

United States Senate

WASHINGTON, DC 20510

August 4, 2016

The Honorable Mary Jo White
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chair White:

As you proceed with the Disclosure Effectiveness Initiative, we write to bring your attention to the attached article about former SEC Commissioner Bevis Longstreth's work on prudence standards under state trusts law. Mr. Longstreth contends that such prudence standards should compel the trustees of not-for-profit institutions to consider climate change concerns in making investment and divestment decisions.

Mr. Longstreth's work shows how the momentum in the investment community has shifted toward greater awareness and consideration of climate-related risks. During the comment period on disclosure effectiveness, you've seen further evidence of this. Notably, a group of 62 institutional investors—including the treasurers of the states of California, Connecticut, Massachusetts, Oregon, Vermont, and Washington—wrote, "a growing number of investors are working to integrate climate risk into their investment strategies, and obtaining more information from fossil fuel companies about their capital expenditures and related risks is a critical part of this process."

It's clear that the investment community increasingly views climate change as a substantial risk and that factors pertaining to climate change—including weather-related and stranded asset risks—are material to investors and necessary for their investment decisions. We ask you to use the Disclosure Effectiveness Initiative as an opportunity to provide investors with greater clarity about investment risks that pertain to climate change.

Thank you for your attention to this letter. As always, we would be pleased to further discuss this topic with you.

Sincerely,


Sheldon Whitehouse
United States Senator


Ed Markey
United States Senator


Barbara Boxer
United States Senator

Will This Retired Lawyer Open the Floodgates of Divestment From Fossil Fuels?



Bevis Longstreth intends a six-page document he's written to provide the key. Don't sell him short, he's done this kind of thing before.

By: David Sassoon
June 8, 2016

Bevis Longstreth, a former SEC commissioner, says his new proposal to state attorneys general for an "interpretive release" and guidance on climate-related risk could open the floodgates of divestment from coal, oil and gas companies. Photo courtesy of Bevis Longstreth

The money managers of university and non-profit endowments owe a debt of gratitude to a lawyer named Bevis Longstreth. He's hardly a household name, but an obscure book he published 30 years ago provoked a modernization of the legal definition of prudent investing that changed their lives for the better.

His work opened the door for trustees of non-profits to make investments that are now at the heart of modern portfolio management. Previously they were out of bounds because they were considered too risky.

"Imagine all the pension funds in this country, and all the institutions like Yale and others, they are all deeply invested in hedge funds," Longstreth said. "When I wrote that book it would have been impossible for them to invest in a hedge fund."

Now Longstreth, 82, is out to rock the world of non-profit money managers again. This time he doesn't have a book, but merely a six-page argument.

His proposal calls for a legal reinterpretation of what constitutes prudent management of institutional funds now that the investment landscape is filled with new risks for fossil fuel investors.

With the world heading toward zero carbon emissions after the signing of the Paris agreement, Longstreth thinks it's time for some fresh guidance.

To that end, he's working channels to convince various attorneys general to spell out those risks in an "interpretive release," and offer guidance on how to handle them. He thinks the attorneys general of New York, Massachusetts and California will be most receptive to his proposal.

If the guidance is published, Longstreth says, it could open floodgates of divestment from coal, oil and gas companies. That's because, as he explains in the extensive interview below, it can't be ignored.

Every state in the union (except Pennsylvania and the territory of Puerto Rico) has its own version of the uniform law governing investments by trustees, known by the acronym UPMIFA. And each attorney general has power to issue guidance on how to exercise prudence under that uniform law.

The question remains whether any attorney general would offer guidance singling out a particular asset class.

Though retired from legal practice and now a three-time novelist, Longstreth brings considerable experience to his latest legal rethink. He was twice appointed by President Ronald Reagan to serve as commissioner of the Securities and Exchange Commission. For decades he was a securities lawyer and partner at Debevoise & Plimpton, a prominent international firm.

He wears wire-rimmed glasses, carries degrees from Princeton (B.S. 1956) and Harvard (LL.B 1961), and has a careful manner of choosing words precisely.

We spoke with Longstreth about his career, his latest legal effort, and how it could provoke change.

ICN: Your career included being a commissioner of the SEC. How were you chosen and how would you characterize your tenure?

Longstreth: I served in the SEC from 1981-1984. I was appointed by President Reagan to a shortened term to fill out somebody who had retired, and then Reagan reappointed me to occupy a Democratic seat on the commission. I think for President Reagan I was not an obvious choice, given my political background, but I was chosen because Jim Baker [Reagan's former chief of staff] wanted me there.

ICN: What was your political background?

Longstreth: I'm a liberal Democrat in almost every respect, whatever that means today. I was very active in opposing the Vietnam War—I designed T-shirts and marched in Washington on more than one occasion, and I was politically involved with the Concerned Democrats of Westchester [in New York] and Putnam County. I suppose that would identify me as a liberal Democrat.

I don't believe in overdone federal economic regulation. I think sometimes we overdo it, but I do believe in a real safety net for the less fortunate of our people.

I suppose the most significant accomplishment that you can point to was when the general counsel and I spearheaded an effort to get legislation to seriously punish insider trading. Until we got going on this project, the SEC was content, if they caught someone insider trading, to simply ask to give back their winnings, but that was it.

There was no financial penalty at all except to have to give up what you illegally obtained. So we went to Congress. We drafted legislation and it was signed into law, imposing treble damages on anyone who was found to be trading on inside information.

ICN: And then?

Longstreth: I started as a lawyer at Debevoise & Plimpton when I graduated from law school in 1961. I became a partner and had a very interesting practice. And then in 1981 I went to the SEC, and then when I came back in 1984, I stayed at that firm until 1993 and started teaching at Columbia Law School. I just published my third novel, too.

ICN: You mention you had an interesting practice. Did it have to do with fiduciary responsibility and evolving standards of prudent investing?

Longstreth: I ended up writing a book on prudence to try to change the law, and that did come about through my practice because I represented institutions like the Ford Foundation. That was one of my major clients, and they were subject to prudence standards, and the advice they were getting from lawyers was very conservative advice, based upon antique notions of prudence.

The seminal case in the whole field of fiduciary conduct—for people who invest other people's money—was called *Amory v. Harvard College*, which was decided in the Supreme Judicial Court of Massachusetts in the 19th century. It was a terrific case in talking about prudence, because it created an elastic standard that basically said honest, unconflicted and informed judgment is all we can ask.

That was the beginning of the law of prudence, but in the 20th century it very quickly became a matter of legal lists, so that for example, mutual funds were prohibited. You couldn't invest in them.

It was a crime to short sell. The hedge fund managers today would be amused by that. It was considered grossly imprudent, *per se*.

A second mortgage was, *per se*, imprudent. It was that sort of thing—labeling products as *per se* speculative and therefore imprudent.

So this book that I ended up writing in 1986 was designed to change that law. And I got into all that because I kept bumping into these doctrines. And at the time, the Ford Foundation in particular wanted to be a leader in new thinking about investments, and this old law just really got in their way, as it got in a lot of people's way.

ICN: There was interest from the endowments at Columbia, Harvard, Princeton and Stanford, right?

Longstreth: Those university endowments, plus the Ford Foundation, Carnegie and a couple of others, paid for the study [specifically, the Alfred P. Sloan Foundation, William and Flora Hewlett Foundation, and the Rockefeller Foundation].

ICN: What did this book lead to?

Longstreth: So the book led almost immediately to a decision by the American Law Institute. They keep an up-to-date version of the law as cases come along and things evolve. And they keep a Restatement of Trusts. It's in that body of legal analysis that the prudence standard comes into play and they decided to use the book to form a platform for updating the law of prudence. They rewrote it.

ICN: Did it help the Ford Foundation and university endowments?

Longstreth: It helped them immensely. It gave them the protection of a legal opinion. Until this restatement came along they couldn't get that protection because the law had not kept pace with the evolution of finance economics.

Imagine all the pension funds of this country and all the institutions like Yale and others, they are all deeply invested in hedge funds. When I wrote that book it would have been impossible for them to invest in a hedge fund.

ICN: So let's fast forward to this interpretive release you want from the attorneys general. What kind of entities would use it? Universities, foundations and pension funds?

Longstreth: No, not pension funds. The law, the Uniform Prudent Management of Institutional Funds Act (UPMIFA) applies to institutions that are not for profits, but it does not apply to pension funds. The pension fund world is governed by ERISA and the Department of Labor, but not by this law. However, there is enormous similarity in the treatment of the word "prudent" in the two bodies of law.

ICN: In other words a development in UPMIFA would have influence over ERISA?

Longstreth: Absolutely. Good lawyers trying to interpret the ERISA standard of prudence would immediately start to quote this law. It's the same word, same meaning, same idea.

The critical idea is that prudence by a fiduciary managing other people's money requires care, skill, but also caution, and that's very different from the board of directors of a for-profit company. They're not supposed to be cautious, they're supposed to be out there taking risks. They have to, to be successful. But in the management of an endowment, caution is important. It is a very vital and fundamental distinction.

ICN: Has the law kept pace with the reality of climate change, and notions of what constitutes prudence and caution?

Longstreth: Climate change is such a traumatic, transcendent issue for the globe. Investors don't know what to make of it.

Since the Industrial Revolution and the discovery of oil, the economies of the world have been driven by the exploitation of oil. The world made these enormous leaps of advancement through the use of oil. Of course it would belong in a portfolio, with that kind of growth since the Industrial Revolution.

So it's simply not easy for investment managers. It is not easy for lawyers trying to help them, to say 'hey, I don't want to hold these things anymore.' It's a big wrenching decision to make, based upon history.

What's needed is some help that specifically addresses the totally unique conditions that we are in now.

ICN: What would an interpretive release do?

Longstreth: For starters, it would compel those subject to this law to be very well-informed, much better informed than they are today, in considering the growing number and depths of risks that are going to arise, and have arisen, from the climate change phenomenon.

Another thing is that the interpretive release could emphasize that embedded in this law is an overriding command—really, that the purposes of the institution and the purposes of the institutional fund have to be taken into account.

That's a fundamental duty. That requirement—which is described as the charitable purpose doctrine, and which in this law is described as a fundamental duty—means that there are certain kinds of investments that, even if they are terrific, you can't hold.

ICN: Because it goes against your charitable purpose?

Longstreth: Yes. Take the Ford Foundation making enormous grants to preserve the great forests of California, and doing that through support of the Sierra Club, and at the same time Ford is invested in a company that's betting the ranch on being able to wipe out those forests.

UPMIFA not only suggests you should not do that, but also that you're breaching your duty if you do.

If I were running a large university, like Columbia or Harvard, I would have to think very carefully about whether I'm not violating the law by holding these things.

The point of the release would be to highlight the need to take the purpose of the institution into account.

ICN: Let's say the Massachusetts attorney general issues an interpretive release along these lines, does it immediately put pressure on Harvard and MIT to divest from fossil fuels, for example?

Longstreth: Yes, it's addressed directly to them. It's like a telephone call directly to Drew Faust [the president of Harvard] saying, 'hey, you are subject to the law we administer and enforce, and here's what we think it means in regard to your portfolio of fossil fuel companies.'

And then by indirection it would apply to Stanford and the University of Texas, and Princeton University, even though they are in other states, because the law is uniform. And you'll influence the SEC, because again they'll be caught with their pants down, doing nothing, when they ought to be leading the charge.

ICN: What if an attorney general that is not disposed to taking climate change seriously—like the one in Texas—gets wind of this and issues his own interpretive release in a different way?

Longstreth: That can happen. I don't know. That creates a split of authority like you get in the district courts. There's no Supreme Court here to decide things, I guess. But it doesn't diminish the value very much. It will bring more attention to the issue. The more attention to the issue you can get, the better.

This release would indicate that before trustees bet against Paris—which is after all what they are doing, when they buy Exxon today, they're betting against Paris—before they do that, they have to satisfy a very high burden.

If Paris is achieved—in other words, if we are going to be successful in holding warming to 2 degrees or 1.5 degrees—there's no way that the reserves now booked and proven can be burned. In fact about 75 percent of them can't be burned. Literally can't be. That's determinable. And if it's determinable, then what about the pricing of Exxon today? How could it not be overpriced?

So the attorneys general need to say if you are going to bet against Paris, you better know what you are doing, have a very good reason for it.

My view is that some day, not too far down the road, it will be almost imprudent, *per se*, to invest in a fossil fuel company that has no particular plan except to keep developing and selling. If you don't exercise prudence, then you're negligent. It's negligence.

ICN: Can this really succeed in the way that you describe?

Longstreth: I would have very little doubt that it would succeed if it's published. It will have a very large impact if something along these lines is issued.

In the simplest terms, it's shifting the burden of proof.

Imagine the chief financial officer of Columbia calls up his money managers and says, 'Look, something's just happened. We can't just assume anymore that from an economic point of view, it looks like a good investment to go into oil and gas companies. We can't assume that anymore. The burden is shifted on us. If you want to do that for our portfolio, you have to give us a written justification for it that goes into a lot of depth, and you'll have to look at this release to see all the different risk factors you have to consider.'

The efficiency of an interpretive release rather than trying to go sue somebody is immense.

ICN: What do you say to the Exxons of the world that say 'there's no problem investing in our stock, our assets are not going to be stranded?'

Longstreth: In terms of this release, an investor who wants to invest in Exxon has to really understand that statement and the basis for it, and the state and direction of the world. To accept that statement is to bet against Paris, to bet against the globe.

Is it really sensible for a stockholder to buy at a price that assumes that they will be able to sell every last drop of oil they have on their books? Isn't that real risk?

Since 2011, the coal industry lost 92 percent of its market cap.

Once it starts to really change—when you hit a tipping point—it's too late to get out of the stock. This is a dramatic case where it's better to be early than late.

ICN: What are your board affiliations?

Longstreth: I was on the board of three money management firms—TIAA-CREF, INVESCAP and GMO—but I'm not on any of them now. I'm too old. I was thrown off of all of them for age.

ICN: What about the Rockefeller Family Fund?

Longstreth: I was chairman of what's called the finance committee there for many years, but now I'm just a member of that committee. I've been there forever.

ICN: Were you involved in the decision for divestment of RFF's endowment from fossil fuels?

Longstreth: Yes, I certainly was. I was also principally involved in the decision at the New School to divest.

I'm a zealot for divestment from all fossil fuel companies.

I would make an exception for a fossil fuel company that has publicly and aggressively acted to help achieve the Paris goals. The only prospect for any company doing that in my opinion among big oil and gas is Statoil in Norway. They have a very good value system, which extends to a responsibility for the welfare of the world as well as the welfare of Norway.

ICN: Are you just an activist trying to undermine jobs and prosperity? Some people who read this are going to say that.

Longstreth: There are many more jobs being created in renewable energy than in the old fossil fuel world.

In any case, that's not the point.

Fiduciaries need to better understand what their duties are in the era climate change, and how to undertake them and satisfy them.