or business association,
 19 that exists for profit-making purposes.

20 Divest means selling, redeeming, transferring, exchanging, or otherwise
 21 disposing of, and refraining from further buying of, certain investments.

22 Fossil Fuel Company means a company listed in the 200 publicly traded
 23 coal, oil, and gas companies that hold reported fossil fuels reserves with
 24 the largest potential carbon emissions, as ranked in the Fossil Free
 25 Indexes US (FFIUS) published by Fossil Free Indexes LLC or a successor
 26 index, as updated annually.

27 Trust funds means the assets held for the Employees' Retirement System
 28 and the assets held for the Consolidated Retiree Health Benefits Trust.

29 (b) Review of investments. Each Board must review the investment holdings
 30 in each actively managed separate account of the trust funds and identify
 31 each investment in any fossil fuel company. Each Board must review its
 32 investment holdings in these accounts periodically and update the list of
 33 fossil fuel companies at least every 6 months.

34 (c) Divestment. Except as provided in subsection (d), each Board:

35 (1) within 1 year after the date this law takes effect, must divest at least
 36 20% of its investments in fossil fuel companies held in an actively
 37 managed separate account as of the date this Act takes effect:

38 (2) within 2 years, must divest at least 40% of its investments in fossil
 39 fuel companies held in an actively managed separate account as of
 40 the date this Act takes effect;

41 (3) within 3 years, must divest at least 60% of its investments in fossil
 42 fuel companies held in an actively managed separate account as of
 43 the date this Act takes effect;

44 (4) within 4 years, must divest at least 80% of its investments in fossil
 45 fuel companies held in an actively managed separate account as of
 46 the date this Act takes effect; and

47 (5) within 5 years, must divest 100% of its investments in fossil fuel
 48 companies held in an actively managed separate account; and

49 (6) must not make any new investment in an actively managed
 50 separate account in any fossil fuel company.

51 (d) Divestment delay. Nothing in this Section must require a Board to take
 52 action as described in this Section unless the Board determines in good
 53 faith that the action described in this Section is consistent with the

54 fiduciary responsibilities of the Board described in Section 33-61C or
 55 Section 33-163. If the Board determines that a delay in divesting from a
 56 fossil fuel company is necessary due to its fiduciary duty, the Board must
 57 report this delay within 30 days to the Executive and the Council along
 58 with an estimated timeline for the resumption of divestment.

59 (e) Research on socially responsible investing. Each Board must:

- 60 (1) review academic and professional literature on socially
 61 responsible investing;
- 62 (2) investigate the benefits and disadvantages of socially responsible
 63 investing of public trust funds; and
- 64 (3) adopt a Socially Responsible policy for investments.

65 (f) Exemption. The divestment or investment prohibition under this Section
 66 must not apply to a company that can demonstrate that it:

- 67 (1) has stopped exploring for new hydrocarbons;
- 68 (2) agrees contractually to not develop or sell 80% of its current
 69 proven fossil fuel reserves; and
- 70 (3) has stopped lobbying or attempting to influence government
 71 officials to preserve its special treatment, including subsidies, tax
 72 breaks, or competitive advantage with respect to clean, renewable
 73 energy.

74 (g) Notice. Each Board:

- 75 (1) before divesting from a fossil fuel company under this Section,
 76 must provide written notice and an opportunity to comment in
 77 writing to each company subject to the action;
- 78 (2) must not divest until 90 days after written notice is provided to the
 79 company; and

80 (3) must not divest if the company shows that it is exempt from
81 divestment under subsection (f).

82 (h) Report. The Board must report annually to the Council and Executive on
83 the operation of and compliance with this Section. The report must:

84 (1) identify each investment in a fossil fuel company held in an
85 actively managed separate account of the trust funds;

86 (2) list each divestment action taken under this Section

87 (3) describe each decision to delay investment under Subsection (d);
88 and

89 (4) calculate the administrative cost of compliance.

90 **33-61A. Indemnification of trustees**

91 (a) *Authorized.* The County must indemnify every member of the Board who
92 is or may become a party to any action, suit, or proceeding, including
93 administrative and investigative proceedings, because of service as a
94 member of the Board, including any action taken to comply with
95 [Section] Sections 33-60A and 33-60C, subject to the conditions stated in
96 this Section.

97 * * *

98 **33-165. Indemnification of Board Members.**

99 (a) *General.* The County must indemnify each member of the Board who is
100 or may become a party to any legal action, including any administrative
101 or investigative proceeding, because of service as a Board member,
102 including any action taken to comply with Sections 33-60A and 33-60C,
103 subject to the conditions in this Section.

104 * * *

105 **Sec. 2. Initial review.** Each Board must complete its initial review of the
106 investment holdings in all actively managed separate accounts of the trust funds and

107 identify all investments in fossil fuel companies within 90 days after the date this Act
108 takes effect.

109 *Approved:*

110

Nancy Floreen, President, County Council

Date

111 *Approved:*

112

Isiah Leggett, County Executive

Date

113 *This is a correct copy of Council action.*

114

Linda M. Lauer, Clerk of the Council

Date

LEGISLATIVE REQUEST REPORT

Bill 44-16

Retirement – Fossil Fuel Investments - Restrictions

DESCRIPTION: Bill 44-16 would restrict the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board of Trustees from investing in certain businesses holding the largest amount of fossil fuel reserves under certain circumstances. The Bill would also require both Boards to research and adopt a socially responsible policy for investing.

PROBLEM: Investing in fossil fuel companies is inconsistent with the County's established policies to be environmentally responsible.

GOALS AND OBJECTIVES: Encourage fossil fuel companies to move into more environmentally responsible renewable energy sources.

COORDINATION: Board of Investment Trustees, Office of Human Resources, County Attorney.

FISCAL IMPACT: To be requested.

ECONOMIC IMPACT: To be requested.

EVALUATION: To be requested.

EXPERIENCE ELSEWHERE: To be researched.

SOURCE OF INFORMATION: Robert H. Drummer, Senior Legislative Attorney

APPLICATION WITHIN MUNICIPALITIES: Not applicable.

PENALTIES: None.

MEMORANDUM

October 11, 2016

TO: Council President Nancy Floreen
Council Colleagues

FROM: Council Vice President Roger Berliner
GO Chair Nancy Navarro

SUBJECT: Fossil Fuel Divestment and Socially Responsible Investing

Colleagues, we are writing to ask for your support for legislation we plan on introducing that more closely aligns our values with our role as a major financial investor of nearly \$4 billion -- *without sacrificing the returns on those investments*. We would do this in two distinct ways: (1) directing the county's Board of Investment Trustees (BIT) to divest from the 200 publicly traded fossil fuel companies that hold reported reserves with the largest potential carbon emissions; and (2) directing the BIT to study adopting a Socially Responsible Investing screen for its portfolio.

We are proposing this measure fully aware of the Board's fundamental fiduciary responsibilities. Our legislation would address this explicitly by allowing the BIT to waive the divestment requirement if the Board were to certify to the Council that in its judgment alternative investments in non-fossil fuels are not available that would meet or exceed the returns of the \$65 million in fossil fuel stocks currently in its portfolio. Given the strength of portfolios without fossil fuels, and the relatively poor performance of fossil fuel stocks, we are confident that the Board will be able to harmonize our county's values with its fiduciary duties.

We are also very mindful of the "slippery slope" argument – i.e., that there are a host of serious moral and ethical issues that have been put forward over the years as a justification for divestment, and we have said no. We believe climate change is different: it represents an existential threat to the entire planet. It is, in our view, in a class by itself, and its correlation with the companies principally responsible for creating climate change is direct. We know it is caused by the burning of carbon-heavy oil, coal, and natural gas. It is why our Council has passed literally dozens of measures to support clean energy and energy efficiency. We should not be investing in the very companies that undermine our commitment to sustainability.

Specifically, this legislation would prohibit the BIT from purchasing any new stocks or bonds in the fossil fuel industry and phase in over a 5 year time line divestment of the \$65 million worth of holdings in the coal, oil and gas companies in the Carbon Underground 200, a list of fossil fuel companies ranked by their potential carbon emissions. As noted, the 5 year phase-in would be subject to an off-ramp if the Board can certify divesting these funds would reduce the return of the portfolio.

More broadly, this legislation would also address longer term issues related to how we invest our money by requiring the BIT to study the impact on its portfolio of adopting a Socially Responsible Investing (SRI) approach, expanding on its current policies in this area. This approach considers environmental, social and corporate governance issues in determining whether to make an investment while seeking to maintain strong returns for investors. It is widely used today by investors: more than \$6.57 trillion in the United States is already invested using socially responsible practices.

SRI is based on the belief that we should use our investments to bring about positive change by aligning our investments with companies that achieve good returns by being a good corporate citizen. Given the ever increasing role corporations have in our world today, exercising that prerogative is important. The latest example of this can be seen in the Wells Fargo scandal in which more than 2 million bank accounts or credit cards were opened without customers' knowledge or permission. An SRI "screen" could result in shifting investments from companies like Wells Fargo to more socially responsible companies, and that would be a good thing.

We thank you in advance for your consideration of this legislation and we look forward to working with you as it moves forward.

Roger Berliner



Council Vice President

Nancy Navarro



Chair, GO Committee