The Facts about Fossil Fuel Divestment

Divestment is one of the most powerful statements that an institution can make with its money. It helps remove the social license that allows the fossil fuel industry to continue to emit dangerous pollutants into the atmosphere at low cost.

The fossil fuel industry's business model depends on its ability to burn all of the carbon in its reserves. To stay below 2 degrees Celsius of warming, scientists and economists say we must leave 80 percent of the current coal, oil and gas reserves in the ground. Simply put, to avoid the most catastrophic effects of climate change we can only burn less than 500 gigatons of carbon, while the fossil fuel industry currently holds 2,860 gigatons in its reserves.

Our generation has a moral imperative to address climate change in a manner that is consistent with the urgency and severity of the crisis. Colleges and universities, for example, exist to educate new generations of young people. Pension funds exist to support the long-term health of their pension holders.

The following facts, used in conversations with college administrators, pension trustees, finance professionals and other thought leaders we encounter in the divestment effort, can be helpful in debunking common misperceptions about fossil fuel divestment:

1. Fiduciary duty demands fossil fuel divestment

Fiduciary responsibility, or fiduciary duty, is a legal term meaning that trustees must act in the best interest of the institution. For many institutional investors, this is interpreted to mean maximizing short-term returns at the expense of all other factors. Many administrators justify a policy of continuing to invest in fossil fuels by stating that any other course of action would be breaking their legal responsibility.

This interpretation of fiduciary duty is a fallacy, as the Securities and Exchange Commission and courts have repeatedly ruled that as long as a portfolio is diversified, it is acceptable to have a non-passive investment strategy, where some investments lose money and some gain money. Further, experts have declared that fiduciary responsibility includes a long-term risk assessment, and investing in climate change is not in the interest of the beneficiaries. An institution has both the opportunity and the obligation to recognize that fiduciary responsibility means looking beyond immediate, short-term, unsustainable and morally untenable ways of generating profits and returns.

Furthermore, disregard for the science of climate change could indicate a poor financial manager. As financial expert Bob Massie says, “Contempt for the science of climate change could very well be considered an indication of a management so woefully out of touch with reality as to cast doubt on their capacity to manage a large enterprise."

2. Shareholder engagement is the wrong tactic for achieving meaningful change in this case

Sometimes shareholder resolutions are effective avenues for change, but the fossil fuel industry is different. Their business plan is inherently flawed since it is based on burning more than five times the maximum amount of carbon established as the limit for keeping global climate change beneath 2 degrees Celsius.

These companies plan to burn this carbon, and indeed their stocks are valued on this assumption. Shareholder engagement is a strategy used to change a company's policies, not their business models.

Divestment campaigns work in part by removing the social license as well as the economic and political power that will allow the companies to continue to burn the carbon in their reserves. Our institutions must draw a hard line against an industry whose actions result in the degradation of communities across the planet, and the destabilization of our climate. They must say that they refuse to profit in the short-term from a business model based on wrecking the planet.

In order to make an economic transition away from fossil fuels, the business model of fossil fuel companies must be shown to be unprofitable, and we must generate consumer demand for alternatives. Neither of those goals can be achieved with shareholder engagement. Even with this information, some institutions have chosen, while divesting, to hold the minimum shares ($2000 worth of a company according to the SEC) in a company to continue to file shareholder proposals.

3. Research and advocacy support divestment, but can't replace it, and fossil fuel companies are not looking for renewable energy solutions

Congress is deadlocked and our political system is rigged to benefit fossil fuel companies. We have marched on Washington, protested at our Senators' and Representatives' offices, and will continue to do so to push for carbon regulation. But to win real legislative efforts, we need to take the power away from the fossil fuel companies so they can no longer dictate our national energy policy. Divestment is a way to both economically, socially and politically marginalize the fossil fuel industry and to build a movement large and powerful enough to overcome their millions of dollars in campaign contributions.

Divestment also means the opportunity for re-investment. As the endowment or institution sells off any fossil fuel holdings a portion of that money can be re-invested in climate solutions making a positive impact in the developing clean tech sector or local infrastructure, for example.

While research is an important part of advancing climate change solutions, we also must create space to implement our research. The responsibilities of our research institutions are not only to advance research, but also to use that research to positively impact the world around us.

We must take on the myth that fossil fuel investments are necessary for profitable portfolios, which is no longer the case. Fossil free portfolios making competitive returns. Further, fossil fuel companies, whose business models are tied to burning fossil fuels, have no reason to fund research into climate solutions except to save face and give the impression that they are looking at alternative fuels, when they spend much more money each year on exploring for new, increasingly unsafe, fossil fuel sources to burn (see question 5 below).

4. Divesting will make a difference

College and University investments are a reflection of their institutional values. Cities and state government investments are a reflection of the values of our communities. Both educational and government institutions are looked to for leadership on important issues.

By investing in fossil fuel companies, we actively sponsor climate change. We actively add to the market confidence in a profitable financial future for the fossil fuel industry. Universities and Pension Funds are

leaders in the investment space. As they move their money other investors will begin to follow, amplifying the impacts of divestment.

Public pension funds are some of the largest pools of public money in the country, as investors they are trendsetters and leaders. They are also responsible for the future livelihood of many in the US—which makes it doubly-important that they remove their investments from overvalued fossil fuels, often referred to as “the carbon bubble.” The more pension funds who address this risk, the more steps we can take toward a fossil fuel free economy while protecting the returns of these funds from the carbon bubble.

If institutional fund managers are compelled to change their policies by universities and colleges, this will create more opportunity for other investors to do the same. By becoming familiar with fossil free investment products, there is the opportunity for fund managers to share those opportunities with other clients, and to advertise those services.

After comparing the fossil fuel divestment movement to other divestment movements, the University of Oxford Smith School found that the fossil free movement is growing faster than any other in history, and the stigmatization of these investments that it is creating will have long term financial effects on the fossil fuel industry.

5. The fossil fuel industry’s economic interests do not align with the development of renewable energy infrastructure

The fossil fuel industry is at odds with the developing cleantech infrastructure needs. Contrary to what many institutional investors and college administrators have argued, the deep-pockets of fossil fuel companies are continuing to invest heavily in expanding fossil fuel use, not curtail it. In past decades, fossil fuel companies have shown little to no interest in shifting their business models away from extraction, and have lobbied heavily to keep their monopoly on the world’s energy systems.

Companies like BP are decreasing investments in clean energy instead of increasing them. In addition, because of the growing risk of a “carbon bubble,” a number of studies show the potential decline of companies with carbon intensive operations in coming years. Fossil fuel companies commit the bulk of their resources for new projects not on renewables, but on exploring for more fossil fuels to burn.

In 2013 the top 200 fossil fuel companies allocated up to $674 billion for finding and developing more fossil fuel reserves and new ways of extracting them.

BP or "Beyond Petroleum" sold off its entire wind and solar energy investments in 2011, In 2007 Shell hit a high of 2.5% invested in "alternative energy" today it's down to 1.5%, same story with Chevron (2008 2.5%, now 1.5%), ConocoPhilips and Philips 66 have no reported alternative energy investments. According to Sustainalytics, 75% of the 200 list have no evidence of clean-tech revenues.

Make no mistake, Exxon could still make a profit as an energy company if it transitioned its massive wealth and expertise over to renewables, but they’ll do it because of government regulation, not because they willingly decide to completely change their existing profit models. And getting that regulation passed is exactly why the stranglehold of the fossil fuel industry must be broken.

6. Fossil fuel divestment decreases portfolio risk and does not mean portfolio losses

On average, fossil fuels make up about five to ten percent of a university's endowment or a pension fund (as the energy sector makes up about 10% of the market). This means a relatively small portion of the endowment's holding will be affected by divestment. Investment managers are beginning to develop fossil free options and as demand grows more fossil free investment products will become available. An immediate freeze on now fossil fuel investments, and divestment over five years allows ample time for managers of any size portfolio to develop alternative investment strategies.

A recent report by the Aperio Group reveals that excluding the top 200 fossil fuel companies from an indexed portfolio would increase theoretical return risk by a mere 0.003%. Aperio Group's data was then confirmed by three independent research firms showing low tracking error with different timelines and benchmarks[1].

Long-term investments in the fossil fuel industry will likely prove to be bad investments. It carries very low risk to the portfolio and hedges against the foreseeable decline in the fossil fuel industry known as the "carbon bubble." If more than 80% of fossil fuel reserves cannot be extracted and burned for profit, they are considered stranded assets, which inflates the value of the companies' stock. These reserves are currently valued at nearly $20 trillion forming a bubble that dwarves the housing tech bubbles that led to past recessions.

- HSBC Global Research found that global carbon regulations could result in fossil fuel companies losing 40-60% of their market capitalization.
- Similar warnings have been issued by CitiBank, Standard and Poor's, the International Energy Agency, and the Bank of England, and most recently the UN Climate Chief
- The head of the IMF gave a speech acknowledging that the fund needs to address climate issues—calling for a reduction in subsidies for fossil fuel companies.
- Also recently, CalPERS (CA pension fund) adopted updated Investment Beliefs that consider the investment risks of climate change to guide its investment policies and ensure the fund's growth.

7. Divesting will protect financial aid programs and student services at colleges and Universities

The return on investment is not the only income that a campus should be concerned with. Campus operating budgets also heavily rely on tuition and alumni donations. Unity College in Maine reported that after they announced divestment they saw a significant increase in donations and interest in the university. Daily campus administrators make choices on how to spend their operating budget to meet numerous different needs. In the case of any hypothetical downturn, the campuses operating budget can be managed in a way that does not sacrifice the mission of the institution. For example, during the recession in FY2009, Brown University's endowment shrunk 29%, yet financial aid increased 10.9%.

Endowments and Pension Funds are some of the longest-term investments in existence, thus should consider long-term risk, not short-term returns. Responsible investment is one of the best means by which to mitigate long-term risk, as it rewards companies and investments that are truly sustainable, and will therefore be profitable in the long-term, not just the short-term. Responsible Investment mitigates long-term risk by identifying potential environmental, social, and governance (ESG) risks before they become portfolio risks. Consider the BP oil spill and the Fukushima nuclear disaster; these catastrophes occurred partially because of environmental and governance failures. Responsible investment addresses ESG risks and factors that conventional investors do not price into investment.

8. Administrators and portfolio managers can easily monitor their portfolio for fossil fuel exposure

A common refrain from administrators or politicians, and even sometimes college presidents or board members is, “we can’t divest because we don’t even know where the money is invested – and even if we did know, we couldn’t make that information public because it would reduce our profits.”

It may be true that they don’t know what stocks or bonds they own at any given moment, but administrators and boards hire the money managers, and thus get to decide where their money is, or isn’t, invested. If they really wanted to divest from fossil fuels, all they would have to do is tell the money managers to do us that.

Institutional investors are beginning to move away from fossil fuels and begin investing in the growing green economy. Foundations like Wallace Global Fund have divested from dirty energy. Two of the nation’s largest pension funds, CalPERS and CalSTRS, have already allocated $1.1 billion into energy efficient infrastructure projects with commitments from the American Federation of Teachers, AFL-CIO, and Clinton Global Initiative to collectively invest $10 billion in the clean energy economy.

It is not the responsibility of the students or community members to develop a full proposal for how and where the institution should re-invest all of the fossil fuel holdings. Ultimately the holdings are directed by the Trustees and board members who can direct their investment managers and consultants to identify alternative investment options.

9. The divestment movement is real, it’s large, and it’s not going away

There are currently divestment campaigns on over 400 University and college campuses and in over 100 cities and religious institutions—and that’s just in the US. To date, there are over 30 cities, 25 universities, and a host of churches (some national) that have already divested or are in process of doing so. There are currently divestment bills in three state legislatures and proposals before financial executives in several more states. The State of Vermont added an optional fossil free retirement option for its employees. In January, 2014, 17 foundations worth $1.7 billion announced they would also be divesting. In September, 2014, another list of foundations announced divestment, including the Rockefellers Brother Fund.

The Country of Norway also agreed earlier this year to review it's largest fossil fuel investments to consider divestment. The city of Orebro, Sweden passed divestment, and the Swedish Pension Fund divested in October, 2014. University of Glasgow was the first endowment to divest in Europe, in October of 2013, followed by Victoria University in New Zealand.

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