UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
CORPORATION FINANCE

March 25, 2022

Ning Chiu
Davis Polk & Wardwell LLP

Re: Morgan Stanley (the "Company")
Incoming letter dated January 14, 2022

Dear Ms. Chiu:

This letter is in response to your correspondence concerning the shareholder proposal (the "Proposal") submitted to the Company by the Sierra Club Foundation for inclusion in the Company's proxy materials for its upcoming annual meeting of security holders.

The Proposal requests that the board adopt a policy by the end of 2022 committing to proactive measures to ensure that the Company's lending and underwriting do not contribute to new fossil fuel development, consistent with fulfilling the United Nations Environmental Program Finance Initiative recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

We are unable to concur in your view that the Company may exclude the Proposal under Rule 14a-8(i)(7). In our view, the Proposal transcends ordinary business matters and does not seek to micromanage the Company.

We are unable to concur in your view that the Company may exclude the Proposal under Rule 14a-8(i)(10). Based on the information you have presented, it appears that the Company's policies, practices and procedures do not substantially implement the Proposal.

Copies of all of the correspondence on which this response is based will be made available on our website at https://www.sec.gov/corpfin/2021-2022-shareholder-proposals-no-action.

Sincerely,

Rule 14a-8 Review Team

cc: Sanford Lewis

Davis Polk

Davis Polk & Wardwell LLP
450 Lexington Avenue
New York, NY 10017
davispolk.com

January 14, 2022

Re: Shareholder Proposal Submitted by the Sierra Club Foundation

Office of Chief Counsel
Division of Corporation Finance
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Ladies and Gentlemen:

On behalf of Morgan Stanley, a Delaware corporation (the "**Company**"), and in accordance with Rule 14a-8(j) under the Securities Exchange Act of 1934, as amended (the "**Exchange Act**"), we are filing this letter with respect to the shareholder proposal (the "**Proposal**") submitted by the Sierra Club Foundation (the "**Proponent**") for inclusion in the proxy materials the Company intends to distribute in connection with its 2022 Annual Meeting of Shareholders (the "**2022 Proxy Materials**"). The Proposal is attached hereto as Exhibit A.

We hereby request confirmation that the Staff of the Division of Corporation Finance (the "**Staff**") will not recommend any enforcement action if, in reliance on Rule 14a-8, the Company omits the Proposal from the 2022 Proxy Materials.

Pursuant to Staff Legal Bulletin No. 14D (CF), Shareholder Proposals (Nov. 7, 2008), Question C, we have submitted this letter and any related correspondence via email to shareholderproposals@sec.gov. Also, in accordance with Rule 14a-8(j), a copy of this submission is being sent simultaneously to the Proponent as notification of the Company's intention to omit the Proposal from the 2022 Proxy Materials. This letter constitutes the Company's statement of the reasons it deems the omission of the Proposal to be proper.

THE PROPOSAL

The Proposal states:

> RESOLVED: Shareholders request that the Board of Directors adopt a policy by the end of 2022 committing to proactive measures to ensure that the company's lending and underwriting do not contribute to new fossil fuel development, consistent with fulfilling the United Nations Environmental Program Finance Initiative recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

EXECUTIVE SUMMARY

The Company believes that the Proposal may be properly omitted from the 2022 Proxy Materials for the following reasons:

- the Proposal governs the provision of underwriting and lending to specific types of customers, and management's responsibility with respect to managing the Company's products and services constitutes ordinary business that does not transcend social policy;
- the Proposal micromanages the Company's ability to conduct its operations by inherently limiting the Company's lending and underwriting activities toward contributing to fossil fuel development, requiring measures to avoid new financings and also cease all forms of ongoing financings for any other business, in the fossil fuel sector or beyond, that is involved or otherwise indirectly supports contributing to fossil fuel development, and mandating that the Company's approach must be consistent with specified external frameworks. Management is left without appropriate discretion to not only decide its level of engagement with fossil fuel development, but also to determine how best to achieve its climate-focused objectives; and
- the Company has met the essential objective of the Proposal, to disclose how it manages and measures its contributions to fossil fuel development in accordance with recognized third-party frameworks.

REASONS FOR EXCLUSION OF THE PROPOSAL

The Company believes that the Proposal may be properly omitted from the 2022 Proxy Materials pursuant to Rule 14a-8(i)(7) because the Proposal relates to the Company's ordinary business operations and impermissibly seeks to micromanage the Company, and pursuant to Rule 14a-8(i)(10) because the Company has already substantially implemented the Proposal.

I. The Company May Omit the Proposal Pursuant to Rule 14a-8(i)(7) Because the Proposal Relates to the Company's Ordinary Business Operations and Impermissibly Seeks to Micromanage the Company.

Rule 14a-8(i)(7) allows a company to omit a shareholder proposal from its proxy materials if such proposal deals with a matter relating to the company's ordinary business operations. The Staff has consistently stated that the policy underlying the ordinary business exception is based on two central considerations: (i) the proposal's subject matter and (ii) the "degree to which the proposal seeks to 'micromanage' the company by probing too deeply into matters of a complex nature upon which shareholders, as a group, would not be in a position to make an informed judgment." Staff Legal Bulletin No. 14L (Nov. 3, 2021) ("**SLB 14L**"), citing Exchange Act Release No. 34-40018 (May 21, 1998) (the "**1998 Release**"). The Company believes the Proposal is excludable under each of these considerations.

A. The Proposal Relates to the Company's Ordinary Business Operations.

With respect to the first policy consideration reiterated by SLB 14L, the Company believes the Proposal may be excluded from the 2022 Proxy Materials under Rule 14a-8(i)(7) because the Proposal relates to the Company's ordinary business operations.

1. *The Provision of Banking Services, Products and Practices Constitutes the Company's Ordinary Business.*

The Staff has repeatedly concurred with the exclusion of proposals requesting the adoption of a policy or preparation of a report that relate to the activities of the central business of financial institutions, including banks' policies regarding the decision to extend credit or provide other financial services to particular types of clients and other customer relations matters. For example, in *JPMorgan Chase & Co.*(Mar. 12, 2010), the Staff concurred with the exclusion of a proposal requesting that the board publish a report assessing, among other things, the adoption of a policy barring future financing by the bank of companies engaged in mountain top removal coal mining, noting that the proposal related to the company's "decisions to extend credit or provide other financial services to particular types of customers" and that "[p]roposals concerning customer relations or the sale of particular services are generally excludable under rule 14a-8(i)(7)"). In *Wells Fargo & Co.* (avail. Jan. 28, 2013, *recon. denied* Mar. 4, 2013), the Staff also concurred with exclusion of a proposal requesting that the company prepare a report discussing the adequacy of its policies addressing the social and financial impacts of its direct deposit advance lending service, with the Staff noting that "the proposal relates to the products and services offered for sale by the company" and "[p]roposals concerning the sale of particular products and services are generally excludable under [R]ule 14a-8(i)(7)." *See also JPMorgan Chase & Co.* (Mar. 16, 2010) (proposal requesting that the board implement a policy mandating that the company cease its current practice of issuing refund anticipation loans); *Bancorp Hawaii, Inc.* (Feb. 27, 1992) (proposal requesting the company implement a policy mandating that the company refrain from purchasing bonds, making loans and acting as a financial consultant in connection with a particular project).

The Proposal requests that the Board adopt a policy committing to proactive measures to ensure that the company's lending and underwriting do not contribute to new fossil fuel development. As a financial institution, the Company's lending and underwriting services, and managerial decisions around such services, are central to the Company's day-to-day business. As reported in the Company's Form 10-K for the year ended 2020, the Company's more than 68,000 employees operates in 39 countries globally, and lending and underwriting form a significant part of the Company's Institutional Securities core business. Consequently, decisions around the extension of credit or provision of other financial services to particular types of clients who require financing for particular types of projects are fundamental to management's ability to run the Company's business. Because the Proposal relates to the Company's provision of two specific forms of banking services that the Company offers as part of its products and services and the Company's decisions with regard to particular types of customers that should receive those products and services—a subject that the Staff has repeatedly found to be a matter of ordinary business that cannot, as a practical matter, be subject to shareholder oversight—the Company believes the Proposal may be properly omitted from the 2022 Proxy Materials pursuant to Rule 14a-8(i)(7).

2. *The Proposal Does not Transcend the Company's Ordinary Business Operations.*

SLB 14L states that in making the determination on whether a proposal raises a significant social policy issue, the Staff will "focus on the social policy significance of the issue that is the subject of the shareholder proposal" and "consider whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company." The mere fact that a proposal is phrased to reference or invoke issues that could implicate significant social policy issues under the Staff's current interpretation of Rule 14a-8(i)(7) is not sufficient to transcend day-to-day business matters. A proposal may still be excluded when it effectively focuses on an ordinary business matter.

Although the Proposal's supporting statement discusses the societal risks posed by climate change, its underlying subject matter focuses not on this issue, but rather on management's decisions around the

extension of credit or provision of other financial services to particular types of clients. *See JPMorgan Chase & Co.* (Mar. 12, 2010), where the Staff permitted exclusion of a proposal because it "addresses matters beyond the environmental impact" of the company's decisions. The core focus of the proposal is around the type of customers that the Company does business with, and as indicated above, banking activities such as lending and underwriting and customer relations do not transcend the Company's ordinary business operations.

B. The Proposal Seeks to Micromanage the Company by Imposing Specific Methods for Implementing Complex Policies.

Based on the second policy consideration underlying the ordinary business exclusion and reiterated by SLB 14L, the Company believes it may omit the Proposal pursuant to Rule 14a-8(i)(7) because it impermissibly seeks to micromanage the Company.

1. The Level of Granularity Sought in the Proposal Inappropriately Limits the Company's Discretion.

According to SLB 14L, the determination of whether a proposal impermissibly micromanages the Company "will focus on the level of granularity sought in the proposal and whether and to what extent it inappropriately limits discretion of the board or management." Here, the Proposal's high degree of granularity seeks to effectively require the Company to cease providing core business operations to certain types of clients who require financing for particular types of projects, thereby inappropriately interfering with the discretion of the Board of Directors (the "**Board**") and management over fundamental decisions and impermissibly micromanaging the Company.

The Proposal specifically requests that the Board adopt a policy that would "ensure" that the Company stop any ongoing lending and underwriting that it is currently involved in, or not begin any new activities that may contribute to, new fossil fuel development. The Proposal stipulates the precise steps the Company would need to take to satisfy the Proposal's objective with a high degree of granularity, specifying the following parameters:

- **Business Activity**: The resolution targets the type of operations that it does not want the Company to participate in funding through lending and underwriting, namely "new fossil fuel development," a highly specific directive with respect to the forms of business activities that the Proposal is seeking to control. Rather than permitting the Company to determine how to achieve the Proposal's goals, the Proposal mandates that the Company cease specific business activities.
- **Current and Future Timelines**: The Proposal targets not only any of the Company's future business activity in the form of financing of "new" enterprises but also the Company's existing business activity that may be "expanding fossil fuels." The Proposal seeks to impermissibly intrude on management's judgment by forcing the Company to not only avoid entering into new client financings, but also cease providing support for any ongoing projects. It would clearly be more burdensome to suspend or terminate any existing agreements with clients.
- **Methodology**: The Proposal would require the Company to use a particular method, by "committing to *proactive* measures" (emphasis added) targeting the Company's business practices of "lending and underwriting." The Company is expected to "ensure" that these proactive measures avoid "contribut[ing]" to new fossil fuel development, which would mean at minimum that the Company must first determine what it means for something to "contribute to new fossil fuel development." The depth of the mandate would capture financing companies that manufacture products used in oil and gas operations, including not only direct equipment but also as wide ranging as software companies

and auto manufacturers. In addition, underwriting a bond issuance for a company may implicate the Proposal since the proceeds are often used for general corporate purposes. These examples demonstrate that the Proposal would require the Company to continually monitor and assess whether business activities that do not currently involve fossil fuels would implicate such development, and then stop those practices before they can be initiated, for both new business arrangements and ongoing transactions. The scope of "contribut[ing]" to fossil fuel development is particularly granular in terms of the Proposal's directive to the Company. While the Company engages in a wide range of business activities that make funding available to clients, the Proposal is specific in identifying the exact forms of policies that the Company should adopt.

- **Frameworks**: The Proposal would dictate the exact standards by which the Company would need to assess the end results of its objective, stating that the proactive measures adopted by the Company must be "consistent with *fulfilling*" (emphasis added) certain specifically enumerated frameworks. For instance, the Proposal cites the International Energy Agency's Net Zero Emissions by 2050 Scenario (the "**IEA 2050 Scenario**"). This scenario is just one of several that the International Energy Agency has published,[1] and one of dozens issued by the various agencies and organizations that are providing these scenarios. The Proposal also cites the United Nations Environment Programme Finance Initiative (the "**UNEPFI**") recommendations to the G20 Sustainable Finance Working Group. This UNEPFI framework consists of 11 specific recommendations to financial institutions, including to: (i) align with science-based targets specified in the framework; (ii) align as soon as possible (and not by end of 2022, as specified in the Proposal) and establish near-term (per the framework, ideally five-year) targets; and (iii) cease financing of new fossil fuel developments.
- **Near-Term Deadline**: The Proposal would require the Company to adopt such a policy "by the end of 2022."

This level of granularity sought in the Proposal would impermissibly eliminate the discretion of the Board or management with respect to certain fundamental ordinary business matters. For the Company to effectively implement the Proposal, the Company would have no discretion over the Proposal's specific focus on "new fossil fuel development." The Company would also not have any discretion over the timing of its implementation, the decision of whether to gradually discontinue or completely cease business activities, the nature of the business activities it would need to cease entirely, the methodology used to do so and the standards by which to measure its success.

In addition to micromanaging the Company's business activities, the Proposal also inappropriately prescribes the manner in which the Company intends to implement its commitments, which are discussed in more detail in Section II of this letter. The issue of climate change and the transition to a low carbon economy is complex, and the Proposal prescribes one specific way for the Company to contribute to the low carbon economy: ceasing to provide any lending and underwriting services to its customers, which the Proposal implies is necessary to help ensure that no new oil and gas development occurs and that no further "contribut[ion]" to further fossil fuel development will be made by the Company to the extent there are activities already initiated. The Proposal seeks to impose this specific policy even in light of the Company's existing commitments, and imposes a specific method that limits the Company's discretion to exercise its judgment. In addition, the Proposal also demonstrates another assumption: that no new fossil fuel development will be required under the IEA 2050 Scenario, and that the way to ensure there is no such new development is for the Company to cease this form of underwriting and lending activities. However, as discussed further below, even under the IEA 2050 Scenario, some degree of new fossil fuel development

[1] For example, the International Energy Agency has also published the Stated Policies Scenario and the Sustainable Development Scenario.

will be necessary, and therefore the Company is best positioned to make decisions with respect to its commitments.

The Proposal's "one size fits all" approach to the complicated objective of reducing fossil fuel emissions does not leave room for management, in the course of its ordinary business day-to-day responsibilities, to weigh the complex variables that are needed in deciding to enter into new businesses, or increase or decrease its existing obligations, nor does it give the Company the flexibility necessary to analyze whether the solution requested by the Proposal is truly the best way for the Company to contribute to a low carbon economy. As mentioned above and discussed further below, funding some degree of new fossil fuel development is not inherently incompatible with the IEA 2050 Scenario because continued use of oil and gas will be required during the period of the transition to a low carbon economy. In particular, as older oil and gas operations reach the end of their useful life, investments in new oil and gas development could be necessary for a period of time. Based on the Company's estimate, many companies in the oil and gas industry are expected to increase production in the near term. The Proposal does not give management the latitude to exercise its discretion and to analyze such variables that are fundamental to its responsibilities to run the business, including with respect to the transition to a low carbon economy, in a manner that is in the best interests of the Company.

In addition, such a blanket policy could have complex and unintended follow-on effects that are not considered by the Proposal; for example, even if the Company takes the exact steps requested by the Proposal, other financial institutions with more flexible lending and underwriting standards may step in to provide such services. In fact, the UNEPFI, one of the frameworks cited by the Proposal, makes this exact point when it notes that:

> A financial institution can focus on eliminating emissions from its portfolio as soon as possible, however, concerns arise that when employing this approach of rapid and blanket divestment, that a less environmentally-conscious investor, insurer or loan provider, would step in to provide financing. The opportunity to engage the real-economy company is then transferred from the financial institution seeking to align its own portfolio, to one which is less concerned with contributing to the achievement of the wider societal goals at hand (in this case agreed climate goals).[2]

Management must also be prepared to address competing stakeholder interests in its efforts to achieve the Company's low carbon objectives, as different states have also become involved in attempting to influence how banks like the Company are financing fossil fuel activities. For example, in November 2021, the West Virginia Office of the State Treasurer (on behalf of West Virginia and 15 other U.S. states) raised concerns regarding "the ongoing and growing economic boycott of traditional energy production industries by U.S. financial institutions" in a letter to various participants in the U.S. banking industry.[3] The letter announced that these states would consider various measures in response to attempts by banks to limit or otherwise restrict the funding and extension of credit to the fossil fuel industry by financial institutions, including by requiring financial institutions "to certify, as a minimum qualification in all future Requests for Proposals (RFPs), that the institution is not engaged in a boycott of fossil fuel companies." In Texas, state entities will divest from companies that impose restrictions on doing business with such companies. As such, were the Company to adopt the measures requested in the Proposal, it could face potentially material roadblocks to

[2] 2021-UNEP-FI.-Recommendations-for-Credible-Net-Zero-Commitments.pdf (g20sfwg.org), paragraph 15.

[3] Fossil%20Fuel%20Banking%20Letter%20Nov%2022.pdf (wvtreasury.com).

doing business with other clients and in certain states, which could impact the Company's financial performance, and add to the complexity that management must weigh.

The Company recognizes that certain fossil fuel companies understand the scale of the effort needed to address climate change and transition to a low carbon economy and have announced or plan to announce changes to their business models and emissions reporting and reduction targets designed to contribute to the global fight against climate change. The Company believes that it is well positioned to help these companies make progress in addressing climate change, and that the way to do this is to continue its lending and underwriting relationships while using its expertise to support these companies in their transition to a low carbon economy. As noted above, the UNEPFI itself has noted that immediate divestment is not necessarily the correct approach for every financial institution; the UNEPFI has also noted that "[p]ortfolio emissions reductions can be measured and deployed through a variety of approaches (methodologies and metrics), all of which are still evolving."[4]

Because decarbonization is a highly complex topic, the Company has invested in analyzing how its business can best contribute. But the Proposal would require management to adopt a singular approach without taking into account the nuances and complexities of this topic, and for shareholders to make a yes/no decision on a significant aspect of the Company's business without a thorough understanding of those issues. The action requested by the Proposal would have far-reaching consequences that could affect the Company's business decisions, require meaningful resources to properly implement and impact its relationships with customers and other stakeholders, including a significant number of U.S. states. The Proposal's blanket approach also does not account for the global reach of the Company's business; even if limiting or divesting from fossil fuel financing or underwriting makes sense in one country, it may not be the optimal strategy and its impact on the Company's global operations is unclear.

The Company believes that there is a benefit to society in helping companies in the fossil fuel industry transition to the low carbon economy; while the Proposal seems to think that the best way to support such transition is to quickly cease lending and underwriting such companies, the Company's approach is guided by its Environmental and Social Policy Statement ("**ESPS**"), which is reviewed regularly with the Company's Nominating and Governance Committee of the Board of Directors and discussed further below. The Proposal does not provide any evidence that a cessation of the Company's lending and underwriting activities in this sector will lead to the Proposal's intended effect of a halt to new fossil fuel development or otherwise support the transition to a low carbon economy. In sum, the action requested in the Proposal would require an immense amount of analysis and input to manage, tasks that management is best able to assume, including through receiving input from various Company employees, advisors and stakeholders, and the Proposal provides no guidance or flexibility that would allow this necessary process to occur.

Although the Proposal is phrased in terms of "adopting a policy" that would commit the Company to pursuing proactive measures not specifically enumerated therein, if adopted, the Proposal would in fact be prescriptive in that it seeks to "*ensure* that the company's lending and underwriting do not contribute to new fossil fuel development" (emphasis added). In practice, there is only one way to "ensure" this central aim of the Proposal—by requiring the Board or management to effectively eliminate certain business practices of the Company focused on specific types of client activities. This level of granularity in the Proposal would eliminate the discretion of the Board and management over this ordinary business matter and impermissibly micromanage the Company.

[4] 2021-UNEP-FI.-Recommendations-for-Credible-Net-Zero-Commitments.pdf (g20sfwg.org), paragraph 21.

2. *The Proposal Probes Matters "Too Complex" for Shareholders, as a Group, to Make an Informed Judgment.*

The micromanagement element of the ordinary business exception under Rule 14a-8(i)(7) is also based on whether a proposal probes matters "too complex" for shareholders, as a group, to make an informed judgement. SLB 14L, citing the 1998 Release. According to SLB 14L, in making this determination as to whether a proposal probes matters "too complex" for shareholders, the Staff may consider "the sophistication of investors generally on the matter, the availability of data, and the robustness of public discussion and analysis on the topic," as well as "references to well-established national or international frameworks when assessing proposals related to disclosure, target setting, and timeframes as indicative of topics that shareholders are well-equipped to evaluate."

Here, the Proposal references certain specific elements of fossil fuel development and the resolution cites to multiple third-party standard-setting frameworks that are too complex for shareholders to make an informed judgement upon. For example, while shareholders, as a group, may have some awareness around the availability of different frameworks that address fossil fuel contributions to climate change as a general matter, they are unlikely to be in a position to fully grasp the specific concept of how those standards evaluate new fossil fuel developments. It would be even more complex and challenging for shareholders to understand how the Company's lending and underwriting services might play a role in that process.

In addition, the Proposal's specific references to numerous third-party frameworks are complex, and shareholders would be unable to determine if these are appropriate and/or feasible frameworks to use to evaluate the Company when voting for the Proposal. The Proposal cites to each of the following frameworks:

- **UNEPFI recommendations to the G20 Sustainable Finance Working Group**: This framework sets out 11 recommendations for "credible net-zero commitments for financial institutions" to employ "state-of-the-art" practices. The recommendations use, among others, the terms "science-based," "low overshoot," "neutralization of residual emissions," "unique purpose implementation" and "real-economy inventories." These terms are complex, may not have universally accepted definitions and rely on scientific, economic and business knowledge, which many shareholders may not possess. The framework was issued very recently, in October 2021, so whether it is indeed the best or most appropriate framework for the Company to employ is too difficult a question for shareholders to evaluate.
- **IFA 2050**: As discussed above, this scenario is just one of several that the International Energy Agency has published, and one of dozens issued by the various agencies and organizations that are providing these scenarios, including the Network for Greening the Financial System (which has issued climate scenarios that are intended to be used by financial institutions).
- **Banking on Climate Chaos**: The Proposal cites to this March 2021 report by an environmental group. The report, which does not appear to be peer-reviewed, itself contains a disclaimer that its authors do not guarantee the accuracy, completeness or correctness of any of the information or analysis contained in the report.[5]

As a result of these complicated references to third-party frameworks, the Proposal epitomizes micromanagement by probing matters too complex for shareholders to be able to make an informed

[5] The report is available publicly here Banking-on-Climate-Chaos-2021.pdf (ran.org).

judgment upon. Consequently, the Company believes that the Proposal may be properly omitted from the 2022 Proxy Materials pursuant to Rule 14a-8(i)(7).

II. The Company May Omit the Proposal Pursuant to Rule 14a-8(i)(10) Because It Has Been Substantially Implemented.

Rule 14a-8(i)(10) permits a company to exclude a shareholder proposal if the company has already substantially implemented the proposal. The Commission has stated that "substantial" implementation under the rule does not require implementation in full or exactly as presented by the proponent. *See* Exchange Act Release No. 34-40018 (May 21, 1998, n.30). The Staff has provided no-action relief under Rule 14a-8(i)(10) when a company has substantially implemented and therefore satisfied the "essential objective" of a proposal, even if the company did not take the exact action requested by the proponent, did not implement the proposal in every detail, or exercised discretion in determining how to implement the proposal. *See*, *e.g.*, *Salesforce.com, Inc.* (Apr. 20, 2021); *Apple Inc.* (Dec. 17, 2020); *Exxon Mobil Corporation* (Mar. 20, 2020); *Wal-Mart Stores, Inc.* (Mar. 25, 2015); *Entergy Corp.* (Feb. 14, 2014); *Duke Energy Corp.* (Feb. 21, 2012); *Exelon Corp.* (Feb. 26, 2010).

A. The Company's Policies, Practices and Procedures Compare Favorably with the Guidelines of the Proposal.

The Staff has consistently found that "a determination that the company has substantially implemented the proposal depends upon whether [the company's] particular policies, practices, and procedures compare favorably with the guidelines of the proposal." *See* Texaco, Inc. (Mar. 28, 1991) (permitting exclusion on substantial implementation grounds of a proposal requesting that the company adopt the Valdez Principles where the company had already adopted policies, practices and procedures regarding the environment). *See also*, *e.g.*, *BlackRock, Inc.* (Apr. 2, 2021); *JPMorgan Chase & Co.* (Mar. 9, 2021); *Devon Energy Corp.* (Apr. 1, 2020); *Johnson & Johnson* (Jan. 31, 2020); *Pfizer Inc.* (Jan. 31, 2020); *The Allstate Corp.* (Mar. 15, 2019); *Johnson & Johnson* (Feb. 6, 2019); *United Cont'l Holdings, Inc.* (Apr. 13, 2018); *eBay Inc.* (Mar. 29, 2018); *Kewaunee Scientific Corp.* (May 31, 2017); and *Wal-Mart Stores, Inc.* (Mar. 16, 2017).

As an initial matter, we note that even under the IEA 2050 Scenario, the natural rate of decline for existing oil and gas production is such that continued oil and gas development will be necessary to meet the world's energy demands. As older oil and gas sources are wound down, continued investment in newer and more efficient resources will be required for a period of time. As a result, new oil and gas development will be necessary and will occur even under the IEA 2050 Scenario. While the Company supports the transition to a low-carbon economy and the goal of achieving net zero by 2050, the Company will engage with its oil and gas clients to understand their greenhouse gas reduction initiatives and other relevant strategies in the context of the broader net zero goal.

With this in mind, rather than a requirement to fully divest from new oil and gas production (as a plain reading of the text of the Proposal might indicate), the Company instead believes that the Proposal's actual "essential objective" is for the Company's "Board of Directors [to] adopt a policy by the end of 2022" that contains measures relating to fossil fuel development, "consistent with…the International Energy Agency's Net Zero Emissions by 2050 Scenario" and science or science-based targets. Consistent with the overall objectives regarding climate change, the Company reviews its ESPS annually. The ESPS was last updated in December 2020.[6] As described below, the ESPS, as supported by the Company's publicly announced net zero commitments and its 2020 TCFD Report, each of which are publicly available and each of which were adopted by the Company's Nominating and Governance Committee of the Board before the end of

[6] Environmental_and_Social_Policy_Statement_December_2020.pdf (morganstanley.com).

2022, demonstrates that the Company has substantially implemented the Proposal by satisfying its essential objective. Thus, the Proposal may be excluded under Rule 14a-8(i)(10).

The table below succinctly demonstrates how the Company's publicly disclosed policies, reports and other commitments are responsive to the Proposal's request for the Company's "Board of Directors [to] adopt a policy by the end of 2022" that contains measures relating to fossil fuel development, "consistent with…the International Energy Agency's Net Zero Emissions by 2050 Scenario" and science or science-based targets. A more detailed discussion of the disclosures contained in these policies, reports or commitments that address the essential objective of the Proposal is set forth following the summary table.

Proposal request	**2021 ESPS and Other Disclosures**
"Board of Directors adopt a policy by the end of 2022" that contains measures relating to fossil fuel development	ESPS, pages 6-8
"consistent with…the International Energy Agency's Net Zero Emissions by 2050 Scenario"	Morgan Stanley September 2020 press release, page 1 Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), pages 3, 8 and 9
"consistent with"…science or science-based targets	Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), page 5 Morgan Stanley 2020 TCFD Report, page 24

The ESPS previously adopted by the Board Nominating and Governance Committee includes various commitments relating to the Company's financing and other activities with respect to emissions-intensive sectors such as oil and gas, coal-fired power generation and thermal coal mining. These include restrictions on certain activities, enhanced due diligence and other commitments to address the risks that Company activities with respect to these sectors pose. As directly relevant to the Proposal, the ESPS states that the Company "will not directly finance new oil and gas exploration and development in the Arctic, including the Arctic National Wildlife Refuge."[7]

In addition, the ESPS states that the Company committed in 2020 to reaching "net-zero financed emissions by 2050."[8] These commitments are consistent with the Company's membership in the United Nations-convened Net-Zero Banking Alliance.[9] Other public statements by the Company include interim 2030 emissions reduction targets for its most carbon-intensive sectors, auto manufacturing, energy and power, which the Company believes are the most emissions-intensive sectors in its corporate portfolio.[10] These three fossil fuel industry reduction targets are not only consistent with, but are sourced from, the IEA 2050 Scenario requested by the Proposal.[11]

[7] ESPS, page 7.

[8] ESPS, Sections 1 and 4.

[9] "Morgan Stanley Net Zero Target Methodology published November 2021, publicly available at Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), page 10; and ESPS, Stakeholder Engagement.

[10] "Morgan Stanley Net Zero Target Methodology published November 2021, publicly available at Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), pages 1 and 8-10.

[11] "Morgan Stanley Net Zero Target Methodology published November 2021, publicly available at Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), pages 3 and 8.

The Proposal requests that the Policy fulfill the UNEPFI recommendations to the G20 Sustainable Finance Working Group. These recommendations essentially request that financial institutions adopt science-based or science aligned targets to track whether they are on path to reach net-zero by 2050.[12] Indeed, the "financed emissions" targets are "aligned with the science-based International Energy Agency's Net-Zero by 2050 emissions pathways."[13] Specifically, the Company has set its 2030 interim targets as "science-aligned" based on net-zero aligned pathways to be "credible."[14] In addition, the Company publicly discloses in its 2020 TCFD Report that is "providing feedback on SBTI's [or Science-based Target Initiative's] development of a methodology for financial sector emissions reduction targets informed by the latest climate science." The Nominating and Governance Committee of the Company's Board of Directors has reviewed this 2020 TCFD Report[15] in accordance with its charter to "consider environmental, social responsibility and sustainability matters."

Finally, these targets currently apply only to the Company's lending, or financing activities. The Net-Zero Target Methodology document, however, states explicitly that the Company is working with the Partnership for Carbon Accounting Financials, which working group the Company co-chairs, to develop a methodology for "facilitated emissions" and that "[d]epending on the pace of methodology development, we intend to include our capital markets activities in the scope of the 2030 targets and our reporting by the end of 2022."[16] Capital markets activities would include underwriting activities.

- Substantial implementation does not require implementation in full or exactly as presented by a proposal, and the Staff has found proposals related to climate change excludable pursuant to Rule 14a-8(i)(10), even if the company's actions were not identical to the guidelines of the proposal. Both *Entergy Corp.* and *Duke Energy Corp.* permitted exclusion of a shareholder proposal pursuant to Rule 14a-8(i)(10), even though the requested disclosures were not made in precisely the manner contemplated by the proponent. Numerous other letters reinforce this approach. *See, e.g.*, *Merck & Co., Inc*. (Mar. 14, 2012) (permitting exclusion of a shareholder proposal requesting a report on the safe and humane treatment of animals because the company had already provided information on its website and further information was publicly available through disclosures made to the United States Department of Agriculture); *Exxon Mobil Corporation* (Mar. 17, 2011) (permitting exclusion of a shareholder proposal requesting a report on the steps the company had taken to address ongoing safety concerns where the Company's "public disclosures compare[d] favorably with the guidelines of the proposal"); and *Exxon Mobil Corporation* (Jan. 24, 2001) (permitting exclusion of a shareholder proposal requesting the review of a pipeline project, the development of criteria for involvement in the project and a report to shareholders because it was substantially implemented by prior analysis of the project and publication of such information on the company's website).
- The Proposal's "essential objective" is for the Company's "Board of Directors [to] adopt a policy by the end of 2022" that contains measures relating to fossil fuel development, "consistent with…the International Energy Agency's Net Zero Emissions by 2050 Scenario" and science or science-based targets. This has been substantially implemented as shown by the disclosures contained in the ESPS, the Company's website and related press releases. The public disclosure by the Company

[12] *See* UNEP FI delivers G20 input paper with recommendations for credible net-zero finance commitments – United Nations Environment – Finance Initiative.

[13] *See* Net-Zero Financed Emissions | Morgan Stanley, "The financed emissions targets are aligned with the science-based International Energy Agency's (IEA) Net-Zero by 2050 emissions pathways."

[14] "Morgan Stanley Net Zero Target Methodology published November 2021, publicly available at Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), pages 5, 6 and 10. *See also* 2030 Targets for Net-Zero Financed Emissions Commitment | Morgan Stanley ("credible net-zero targets").

[15] Morgan Stanley 2020 TCFD Report at page 24.

[16] "Morgan Stanley Net Zero Target Methodology published November 2021, publicly available at Morgan-Stanley-Net-Zero-Target-Methodology.pdf (morganstanley.com), page 11.

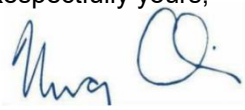
compares favorably with the essence of the Proposal, and thus the Proposal is excludable under Rule 14a-8(i)(10).

CONCLUSION

For the reasons set forth above, we believe that the Proposal may be excluded from the Company's 2022 Proxy Materials pursuant to Rule 14a-8(i)(7) and Rule 14a-8(i)(10). The Company respectfully requests the Staff's concurrence with its decision to exclude the Proposal from its 2022 Proxy Materials and further requests confirmation that the Staff will not recommend enforcement action to the SEC if it so excludes the Proposal.

We would be happy to provide you with any additional information and answer any questions that you may have regarding this request. Please do not hesitate to call me at (212) 450-6145 or Martin Cohen at Marty.Cohen@morganstanley.com or (212) 537-2007 if we may be of any further assistance in this matter.

Respectfully yours,



Ning Chiu

Attachment

cc w/ att: Martin Cohen, Morgan Stanley

Paul Rissman, Sierra Club

EXHIBIT A

Proposal

Resolved: Shareholders request that the Board of Directors adopt a policy by the end of 2022 committing to proactive measures to ensure that the company's lending and underwriting do not contribute to new fossil fuel development, consistent with fulfilling the United Nations Environmental Program Finance Initiative recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

Supporting Statement

Morgan Stanley "recognizes that climate change is occurring, and acknowledges the scientific consensus…that greenhouse gases emitted by human activities are the primary driver. We recognize the benefits of helping to reduce greenhouse gas emissions as climate change poses significant risks to the global economy."[17] Morgan Stanley is a member of the Net Zero Banking Alliance (NZBA), for which our CEO committed to align with pathways consistent with a maximum temperature rise of 1.5 degrees Celsius above pre-industrial levels, utilizing decarbonization scenarios from "credible and well-recognized sources."[18]

However, membership in the Alliance does not necessarily equate with alignment with global climate goals. The United Nations Environmental Program Finance Initiative (UNEP FI), which convenes the NZBA, published an Input Paper to the G20 Sustainable Finance Working Group which defines credible net zero commitments of financial institutions, including: "A financial institution establishing a net-zero commitment should begin aligning with the required assumptions and implications of IPCC 1.5°C no/low overshoot pathways as soon as possible….All no/low overshoot scenarios indicate an immediate reduction in fossil fuels, signaling that investment in new fossil fuel development is not aligned with 1.5°C."[19] Another of the world's most credible sources, the International Energy Agency (IEA), in its Net Zero Emissions by 2050 Scenario (NZE), states that "no fossil fuel exploration is required and no new oil and natural gas fields are required beyond those that have already been approved for development."[20] Morgan Stanley has restricted financing for new coal operations and Arctic drilling, but has no policy to halt financing any new oil and gas exploration and development. Morgan Stanley is the fifth-highest U.S. financier or facilitator of companies expanding fossil fuels, according to the Banking on Climate Chaos report.[21]

Morgan Stanley faces two associated problems: first, its prominence in asserting climate leadership flies in the face of its actions, creating reputational risk from accusations of greenwashing; second, in underwriting projects which are unneeded under the UNEP FI recommendations or the IEA NZE scenario, it is knowingly loading potentially stranded assets onto its clients' balance sheets, creating litigation risk.[22] In this regard, investors need to know that Morgan Stanley's lending and underwriting policies are consistent with its own net zero commitment.

[17] https://www.morganstanley.com/about-us-governance/Environmental_and_Social_Policy_Statement_December_2020.pdf, at 10.

[18] https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-NZBA-Commitment-Statement.pdf

[19] https://g20sfwg.org/wp-content/uploads/2021/10/2021-UNEP-FI.-Recommendations-for-Credible-Net-Zero-Commitments.pdf, at 15.

[20] https://iea.blob.core.windows.net/assets/88dec0c7-3a11-4d3b-99dc-8323ebfb388b/WorldEnergyOutlook2021.pdf, at 100.

[21] https://www.ran.org/wp-content/uploads/2021/03/Banking-on-Climate-Chaos-2021.pdf, at 38.

[22] https://www.justice.gov/opa/pr/goldman-sachs-agrees-pay-more-5-billion-connection-its-sale-residential-mortgage-backed

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February 10, 2022
Via electronic mail

Office of Chief Counsel
Division of Corporation Finance
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

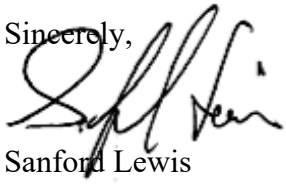
Re: Shareholder Proposal to Morgan Stanley Regarding Fossil Fuel Financing on Behalf of the Sierra Club Foundation

Ladies and Gentlemen:

The Sierra Club Foundation (the "Proponent") is the beneficial owner of common stock of Morgan Stanley (the "Company") and has submitted a shareholder proposal (the "Proposal") to the Company. I have been asked by the Proponent to respond to the letter dated January 14, 2022 ("Company Letter") sent to the Securities and Exchange Commission by Ning Chiu of Davis Polk. In that letter, the Company contends that the Proposal may be excluded from the Company's 2022 proxy statement. A copy of this letter is being emailed concurrently to Ms. Chiu.

The materials attached demonstrate that the Company has no basis under Rule 14a-8 for exclusion of the Proposal. As such, we respectfully request that the Staff inform the Company that it is denying the no action letter request.

Sincerely,



Sanford Lewis

Response to No Action Request of January 14, 2022
Morgan Stanley
Proposal on Fossil Fuel Lending and Underwriting

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SUMMARY

The Proposal (attached as an Appendix) asks the Board of Directors of Morgan Stanley ("MS") to adopt a policy by the end of 2022 committing the Company to proactive measures, to ensure that the company's lending and underwriting practices do not contribute to new fossil fuel development - consistent with fulfilling the UN's Environmental Program Finance Initiative ("UNEP FI") recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

The Company asserts that the Proposal may be excluded under Rule 14a-8(i)(7) because the Company claims that the Proposal deals with matters relating to the Company's ordinary business operations. However, when examining the Proposal against the Commission and Staff's guidance on shareholder proposals, including ordinary business and micromanagement, it is evident that the Proposal addresses a transcendent policy issue and does not micromanage or otherwise inappropriately address the Company's ordinary business.

The Proposal does not micromanage as it benchmarks Company activities against the most prominent and credible applicable international guidance - the International Energy Agency's net zero roadmap and the UNEP FI recommendations regarding what a financial institution's "credible net zero commitments" necessitate. In asking the Company to adopt a policy on the financing of new fossil fuel development in alignment with IEA and UNEP FI benchmarks, the Proposal addresses an issue that does not probe too deeply for investors, but rather provides an appropriate opportunity for investors to weigh in on key risks and strategy, and to encourage the Company to establish an internal policy in alignment with its public statements on climate.

Although the Company has made various climate commitments including "net zero by 2050" and interim targets for high carbon sectors, the Company is one of the leading financiers of fossil fuel development. Numerous international assessments have concluded that current financing of new fossil fuel development is on a trajectory that overshoots the amount of fossil fuels that need to stay in the ground to contain global temperature increase to 1.5°C. The Company's current financing policies appear inconsistent with the global goals and their own public statements.

The wording of the Proposal is neither too specific nor constraining of board and management discretion. The Proposal leaves ample flexibility for the Board to identify the means of implementation: what kind of "*proactive measures*" does the board, in its discretion, believe is appropriate "*to ensure that the company's lending and underwriting practices do not contribute to new fossil fuel development"* consistent with the referenced international guidance?

Contrary to the Company Letter, the Proposal does not prescribe or request divestment from fossil fuel companies. Rather, the Proposal only seeks to ensure that the Company's financing does not support new fossil fuel development so that it may remain consistent with its public climate commitments.

Therefore, because the Proposal does not micromanage the board, but in fact raises appropriate issues for shareholder deliberation, it is not excludable under Rule 14a-8(i)(7).

In addition, the Company Letter asserts that the Proposal is substantially implemented by the Company's existing policies and targets. In reality, the Company's actions do not implement the essential purpose of the Proposal, which is to ensure that it adopts proactive measures intended to ensure that the Company's

lending and underwriting practices do not contribute to new fossil fuel development that is inconsistent with UNEP FI and IEA net zero 2050 benchmarks. Instead, the Company Letter makes it clear that the Company intends to keep the door open to financing additional fossil fuel development.

The Company's adopted policies and targets which it claims are "on the path to net zero" are not consistent with the core precept of the Proposal, which is "not contributing to new fossil fuel development."

The Company tries to recast the guidelines and purpose of the Proposal as requesting that the Company adopt a policy *relating to* fossil fuels. The Company *has* existing policies "relating to fossil fuels", but they leave substantial room for new fossil fuel development. Moreover, if the Company were to assert to its investors that its existing disclosures fulfill the Proposal, that would be misleading; this is a further reason that the Proposal is not substantially implemented. Therefore, the Proposal is not excludable under Rule 14a-8(i)(10).

BACKGROUND

In the global effort to mitigate climate change, many countries and corporations have committed to achieving net zero by 2050 and to align with the Paris Agreement climate goals of constraining global temperature increase. Morgan Stanley is among the banks that have committed to "net zero by 2050."[1] While corporate and national climate pledges to achieve net zero by 2050 proliferate, most actions and policies from both nations and companies do not align with the pledges or with a 1.5°C scenario. Despite the pledges, greenhouse gas (GHG) emissions continue to rise, and the current amount of planned fossil fuel development would exceed the projected "carbon budget" to constrain global temperature increase.

Since the concept was introduced in 2011 by the nongovernmental organization Carbon Tracker, the carbon budget reflects the amount of fossil fuels that can enter global commerce without violating global goals to contain temperature increase. In 2021, a research report published in *Nature* indicated that, for a 50% chance of global temperature increase to remain below 1.5°C — the aspirational goal of the 2015 Paris agreement — the world cannot emit more than 580 gigatonnes of carbon dioxide before 2100. As part of the report, researchers calculated that 89% of coal reserves, 58% of oil reserves and 59% of gas reserves must remain unextracted to ensure that not more than 580 gigatonnes of carbon dioxide is emitted before 2100. The report notes that their estimate of the carbon budget:

> …implies that most regions must reach peak production now or during the next decade, rendering many operational and planned fossil fuel projects unviable. We probably present an underestimate of the production changes required, because a greater than 50 per cent probability of limiting warming to 1.5 °C requires more carbon to stay in the ground and because of uncertainties around the timely deployment of negative emission technologies at scale.[2]

Currently, neither corporate nor national commitments align with this carbon budget projection and with the amount of fossil fuels that must remain in the ground to meet it. In its "Net Zero by 2050" roadmap,

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[1] *See* Environmental and Social Policy Statement *found at* https://www.morganstanley.com/about-us-governance/pdf/Environmental_and_Social_Policy_Statement_December_2020.pdf

[2] *See* Welsby, D., Price, J., Pye, S. *et al.* Unextractable fossil fuels in a 1.5 °C world. *Nature* **597,** 230–234 (2021) *found at* https://doi.org/10.1038/s41586-021-03821-8

the International Energy Agency (IEA) reported that current climate pledges would still create 22 billion tons of CO2 emissions in 2050, a number well above zero.[3] Therefore, to reach the collective 1.5°C goal, more aggressive policies would need to be implemented.

The financial sector, including Morgan Stanley as one of the leading financiers of fossil fuel development, faces a significant challenge to redirect financial flows and align with the net zero 1.5°C scenario.

The United Nations Environment Programme Finance Initiative ("UNEP FI") and IEA have identified the containment of supply growth above the world's carbon budget as a critical priority action in corporate and government efforts to achieve the global goals. As mentioned in the Proposal, the UNEP FI issued recommendations for credible net-zero commitments from financial institutions, which included a recommendation for financial institutions that have made net-zero commitments to "align as soon as possible"[4]:

> A financial institution establishing a net-zero commitment should begin aligning with the required assumptions and implications of IPCC 1.5°C no/low overshoot pathways as soon as possible. This is because the pathways require immediate actions to have a realistic chance of limiting warming to 1.5°C. ***This would include, for example, the immediate cessation of any new fossil fuel investments, and rapid decommissioning of remaining fossil fuel production as indicated by the scenarios.*** [Emphasis added]

The UNEP FI also notes in its recommendations that "All no/low overshoot scenarios indicate an immediate reduction in fossil fuels, *signaling that investment in new fossil fuel development is not aligned with 1.5°C.*" [Emphasis added]

Morgan Stanley and Fossil Fuel Expansion

Based on the IEA and UNEP FI benchmarks, it is clear that banks need to expeditiously end support for expansion of fossil fuel extraction and related infrastructure, whether through project finance or general corporate finance. In this instance, the Company's CEO has signed the Net Zero Banking Alliance ("NZBA") Commitment.[5] That Commitment commits member banks to "use the bank-led UNEP FI Guidelines for Climate Target Setting for Banks."[6] The UNEP FI Guidelines for Climate Target Setting for Banks specify "The scenarios used by banks shall come from credible and well-recognised sources…The scenarios selected shall be "no-overshoot" or "low-overshoot" scenarios."[7] Those scenarios include, as noted above, "the immediate cessation of any new fossil fuel investments, and rapid decommissioning of remaining fossil fuel production as indicated by the scenarios."

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[3] *See* Net Zero by 2050—A Roadmap for the Global Energy Sector *found at* https://iea.blob.core.windows.net/assets/deebef5d-0c34-4539-9d0c-10b13d840027/NetZeroby2050-ARoadmapfortheGlobalEnergySector_CORR.pdf

[4] https://www.unepfi.org/publications/recommendations-for-credible-net-zero-commitments-from-financial-institutions/

[5] https://www.unepfi.org/net-zero-banking/commitment/

[6] https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-NZBA-Commitment-Statement.pdf

[7] https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-Guidelines-for-Climate-Change-Target-Setting.pdf

Despite its membership in NZBA, Morgan Stanley remains one of the largest financiers of the fossil fuel sector, including new fossil fuel development. Although the Company has established targets to reduce its financed emissions lending intensity for three sectors of its lending portfolio, the Company's policies appear to leave significant leeway for financing new fossil fuel extraction and related infrastructure. The financed emission lending intensity targets that it has established are compatible with expansion of fossil fuels.

The Company's opposition to this proposal, and its clear statement that "funding some degree of new fossil fuel development" and that "many companies in the oil and gas industry are expected to increase production in the near term" (see Company Letter page 6), provide ample evidence that the company is not actually planning on taking actions necessary to meet the UNEP FI and IEA credibility benchmarks on fossil fuel development.

The Proposal offers investors a key opportunity to voice their opinion on the issue and in doing so, advise the Company as to whether investors believe the Company should meet this IEA/UNEP FI credibility standard.

ANALYSIS

Rule 14a-8(i)(7)

The Company Letter asserts that the Proposal addresses the ordinary business of the Company. However, when examining the Proposal against the Commission and Staff's guidance on shareholder proposals, including ordinary business and micromanagement, it is evident that the proposal addresses a transcendent policy issue and does not micromanage or otherwise inappropriately address the Company's ordinary business.

Ordinary Business According to the Commission

In 1998, the Commission issued a rulemaking release ("1998 Release") updating and interpreting the ordinary business rule, by both reiterating and clarifying past precedents. That release was the last time that the Commission discussed and explained at length the meaning of the ordinary business exclusion. The Commission summarized *two central considerations* in making ordinary business determinations – whether the proposal addresses a significant social policy issue, and whether it micromanages.

First, the Commission noted that certain tasks were generally considered so fundamental to management's ability to run a company on a day-to-day basis that they could not be subject to direct shareholder oversight (e.g., the hiring, promotion, and termination of employees, as well as decisions on retention of suppliers, and production quality and quantity). However, proposals related to such matters but *focused on sufficiently significant social policy issues* (i.e., significant discrimination matters) generally would <u>not</u> be excludable.

Second, proposals could be excluded to the extent they seek to "micromanage" a company by probing too deeply into matters of a complex nature upon which shareholders, as a group, would be unable to make an informed judgment. This concern did not, however, result in the exclusion of all proposals seeking detailed timeframes or methods. As the 1998 Release indicated:

> Timing questions, for instance, could involve significant policy where large differences are at stake, and proposals may seek a reasonable level of detail without running afoul of these considerations.

Proposals that passed the first prong but for which the wording involved some degree of micromanagement could be subject to a case-by-case analysis of *whether the proposal probes too deeply* for shareholder deliberation. The Staff's interpretation of micromanagement has evolved over the years, most recently articulated in the November 3, 2021 Staff Legal Bulletin 14L.[8] To assess micromanagement going forward, the bulletin notes that the Staff:

> will focus on the level of granularity sought in the proposal and whether and to what extent it inappropriately limits discretion of the board or management. **We would expect the level of detail included in a shareholder proposal to be consistent with that needed to enable investors to assess an issuer's impacts, progress towards goals, risks or other strategic matters appropriate for shareholder input.** [Emphasis added]
>
> ***
>
> Additionally, in order to assess whether a proposal probes matters "too complex" for shareholders, as a group, to make an informed judgment, we may consider the sophistication of investors generally on the matter, the availability of data, and the robustness of public discussion and analysis on the topic. The staff may also consider references to well-established national or international frameworks when assessing proposals related to disclosure, target setting, and timeframes as indicative of topics that shareholders are well-equipped to evaluate.
> This approach is consistent with the Commission's views on the ordinary business exclusion, which is designed to preserve management's discretion on ordinary business matters but not prevent shareholders from providing high-level direction on large strategic corporate matters.
>
> ***
>
> While the analysis in this bulletin may apply to any subject matter, many of the proposals addressed in the rescinded SLBs requested companies adopt timeframes or targets to address climate change that the staff concurred were excludable on micromanagement grounds. Going forward we would not concur in the exclusion of similar proposals that suggest targets or timelines so long as the proposals afford discretion to management as to how to achieve such goals.

Micromanagement Analysis Under Staff Legal Bulletin 14L

Thus, the Staff Legal Bulletin's analysis of issues of micromanagement comes down to two basic tests to determine whether a proposal "probes to deeply" for shareholders' consideration:

> First, does the proposal frame the investor deliberation in a manner consistent with market discussions, available guidelines and the state of familiarity/expertise on the issues in the investing marketplace?

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[8] The Staff Bulletin notes an evolution in the staff's thinking. In rescinding prior staff legal bulletins, the bulletin notes that: we believe that the rescinded guidance may have been taken to mean that any limit on company or board discretion constitutes micromanagement.

Second, does it leave sufficient flexibility for board and management discretion?

We will address each of these questions in turn.

A Deliberation Appropriate to Shareholders

It is appropriate for shareholders to deliberate on whether the Company should live up to credible global fossil fuel supply development requirements. Staff Legal Bulletin 14 L notes that in considering ordinary business challenges and micromanagement, the Staff will consider whether the deliberation posed by the proposal in question is consistent with current investor discourse and credible national or international guidelines:

> **We would expect the level of detail included in a shareholder proposal to be consistent with that needed to enable investors to assess an issuer's impacts, progress towards goals, risks or other strategic matters appropriate for shareholder input.**
>
> …in order to assess whether a proposal probes matters "too complex" for shareholders, as a group, to make an informed judgment, we may consider the sophistication of investors generally on the matter, the availability of data, and the robustness of public discussion and analysis on the topic. **The staff may also consider references to well-established national or international frameworks when assessing proposals related to disclosure, target setting, and timeframes as indicative of topics that shareholders are well-equipped to evaluate.** [Emphasis added]

Global Guidelines

The core benchmark of the Proposal is consistency with global guidelines on an aggressive, 1.5°C trajectory. The Proposal asks the Company to adopt a fossil fuel development policy that is “consistent” with the IEA and UNEP FI guidelines. These are widely adopted and credible global benchmarks for an aggressive 1.5°C scenario and response on climate change.

The Net Zero Emissions by 2050 Roadmap was established by the International Energy Agency (IEA).

> The IEA is at the heart of global dialogue on energy, providing authoritative analysis, data, policy recommendations, and real-world solutions to help countries provide secure and sustainable energy for all.
>
> The IEA was created in 1974 to help coordinate a collective response to major disruptions in the supply of oil. While oil security remains a key aspect of our work, the IEA has evolved and expanded significantly since its foundation.
>
> Taking an all-fuels, all-technology approach, the IEA recommends policies that enhance the reliability, affordability and sustainability of energy. It examines the full spectrum issues including renewables, oil, gas and coal supply and demand, energy efficiency, clean energy technologies, electricity systems and markets, access to energy, demand-side management, and much more.[9]

[9] https://www.iea.org/about/mission

The IEA has established various scenarios for global climate change responses, with its latest Net Zero by 2050 Roadmap providing a detailed description of an ambitious global project to alter the world's energy infrastructure and align with net zero and 1.5°C goals. That roadmap includes the statement that **"that no fossil fuel exploration is required and no new oil and natural gas fields are required beyond those that have already been approved for development."**[10]

The United Nations (UN)[11] is the body that has convened the global climate talks, facilitated the global climate agreements and led the scientific assessments of climate change. **Among UN's climate initiatives, the United Nations Environment Programme Finance Initiative (UNEP FI) is the home for the Net Zero Banking Alliance, of which Morgan Stanley is a member.**

The UNEP FI 2021 report entitled "Recommendations for Credible Net-Zero Commitments from Financial Institutions" provides clear guidance and benchmarks for issuers and their investors in assessing whether current company pledges are matched by credible commitments considering the global agreements and goals. The UNEP FI report is geared toward a clear benchmark of financial institution credibility on their net zero commitments, making it clear that one of the most important benchmarks of credibility is to "align as soon as possible"[12]:

> A financial institution establishing a net-zero commitment should begin aligning with the required assumptions and implications of IPCC 1.5°C no/low overshoot pathways as soon as possible. This is because the pathways require immediate actions to have a realistic chance of limiting warming to 1.5°C. **This would include, for example, the immediate cessation of any new fossil fuel investments, and rapid decommissioning of remaining fossil fuel production as indicated by the scenarios**. [Emphasis added]

Thus, the Proposal is grounded in and benchmarked against key international frameworks and guidelines. As SLB 14L notes, "The staff may also consider references to well-established national or international frameworks when assessing proposals related to disclosure, target setting, and timeframes as indicative of topics that shareholders are well-equipped to evaluate." This Proposal is not about "investors probing too deeply" into Company management, but rather about asking the Company to come into line with the global benchmarks for proactive responses to climate change.

Prominence of Discussion

The issues relevant to the Proposal have also been addressed in media coverage, investor publications, and in international guidance. Therefore, the introduction of this issue as a topic for the Company's shareholder meeting is appropriate and pitched consistent with shareholder understanding and deliberation. Public debate and analysis regarding the actions required towards a net zero future are robust and ongoing.

For example, on May 18, 2021,The New York Times covered the IEA's World Energy Outlook with a headline "***Nations Must Drop Fossil Fuels, Fast, World Energy Body Warns***: A landmark report from

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[10] *See* World Energy Outlook 2021 *found at* https://iea.blob.core.windows.net/assets/88dec0c7-3a11-4d3b-99dc-8323ebfb388b/WorldEnergyOutlook2021.pdf

[11] https://www.un.org/en/climatechange

[12] https://www.unepfi.org/publications/recommendations-for-credible-net-zero-commitments-from-financial-institutions/

the International Energy Agency says countries need to move faster and more aggressively to cut planet-warming pollution."[13]

> Nations around the world would need to immediately stop approving new coal-fired power plants and new oil and gas fields and quickly phase out gasoline-powered vehicles if they want to avert the most catastrophic effects of climate change, the world's leading energy agency said Tuesday.

The article also noted the importance for investors:

> That's significant, given the fact that the influential agency is not an environmental group but an international organization that advises world capitals on energy policy. **Formed after the oil crises of the 1970s, the agency's reports and forecasts are frequently cited by energy companies and investors as a basis for long-term planning**. [Emphasis added]

The New York Times also covered the UN sponsored Production Gap report and the IEA Net Zero Scenario in October 2021 with a headline "***Fossil Fuel Drilling Plans Undermine Climate Pledges, U.N. Report Warns***: Countries are planning to produce more than twice as much oil, gas and coal through 2030 as would be needed if governments want to limit global warming to Paris Agreement goals."[14]

> The International Energy Agency recently looked at what would be needed to hold global warming to 1.5 degrees Celsius. All of the world's nations would have to drastically cut their fossil-fuel use over the next three decades until they are no longer adding any greenhouse gases to the atmosphere by 2050, essentially achieving "net zero" emissions.
>
> Under that scenario, the agency said, the world's nations would not approve the development of any new coal mines or new oil and gas fields beyond what has already been committed today.

A January 7, 2022 opinion piece in the Financial Times highlights the dilemma of banks who are part of the UNEP FI's Net Zero Banking Alliance but have yet to commit to a phase-out of new fossil fuel development titled: *"**Banks risk becoming new fossil fuel villains in 2022: Financing climate change culprits is becoming more visible and troublesome than ever before.**"*[15]

> Definitions of green financing can be generous, but the direction of greenward travel seems clear — except for one thing. Banks may be turning on the taps for green finance but they are far from closing them for fossil fuels. The world's 6o largest private sector banks have put more than $3.8tn into the oil, gas and coal sectors since the 2015 Paris agreement, according to NGO research. And a lot has gone to oil and gas companies with big expansion plans.
>
> With no sign of rapid change, banks face a double difficulty in exposing their fossil financing to more scrutiny — and charges of climate villainy without showing how they might eventually wind it back.
>
> In theory, the problem should be solved by a group like the Net Zero Banking Alliance, whose 98 members account for more than 40 percent of global banking assets. They have to set out plans for zeroing out emissions. The trouble is the brutal maths. Scientists have established it is much

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[13] https://www.nytimes.com/2021/05/18/climate/climate-change-emissions-IEA.html
[14] https://www.nytimes.com/2021/10/20/climate/fossil-fuel-drilling-pledges.html
[15] https://www.ft.com/content/73615213-08ce-4786-9b8c-773029552bbc

> safer to limit global warming to 1.5°C. So human-made carbon emissions, much of which come from burning oil, gas and coal, should nearly halve by 2030 and fall to net zero by around 2050.
>
> ***
>
> Banks have reduced backing for coal over time. But very few net zero alliance members have issued detailed plans showing how and when they might wind down support for oil and gas…

As demonstrated by the examples above, the broader context of the Proposal is comprehensible by Morgan Stanley's investors, appropriate for discussion in the debate and not outside of the grasp of investor deliberation and engagement.

Investor Interests in the Subject Matter of the Proposal

The financing of continued fossil fuel development by the Company poses important questions for its shareholders: stranded assets and reputational risk to the company, systemic and portfolio wide risks for diversified investors, and due diligence concerns for ESG investors. It is salient for investors to ask the Company, as one of the largest financiers of fossil fuels, to come into alignment with the leading global benchmarks for an effective climate change mitigation response. The following discussion addresses each of these in turn:

1) <u>Issuer-specific risks</u>. Reducing the extent to which Morgan Stanley's fossil fuel financing places the Company's assets at risk, including risks of stranded assets and reputational damage.

2) <u>Portfolio-wide and Systemic risks</u>. Reducing the extent to which the Company's fossil fuel financing may be inconsistent with an investor's commitment to manage systemic risk by aligning with global climate goals.

3) <u>ESG Due diligence risks</u>. Ensuring that fiduciaries including investment firms, asset managers, analysts and trustees have necessary information from Morgan Stanley as a portfolio company, to conduct due diligence on the fiduciaries' ESG related claims.

ISSUER-SPECIFIC RISKS

For each of the last 5 years, Morgan Stanley has been one of the world's leading banks financing fossil fuels. However, in order to meet its own commitment to align its financed emissions with the goals of the Paris Agreement, it needs to adopt immediate steps to slash its financing for fossil fuels. Additionally, expansion of new fossil fuel assets poses risks to the company including increasing the number of stranded assets in its portfolio and reputational risk associated with a public appearance of greenwashing.

Stranded Asset Risk

Morgan Stanley is at an increasing risk of asset stranding by financing fossil fuels including fossil fuel expansion. Stranded assets are a likely consequence of the approaching energy transition.

As discussed on page 2 of this letter, a recent research report estimated that the majority of the known reserves of coal, oil and gas must remain unextracted for the world to have a 50% chance of keeping the global temperature increase below 1.5°C. The implications for the fossil fuel industry from this

temperature target are significant. The Production Gap Report[16], which tracks the discrepancy between planned fossil fuel production and global production levels consistent with 1.5°C warming warned that:

> The limits to future extraction implied by the Paris Agreement (see Chapter 2), combined with competition from rapidly advancing renewable energy technologies, are changing the market outlook for coal, oil, and gas. In this context, extractive projects, which typically have a 30- or 40-year time horizon, may well leave a legacy of stranded assets and unmet liabilities.

A think tank of financial experts that has for several years evaluated the impact of the energy transition on oil and gas companies compared oil and gas production levels in the 2030s under IEA's Net Zero Scenario (NZE) with 2021 levels for the world's 40 largest listed oil and gas companies. It found that "for most companies – including majors like Shell, Chevron and Eni – production falls by at least half." The same report found that temperature goals and pathways less ambitious than 1.5°C and NZE would still leave more than half of the world's largest listed oil and gas companies highly exposed to asset stranding.[17] The report concluded:

> Regardless, in any low-carbon future, the overarching challenge for the oil and gas industry is that the space for new production narrows over time, while the risk of investing in assets that are not required increases, placing capital at risk.
>
> "If [oil and gas] companies are serious about aligning with the Paris goals and reaching net zero globally by mid-century, they need to be prepared for a rapid wind-down of their traditional business segments. Similarly, investors that want to be 1.5°C ready need to be aware of the serious implications that this has for the oil and gas companies they hold.

Concerns about asset stranding in the oil and gas sectors are highly relevant for Morgan Stanley's financing activities. The Company is among the largest oil and gas financiers globally. Between 2016 and 2020, Morgan Stanley provided $111 billion in lending and underwriting to the fossil fuel industry, 12th among global banks. Its largest fossil fuel clients over that time included ExxonMobil ($8.3 billion in financing from the Company during 2016-20), Shell ($6.6B), BP ($4.2B), and Saudi Aramco ($3.9B).[18] Six of the top ten global oil and gas companies most exposed to asset stranding (according to the analysis cited above) are clients of Morgan Stanley. One of the most exposed companies is ExxonMobil, the largest fossil fuel client of the Company.

The Net Zero Energy scenario (NZE Scenario) that Morgan Stanley has used in its sectoral emission target setting was built on several principles including the goal of "minimizing stranded assets where possible", according to the IEA.[19] Consistent with this goal, one of the key near-term requirements of the NZE Scenario is that no new oil and natural gas fields are developed beyond those that have already been approved, as discussed on page 7 of this letter. Beyond the sectoral targets, Morgan Stanley needs to adopt a policy ensuring that its lending and underwriting do not contribute to new fossil fuel development to make its targets credible against the IEA benchmark and to also ensure that it does not unnecessarily contribute to the creation of stranded assets.

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[16] *See* SEI, IISD, ODI, E3G, and UNEP. (2020). The Production Gap Report: 2020 Special Report *found at* http://productiongap.org/2020report

[17] *See* Carbon Tracker. Adapt to Survive. September 2021. Why oil companies must plan for net zero and avoid stranded assets *found at* https://carbontracker.org/reports/adapt-to-survive/

[18] *See* Banking on Climate Chaos 2020 Report and Data *found at* www.bankingonclimatechaos.org

[19] *See* IEA's Net Zero by 2050—A Roadmap for the Global Energy Sector

Climate change and the transition to a low carbon world pose material risks to banks financing the energy sector. The Proposal is an opportunity for shareholders to protect their investments by asking for a policy that aligns Morgan Stanley's approach with a credible 1.5°C pathway and limits the company's exposure to stranded asset risk from its lending and underwriting activities.

Reputational Risk

In addition, the Proposal is also aligned with investor interest in reputational risk, and ensuring that the company is not vulnerable to charges of greenwashing given its participation in efforts like the Net Zero Banking Alliance. The Company's resistance to ending new fossil fuel development is contrary to a global transition consistent with 1.5°C warming and the requirements of the frameworks and methodologies used by the Company in its emissions targets and commitments. The Office of the Comptroller of the Currency has recognized this risk in its recent proposal[20] on climate accountability of banks, noting that:

> [W]here banks engage in public communication of their climate-related strategies, boards and management should ensure that any public statements about their banks' climate-related strategies and commitments are consistent with their internal strategies and risk appetite statements.

Morgan Stanley engages in many such communications, including Morgan Stanley's commitment to net zero financed emissions by 2050 and its interim 2030 targets. Yet, as we discussed above, UNEP FI has defined a *credible financial institution's net zero commitment as* necessitating alignment with global goals including the need to halt financing of new fossil fuel development.

The Proposal provides a key opportunity for the Company's investors to inquire more deeply about reputational risk and encourage the Company to sustain the credibility of its net zero commitments, by aligning its policies with international benchmarks and moving beyond its current equivocal approach to new oil and gas development.

PORTFOLIO-WIDE AND SYSTEMIC RISKS

The Company's fossil fuel financing may be inconsistent with an investor's commitment to alignment with global climate goals

Many investors and fiduciaries have undertaken policies and commitments to align their portfolios with global climate goals. The BankTrack website which focuses on analysis of banking and climate change summarizes this systemic view in its analysis[21]:

> The Paris Climate Agreement, which was signed in 2015, aims to "avoid dangerous climate change by limiting global warming to well below 2°C and pursuing efforts to limit it to 1.5°C". The scientific basis for limiting global warming to 1.5°C instead of 2°C was further strengthened in 2018 by the IPCC's special report on global warming of 1.5°C. This report clearly showed that all negative effects of global warming such as sea level rise, water and food insecurity, damage to ecosystems and ocean acidification are less severe at warming of 1.5°C compared to 2°C.

[20] https://www.occ.treas.gov/news-issuances/news-releases/2021/nr-occ-2021-138a.pdf
[21] https://www.banktrack.org/page/banks_and_fossil_fuel_expansion

> To estimate the amount of carbon dioxide that still can be emitted until reaching a certain temperature threshold, like 1.5°C of warming, climate scientists work with 'carbon budgets'. Analysis by Oil Change International shows that the currently developed fossil fuel reserves for gas, oil and coal are already double the remaining carbon budget for a 50% chance of staying below 1.5°C of global warming. In the beginning of 2021, the International Energy Agency came to the same conclusion and stated that there was 'no need for more fossil fuels' in their Net Zero by 2050 Roadmap.
>
> Based on this analysis, it can be concluded that *all fossil fuel expansion is incompatible with the goals agreed upon in the Paris Climate Agreement*. (*Fossil fuel expansion* encompasses all development of untapped fossil fuel sources and building the infrastructure to bring these fossil fuels to the market.) In this context, any further exploration for new reserves and the construction of new fossil fuel infrastructure is indefensible and should not be pursued by any government or company, or financed by any bank. Unfortunately, many banks continue to finance fossil fuel expansion, while the policies of most banks to limit or stop their finance for expansion remain weak or often even non-existent.

Thus, shareholders and investment fiduciaries monitoring the global impacts of climate change, in voting on the current Proposal, provide important input to the board and management as to how to encourage companies to exercise leadership in the urgent need for a phase down in new fossil fuel development.

To the growing portion of institutional and diversified investors who as part of their fiduciary obligations need to consider and engage on the systemic, economy and portfolio wide implications of their holdings, the Proposal provides a key opportunity to engage with a major fossil fuel funder.

In addition, failure to address these broad concerns poses systemic economic risks. A recent report, "Wall Street's carbon bubble: the global omissions of the US financial sector" has noted that banks' fossil fuel assets reflect a new market bubble, analogous to subprime mortgages prior to the housing market crash of 2008:

> In order to keep global warming under 1.5 degrees Celsius, there is a finite limit to total emissions, known as the "carbon budget." To remain within that budget, global net anthropogenic CO2 emissions must decline by 45 percent from 2010 levels by 2030. This will require a rapid phase-out of the largest sources of emissions, including emissions from fossil fuel production.
>
> Unfortunately, the potential emissions from currently operating oil, gas, and coal fields and mines alone would send the world past 2°C of warming. Instead of heeding warnings, the fossil fuel industry plans to increase production through 2030, producing twice as much emissions as the carbon budget allows. This means that, if the world is to achieve the 1.5°C warming limit, a portion of existing fossil fuel projects will turn into "stranded assets," defined by the International Energy Agency as "those investments which have already been made but which, at some time prior to the end of their economic life… are no longer able to earn an economic return." Companies are therefore raising and spending capital for projects that will not provide the returns investors expect.
>
> The market is now carrying a significant amount of "unburnable carbon." This means, according to Ben Caldecott, there is a "disconnect between the current value of the listed equity of global

> fossil fuel producers and their potential commercialisation under a strict carbon budget constraint." This disconnect is termed the "carbon bubble."[22]

As described in a paper by David Comerford and Alessandro Spignati:

> [A]nalogously to the subprime mortgage problem that precipitated the 2008-09 Financial Crisis, the global economy is once again mis-pricing assets as markets overlook this 'unburnable carbon' problem. This issue is termed the 'Carbon Bubble' because the imposition of climate policy consistent with the Potsdam Climate Institute's calculations would mean the fundamental value of many fossil fuel assets must be zero as they cannot be used. Their current market value must therefore be made up of a zero fundamental value, and a 'bubble' component: the Carbon Bubble.[23]

The scale of this mispricing problem is significant. According to Carbon Tracker Initiative[24], **"governments and global markets are currently treating as assets reserves equivalent to nearly 5 times the carbon budget for the next 40 years." Based on some estimates, the impact of losses from stranded fossil fuel assets may "amount to a discounted global wealth loss of $1-4 trillion."** [Emphasis added]

Thus the continued refusal by companies and financial institutions to adapt their business activity to align with a carbon-constrained future in a timely manner may lead to large losses in value throughout the global financial system. If asset repricing occurs abruptly, this inaction will lead to sudden, painful financial and economic shocks that could precipitate a global financial crisis.

This appropriate systemic and portfolio wide concern is connected with fiduciary duties of investors, specifically the fiduciary duty of impartiality which necessitates a balancing of interests of beneficiaries who may draw on the assets in the near term and those for whom retirement or other need for the assets are longer-term and may be undercut by a carbon bubble and related market shocks.[25]

ESG DUE DILIGENCE RISKS

Ensuring that investment firms, asset managers and other fiduciaries have information necessary for due diligence on any ESG related claims

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[22] https://www.americanprogress.org/article/wall-streets-carbon-bubble/

[23] https://www.bankofengland.co.uk/-/media/boe/files/events/2016/november/the-carbon-bubble-climate-policy-in-a-fire-sale-model-of-deleveraging-speaker-paper.pdf

[24] https://www.banktrack.org/download/unburnable_carbon/unburnablecarbonfullrev2.pdf

[25] A law review article reviewing this duty of impartiality noted in particular that with regard to the potential conflict between long or short term bias: "As a practical matter, such communication is done through stockholders' resolutions, allowing stockholders to express their preferences for certain corporate actions…the fiduciary duty of impartiality provides an analytic framework for the consistent resolution of stockholders' conflicts of interest. It is a balancing test that provides a corporation's board of directors a flexible tool with which to weigh various, and often conflicting, interests of stockholders to reach a resolution that maximizes the value of the enterprise as a whole." Shachar Nir, One Duty to All: The Fiduciary Duty of Impartiality and Stockholders' Conflict of Interest, 16 Hastings Bus. L.J. 1 (2020). *Available at* https://repository.uchastings.edu/hastings_business_law_journal/vol16/iss1/2

On March 4, 2021, the SEC initiated a new Task Force focused on climate and ESG issues looking primarily at the "veracity of issuers' ESG disclosures as well as those of investment fiduciaries."[26] In the present instance, the current Proposal speaks directly to the credibility of Morgan Stanley's climate change pledges and claims, and therefore advances the objectives of the Task Force in ensuring that the credibility of issuer claims on climate change are defensible.

Based on the UNEP FI issued recommendations for credible net-zero commitments from financial institutions, the credibility of Morgan Stanley's climate commitment is questionable without a concurrent commitment to eliminating the funding of new fossil fuel development.

The Proposal provides an opportunity for the Company's investors to make clear the need for the Company Board and management to guide company policy in a manner that would address what appears to be a fundamental flaw in current company plans. In addition, the shareholder right to file and vote on this proposal offers the best available opportunity for ESG investment fiduciaries to act on their due diligence responsibilities, to ensure that their ESG commitments are backed with the data and verification necessary to make any ESG claims. To the extent that investment fiduciaries claim that stock holdings in Morgan Stanley are net zero aligned, the request of the Proposal provides an opportunity to verify that claim with due diligence and proxy voting.

This investor due diligence that is enabled by the Proposal is responsive to the demands and scrutiny placed on ESG investors according to the report of the SEC Division of Examinations' Review of ESG Investing, April 9, 2021. That review noted that numerous investment products and financial services have incorporated environmental, social, and governance ("ESG") factors to meet demand. The division noted that it will be monitoring the accuracy of disclosures on ESG investing, and that examinations of firms claiming to engage in ESG investing will focus on, among other matters, a review of a firm's policies, procedures, and practices related to ESG and its use of ESG-related terminology; due diligence and other processes for selecting, investing in, and monitoring investments in view of the firm's disclosed ESG investing approaches; and whether proxy voting decision-making processes are consistent with ESG disclosures and marketing materials. The division also noted that 5 Advisers Act Section 206 imposes a fiduciary duty on investment advisers to provide full and fair disclosure of all material facts relating to the advisory relationship and to provide advice that is in the best interest of the client. Investment advisers also have antifraud liability with respect to communications to clients and prospective clients under Advisers Act Section 206. See Commission Interpretation Regarding Standard of Conduct for Investment.[27]

In short, proponents believe that the growing responsibilities of ESG investors to walk their talk necessitates support for the Proposal, to ensure that a large portfolio holding in a financial institution like Morgan Stanley does not leave an ESG investor vulnerable to enforcement actions on failure to exercise due diligence on portfolio company practices inconsistent with ESG, net zero, 1.5°C alignment and similar commitments.

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[26] *See* SEC Announces Enforcement Task Force Focused on Climate and ESG Issues *found at* https://www.sec.gov/news/press-release/2021-42

[27] The Review also noted, despite claims to have formal processes in place for ESG investing, a lack of policies and procedures related to ESG investing; policies and procedures that did not appear to be reasonably designed to prevent violations of law, or that were not implemented; documentation of ESG-related investment decisions that was weak or unclear; and compliance programs that did not appear to be reasonably designed to guard against inaccurate ESG-related disclosures and marketing materials.

The Proposal is Not Too Directive for Purposes of Rule 14a-8(i)(7)/Micromanagement

How Flexible or Specific Should a Shareholder Proposal Be?

The shareholder proposal rule states that a proposal should "state as clearly as possible the course of action" that the proponent believes "the company should follow"[28] as an advisory "request" for company action. Thus, any claim that the proposal is overly inflexible must be evaluated against this fundamental guidance in the rule itself. Moreover, failure to be specific invites a company challenge based on vagueness, that either the company or its shareholders will not understand the scope of the proposal or how it will be implemented.

It is also possible for a proposal to encroach too far onto the board and management discretion. But as an advisory proposal, the board and management's discretion is seldom encroached by a proposal. Even after a majority of support on an advisory proposal, the board and management are *expected* to exercise discretion to act as fiduciaries in the interests of the corporation. The request of the current Proposal is advisory, not directive.

The Company Letter argues that the Proposal "imposes" specific methods for implementing complex policies and inappropriately limits the discretion of the Company's management. However, as we have stated above, the Proposal does nothing to impose specific requirements on the management. The request of the Proposal is merely advisory, and leaves management wide latitude in accomplishing the general purpose and objective.

The Company Letter also asserts that the Proposal would provide management with no discretion to assess the risks and opportunities associated with lending[29]. However, there is actually substantial flexibility within the guidance of the proposal for the company to *identify proactive activities* to ensure that the company's lending and underwriting *do not contribute to new fossil fuel development*.

The Proposal Does Not Request Divestment From Particular Companies

The Company Letter argues that even though the Proposal is directed at important objectives and a transcendent policy issue it micromanages because:

> "The Proposal specifically requests that the Board adopt a policy that would "ensure" that the Company stop any ongoing lending and underwriting that it is currently involved in, or not begin any new activities that may contribute to, new fossil fuel development."

But this suggestion is inconsistent with the Proposal. To the contrary, this advisory Proposal only asks the Company to commit to proactive measures consistent with recommendations already articulated by authoritative bodies UNEP FI and IEA – that both have indicated that new fossil fuel development is not compatible with the 1.5°C scenario.

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[28] *See* Rule 14a-8(a).

[29] The Company Letter mistakenly asserts: "The Proposal would not provide management with any discretion to assess the risks and opportunities associated with the implementation of the underlying policy objectives, to leverage the extensive work it has done to establish its own existing climate-related business policies and to develop strategies in conjunction with its clients that could support a clean-energy transition and improved climate sustainability. Rather, stockholders are being asked to assume this managerial responsibility and dictate, by institutional policy, which companies are suitable to be the Company's clients."

The Proposal does not delineate acceptable clients for the Company, but rather whether the activities that it finances should be aligned with key benchmarks for the credibility of commitments by large financial institutions – the extent to which their financing is aligned with or in conflict with the need to keep undeveloped fossil fuels in the ground.

Furthermore, nothing in the Proposal contemplates or demands divestment from current oil and gas companies; it only asks the Company to establish a policy of proactive measures to ensure that its financing services do not support new fossil fuel development. The proposal is agnostic as to which clients the Company provides financing to. For instance, to the extent that oil and gas companies are developing renewable or clean energy projects, there is no requirement in the Proposal that would necessitate ending the financing of those clients. Indeed, as the IEA has itself pointed out:

> The expertise of the oil and natural gas industry fits well with technologies such as hydrogen, CCUS and offshore wind that are needed to tackle emissions in sectors where reductions are likely to be most challenging.[30]

A compelling demonstration of the flexibility and discretion afforded by the Proposal is contained in the UNEP FI "credible commitments" document. UNEP FI in its credible net zero commitments guidance notes that there are multiple possible pathways to credible alignment by financial institutions including an absolute contraction approach, an economic intensity-based approach, a capacity or technology based approach, a portfolio coverage approach and sectoral alignment. *Whichever of these pathways the board and management should choose, new fossil fuel development is excluded – it is not consistent with 1.5°C alignment.*[31]

The Proposal is squarely on target for a shareholder assessment of this key vulnerability in the Company's strategy to date. As Staff Legal Bulletin 14 L put it: "This approach is consistent with the Commission's views on the ordinary business exclusion, which is designed to preserve management's discretion on ordinary business matters but not prevent shareholders from providing high-level direction on large strategic corporate matters."

Significant Policy Issue Analysis and "Products and Services"

The Company Letter inaccurately asserts that the Staff should permit exclusion under Rule 14a-8(i)(7) of the shareholder proposal as relating to the products and services offered for sale by the company as a financial services company.

Contrary to the Company's assertion, the Staff has made it clear in legal bulletins and in precedents that proposals directed to "nitty-gritty" aspects of the company's business, including products or services offered, are not excludable to the extent they are focused on significant policy issues and do not attempt to micromanage business relationships. Thus, the current Proposal, which does not instruct the Company as to which clients it should serve but only seeks a policy for lending and underwriting that is consistent with global benchmarks and Company's stated commitments and targets, does not impinge on the ordinary business of the company in a manner that renders it excludable.

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[30] https://www.iea.org/reports/net-zero-by-2050

[31] The UNEP FI notes that there is no universal pathway to 1.5 degrees and that each company must tailor its pathway to its own circumstances.

The Proposal does not attempt to dictate lending or underwriting services or customers. Although such decisions are "nitty-gritty" for the company, where the focus of the proposal is entirely on a significant policy issue, the fact that it may touch on issues related to products and services offered does not cause it to be excludable. Staff Legal Bulletin 14H, October 22, 2015, made this clear:

> [T]he Commission has stated that proposals focusing on a significant policy issue are not excludable under the ordinary business exception "because the proposals would transcend the day-to-day business matters and raise policy issues so significant that it would be appropriate for a shareholder vote." [Release No. 34-40018] Thus**, a proposal may transcend a company's ordinary business operations even if the significant policy issue relates to the "nitty-gritty of its core business**." [Emphasis added]

The potential for the proposal to touch on a company's products or services is one such "nitty-gritty" issue that does not lead to exclusion when the proposal clearly focuses on a significant policy issue facing the company. The same type of ordinary business objection was unsuccessfully asserted in *J.P. Morgan Chase (February* 28, 2020) where the proposal requested that the company issue a report outlining if and how it intends to reduce the GHG emissions associated with its lending activities in alignment with the Paris Agreement's goal of maintaining global temperature rise below 1.5 degrees Celsius. The company had argued that the proposal impermissibly addressed the offering of products and services, an ordinary business matter. As in the present case, the company's argument cited the same cases in which the proposal touched on products and services but lacked an overriding significant policy issue,[32] or where the proposal sought to dictate outcomes at the company in the offering of particular products or services.[33] The Staff rejected the ordinary business argument.

Since the current Proposal raises the significant policy issue of climate change and does not dictate outcomes, the Proposal is distinguishable from the cases raised by the Company and is not excludable on this basis. The Staff has long determined that proposals addressing climate risk are appropriate for financial services companies so long as such proposals do not delve into the individual application of such policies to customers. For instance, in *PNC Financial Services Group, Inc.* (February 13, 2013) the proposal requested that the Board report to shareholders PNC's assessment of the greenhouse gas emissions resulting from its lending portfolio and its exposure to climate change risk in lending, investing, and financing activities. The Staff determined that the proposal was not excludable because it addressed the significant policy issue of climate change. PNC had argued, as the Company does here, that the proposal micromanaged the business or related to products and services. The Staff rejected the claim.

Significantly, the focus of a proposal on a policy level rather than directing the Company's relations with particular suppliers or customers is sufficient to avoid the products and services exclusion. For example, in *TJX Companies (*April 9, 2020) the proposal requested that the board commission an independent analysis of any material risks of continuing operations without a company-wide animal welfare policy or restrictions on animal-sourced products associated with animal cruelty. The company objected that the proposal was excludable as relating to sales of particular products, but the proponent effectively argued

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[32] *Hewlett-Packard Co.* (Jan. 23, 2015), in which the Staff concurred with the exclusion of a proposal requesting that the board provide a report on the company's sales of products and services to certain foreign entities, with the Staff noting that the proposal related to ordinary business and "does *not focus* on a significant policy issue" (emphasis added).

[33] S*ee also Bank of America Corp. (Trillium)* (Feb. 24, 2010), where the Staff concurred in the exclusion under Rule 14a-8(i)(7) of a proposal seeking analysis of the company's implementation of its mountain top removal policy "beyond environmental issues", i.e., whether to extend credit to particular customers.

that the focus of the proposal on a clear, significant policy issue for the company caused the proposal to transcend ordinary business.

This followed a long line of prior staff decisions. It is well-established that a proposal is not excludable merely because it deals with the sale of a company's products or services where significant social policy issues are implicated--as they are here.

The current Proposal is in some ways similar to the proposal in *J.P. Morgan Chase (*March 13, 2020) where the proposal asked JPMorgan Chase to describe how it plans to respond to rising reputational risks for the Company and questions about its role in society related to its involvement in Canadian oil sands production, oil sands pipeline companies, and Arctic oil and gas exploration and production. This was not excludable as focused on ordinary business despite a similar relationship to products and services as in the current proposal. One might ask whether the current proposal's more direct request to adopt a policy alters this relationship. It is clear that it does not — regardless of whether a proposal is cast as a request for a report, or a request for policies, a proposal should abide by the requirements of the rule to state the request in an advisory manner and state as clearly as possible what investors are requesting.

In fact, we see the same logic applied in *Bank of America Corporation* (February 23, 2006) where the proposal requested that the board develop higher standards for the securitization of subprime loans to preclude the securitization of loans involving predatory practices. Despite the focus on establishment of a *particular policy*, the staff nevertheless rejected the ordinary business/products and services argument. If a proposal addresses a transcendent social policy issue, and even if it addresses products and services, shareholders are expected to describe it as clearly as possible in terms of what they would like the company to do, as was done in the precedent and the current proposal.

Even a proposal that expressly seeks to ban a particular product or service of a company, a more restrictive request than the current proposal, may transcend ordinary business if it clearly focuses on a significant policy issue relevant to the company. For example, in *Amazon.com Inc*. (March 28, 2019) a proposal that was clearly directed toward a company product was found non-excludable. The proposal requested that the board prohibit sales of facial recognition technology to government agencies unless the board concludes, after an evaluation using independent evidence, that the technology does not cause or contribute to actual or potential violations of civil and human rights. An ordinary business claim similar to the Company Letter on the current Proposal was rejected, and rejected again on request for reconsideration. The proponent in opposition to the request for reconsideration wrote: "The Company's Amazon Web Services (AWS) segment is the leading cloud computing company, and is integrating facial recognition software to its services, which the Proposals assert is being done at risk to civil liberties, privacy and public trust in the Company's products and services."

Similarly, proposals seeking to halt the sale of food containing GMO's have been found not to be excludable as addressing ordinary business because of the transcendent policy issue - public concern about the use of and safety of GMO's. Relevant to the present matter is *Quaker Oats Company* (March 28, 2000), in which the proposal requested that the board (1) adopt a policy of removing genetically engineered crops, organisms, or products thereof from all products sold or manufactured by Quaker, where feasible, until long-term testing has shown that they are not harmful to humans, animals, and the environment, with the interim step of labeling and identifying these products, and (2) report to shareholders by August 2000. The Staff was unable to concur that the company was entitled to exclude the proposal in reliance on Rule 14a-8(i)(7), due to the presence of significant policy issues. The context -- a lack of proven safety -- is relevant in the present instance as well.

Another example was the request of *Yahoo! Inc.* (April 5, 2011) where the company requested permission to omit a shareholder proposal from its 2011 proxy materials, which directed the company to formally

adopt human rights principles to guide its business in China and other repressive countries. Despite the potential impact on products and services offered in China and elsewhere, the Staff concluded that the proposal focused on the significant policy issue of human rights and was not excludable under Rule 14a-8(i)(7).

Analogous to the current proposal was the proposal in *Bank of America Corporation* (February 22, 2008) on implementation of the equator principles. Proposal requested a report to "describe and discuss how Bank of America's implementation of the Equator Principles has led to improved environmental and social outcomes in its project finance transactions." Bank of America Corporation argued among other things that the proposal related to the Company's ordinary business operations, namely the extension of credit and credit decisions. The staff was unable to accept these views and concluded that exclusion of the proposal from proxy materials was not appropriate.

Similarly, in *Bank of America (*February 26, 2009) the proposal directly focused on requesting a report to shareholders evaluating with respect to practices commonly deemed to be predatory, the company's credit card marketing, lending and collection practices and the impact these practices have on borrowers. Despite the focus on products and services, the prominence of predatory and subprime lending as an issue of concern transcended the ordinary business concern.

The Staff has long recognized that shareholder proposals may properly address business decisions regarding the sale of products where significant policy issues are at issue. *See e.g., Kimberly-Clark Corp.* (Jan. 12, 1988); *Texaco, Inc.* (February 28, 1984); *American Telephone and Telegraph Company* (December 12, 1985); *Harsco Corporation* (January 4, 1993); *Firstar Corporation* (February 25, 1993). In Staff Legal Bulletin No. 14C, the Division considered proposals related to the environment and public health, which it had previously found to involve significant policy considerations, and advised that "[t]o the extent that a proposal and supporting statement focus on the company minimizing or eliminating operations that may adversely affect the environment or the public's health, we do not concur with the company's view that there is a basis for it to exclude the proposal under rule 14a-8(i)(7)." SEC, Division of Corporation Finance, Staff Legal Bulletin No. 14C.

Rule 14a-8(i)(10)

The Company Letter asserts that the Proposal may be excluded from the 2022 Proxy Materials as substantially implemented pursuant to Rule 14a-8(i)(10). In order for the Company to meet its burden of proving substantial implementation pursuant to Rule 14a-8(i)(10), it must show that its activities meet the guidelines and essential purpose of the Proposal. The Staff has noted that a determination that a company has substantially implemented a Proposal depends upon whether a company's <u>particular policies, practices, and procedures compare favorably with the guidelines of the Proposal</u> (*Texaco, Inc.,* Mar. 28, 1991). Substantial implementation under Rule 14a-8(i)(10) requires a company's actions to have satisfactorily addressed *both* the proposal 's guidelines and its essential objective. See, e.g., *Exelon Corp.* (Feb. 26, 2010).

Thus, when a company can demonstrate that it has already taken action that meets most of the guidelines of a proposal and the proposal's essential purpose, the Staff has concurred that the proposal has been "substantially implemented." In the current instance, the Company has substantially fulfilled *neither* the <u>guidelines</u> *nor* the <u>essential purpose</u> of the Proposal.

Guidelines and Essential Purpose of the Proposal

The Proposal requests that Morgan Stanley's Board of Directors adopt a policy by the end of 2022 committing the company to proactive measures to ensure that the company's lending and underwriting do not contribute to new fossil fuel development, consistent with fulfilling the United Nations Environmental Program Finance Initiative ("UNEP FI") recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

The UNEP FI 2021 report entitled "Recommendations for Credible Net-Zero Commitments from Financial Institutions"[34] provides clear guidance and benchmarks for issuers, and for their investors, in assessing whether current company pledges are matched by commitments that have credibility considering the global climate agreements and goals. The UNEP FI report is geared toward a clear benchmark of financial institution credibility on their net zero commitments, making it clear that one of the most important benchmarks of credibility is to "align as soon as possible":

> A financial institution establishing a net-zero commitment should begin aligning with the required assumptions and implications of IPCC 1.5°C no/low overshoot pathways as soon as possible. This is because the pathways require immediate actions to have a realistic chance of limiting warming to 1.5°C. **This would include, for example, the immediate cessation of any new fossil fuel investments, and rapid decommissioning of remaining fossil fuel production as indicated by the scenarios**. [Emphasis added]

Furthermore, financing of new fossil fuel exploration and development is not consistent with the IEA's NZE Scenario, which the Company used to establish its interim 2030 emission reduction targets.

Thus, the guidelines and essential purpose of the Proposal require the adoption of a policy that is benchmarked against and aligned with the UNEP FI and IEA guidelines.

Company Letter Distorts Essential Purpose

The Company Letter states the Company instead believes that:

> the Proposal's "essential objective" is for the Company's 'Board of Directors [to] adopt a policy by the end of 2022' that contains measures relating to fossil fuel development, 'consistent with...the International Energy Agency's Net Zero Emissions by 2050 Scenario' and science or science-based targets.' [Emphasis added]

However, this distorts the "essential purpose" of the proposal. The Proposal does not request that the company adopt a policy containing measures *relating* to fossil fuel development. Instead, the Proposal requests that the Company adopt a policy *consistent* with fulfilling the UNEP FI and IEA benchmarks.

The Company Letter on page 9 states that "as older oil and gas sources are wound down, continued investment in newer and more efficient resources will be required for a period of time. As a result, new oil and gas development will be necessary and will occur even under the IEA 2050 scenario." These statements are inconsistent with the UNEP FI and IEA benchmarks.

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[34] https://www.unepfi.org/publications/recommendations-for-credible-net-zero-commitments-from-financial-institutions/

Environmental and Social Policy Statement

Morgan Stanley's Environmental and Social Policy Statement (ESPS)[35] includes two policies that prohibit financing of specific fossil fuel transactions — development of *new thermal coalmine development* and new oil and gas development *in the Arctic*.

However, under the UNEP FI guidelines for ensuring financial institutions have credible commitments to net zero, no new fossil fuel investments may be made, of any kind. Clearly the Company's current ESPS, in limiting only two very specific types of fossil fuel development, falls short of the UNEP FI and IEA guidelines. The ESPS does not prevent Morgan Stanley from contributing to a wide array of new fossil fuel development through its lending and underwriting activities.

Net Zero Target Methodology

The Company's commitment in 2020 to reach "net zero finance emissions by 2050" and its related emission reduction targets for carbon intensive sectors do not fulfill the guidelines or essential purpose of the Proposal.

The Company's intensity-based target metric allows for an *increase in absolute emissions* at a time when emissions need to be drastically cut. Morgan Stanley's targets ignore an essential condition for aligning with the UNEP FI and IEA guidelines: stopping funding for the expansion of fossil fuels. However, the details of the Company's targets allow it to *increase* the financing of fossil fuels development by using emission intensity metrics, not absolute emission metrics. The Company has repeatedly highlighted the flexibility that its own target metrics provide. **This approach actually allows the company to *assert* climate alignment even as it may continue to fund *unaligned* new fossil fuel development.** For instance, "We chose an approach that measures our financed emissions relative to total lending, as opposed to an absolute emissions approach, allowing the size of our lending capabilities to remain unconstrained."[36] "Using an intensity approach properly incentivizes Morgan Stanley to proactively work with our clients on climate transition opportunities, not simply reduce our emissions by withdrawing capital from carbon-intensive sectors."[37]

Simply put, Morgan Stanley has not taken any concrete action to reduce its absolute emissions. Although the Company has made the net zero commitment and published interim targets, neither the net zero commitment nor the interim targets prevent Morgan Stanley from actually contributing to new fossil fuel development through lending and underwriting activities.

The concerns about Morgan Stanley's future financing activities are not hypothetical, but are based on the Company's financing practices to date. Between 2016 and 2020, Morgan Stanley provided $111 billion in lending and underwriting to the fossil fuel industry, 12th among global banks. Its top fossil fuel clients over that time included ExxonMobil ($8.3B), Shell ($6.6B), BP ($4.2B), and Saudi Aramco ($3.9B).[38]

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[35] *See* Environmental and Social Policy Statement (Updated: December 2020) *found at* https://www.morganstanley.com/content/dam/msdotcom/en/about-us-governance/pdf/Environmental_and_Social_Policy_Statement_December_2020.pdf

[36] *See* Reaching Net-Zero Financed Emissions *found at* https://www.morganstanley.com/about-us/sustainability-at-morgan-stanley/net-zero-financed-emissions

[37] *See* Methodology for Morgan Stanley's 2030 Interim Financed Emissions Targets on the Path to Net-Zero *found at* https://www.morganstanley.com/content/dam/msdotcom/about-us/netzero/Morgan-Stanley-Net-Zero-Target-Methodology.pdf

[38] Data from https://www.bankingonclimatechaos.org/

These firms are among oil and gas companies with the largest current expansion plans as ranked by their exploration capital expenditures and the amount of resources under development.[39]

Morgan Stanley, like other large financial institutions, used IEA's net zero energy scenario (NZE Scenario) to establish 2030 emission targets for three sectors of its lending portfolio including the energy sector:

> We used the absolute IEA NZE emissions pathways for oil and gas to define the Energy sector's 2030 interim target. These roadmaps describe the technological advances, fuel transition and operational efficiencies that companies we lend to in these subsectors will need to make in order to reach net-zero emissions by 2050.[40]

The NZE Scenario is a pathway for the world to achieve net zero emissions by 2050. The pathway includes milestones, or priority actions that need to be taken in the next three decades, including stopping new developments of oil, gas and coal:

> Beyond projects already committed as of 2021, there are no new oil and gas fields approved for development in our pathway, and no new coal mines or mine extensions are required. The unwavering policy focus on climate change in the net zero pathway results in a sharp decline in fossil fuel demand, meaning that the focus for oil and gas producers switches entirely to output – and emissions reductions – from the operation of existing assets.[41]

Institutions that use the NZE Scenario in setting their emissions targets need to follow through with policies and actions that are consistent with the pathway; otherwise their targets are not credible and not consistent with net zero emissions by 2050.

Morgan Stanley and its energy sector clients will need to take actions that are consistent with the NZE Scenario for the bank's emission targets to be credible and consistent with its commitment of net zero emissions by 2050. Given IEA's requirement that no new fossil fuel supply investments be made after 2021, a policy ensuring that Morgan Stanley's lending and underwriting do not contribute to new fossil fuel development is a necessary complement to its targets. Without such a policy, Morgan Stanley's emissions targets and net zero commitment are not credible. It appears that the Company intends to leave substantial leeway to continue financing new fossil fuel development.

Staff Precedents Confirm That the Proposal Is Not Excludable

Staff decisions confirm that when it comes to climate change proposals which contain guidelines requesting reporting geared to a specific set of concerns such as the development of targets aligned with external benchmarks, a failure to address the guidelines of the Proposal are a basis for rejecting a substantial implementation claim.

The Company's attempt to treat the Proposal as substantially implemented is similar to *Dominion Resources*, (February 11, 2014) where the Staff held that the proposal was not excludable under Rule 14a-

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[39] *See* data from Global Oil & Gas Exit List *found at* gogel.org

[40] *See* Methodology for Morgan Stanley's 2030 Interim Financed Emissions Targets on the Path to Net-Zero *found at* https://www.morganstanley.com/content/dam/msdotcom/about-us/netzero/Morgan-Stanley-Net-Zero-Target-Methodology.pdf

[41] *See* IEA Net Zero by 2050 A Roadmap for the Global Energy Sector

8(i)(10). The proposal requested the Board of Directors to "adopt quantifiable goals, taking into account International Panel on Climate Change guidance, for reducing total greenhouse-gas emissions" and to issue a report. Dominion argued that it had substantially implemented the proposal because it had adopted an "integrated strategy" regarding greenhouse gas (GHG) emissions and had goals set for renewable energy targets across its energy portfolio. Further, it had adopted a range of measures that would have the effect of decreasing its emissions, including converting coal plants to biomass, retiring others, and installing solar energy and fuel cell facilities. Dominion argued that it had substantially implemented the proposal based on their existing reporting and plans, and efforts to reduce carbon intensity. It was noted by the proponent that the renewable power standards the company planned to meet could allow total GHG emission to rise. As in the present case, the net effect was not alignment with the international guidance or the guidelines and purpose of the proposal. The SEC held that the proposal had not been substantially implemented, noting that the proposal requested "that the board adopt quantitative goals, taking into account International Panel on Climate Change guidance, for reducing total greenhouse-gas emissions from the company's products and operations and report on its plans to achieve these goals."

Similarly, in *Alpha Natural Resources, Inc.* (March 19, 2013) the proposal requested that the company prepare a report on the company's goals and plans to address global concerns regarding fossil fuels and their contribution to climate change, including analysis of long- and short-term financial and operational risks to the company and society. The Staff did not find substantial implementation where the company had failed to disclose any analysis of long- and short-term financial and operational risks to the company and society. See also, *Dominion Resources, Inc.* (February 17, 2017 - two decisions), *The Middleby Corporation* (February 07, 2017), *The AES Corporation* (January 11, 2017), *Exxon Mobil Corporation* (March 22, 2016 - two decisions), *Chevron Corporation* (March 11, 2016), *Hess Corporation* (February 29, 2016), *Lowe's Companies, Inc.* (March 10, 2017).

A company can do extensive reporting on an issue and still <u>not</u> be considered to have substantially implemented a proposal seeking a report within the same issue area. For instance, in *Chesapeake Company* (April 13, 2010) the company asserted that its extensive web publications constituted substantial implementation of the proposal on natural gas extraction. The Staff concluded that despite a volume of writing by the company on hydraulic fracturing, the matter was not substantially implemented given the guidelines of the proposal. Numerous other company attempts to exclude proposals under Rule 14a-8(i)(10) have failed where the company has provided public disclosure of some, but not all, of the elements of reporting requested. See for instance *Marathon Oil Corporation* (January 22, 2013); *Nike, Inc.* (July 5, 2012) (requesting reports on lobbying or political contributions and expenditures); *Southern Company* (March 16, 2011) (proposal requesting a report on the company's efforts, above and beyond current compliance, to reduce environmental and health hazards associated with coal combustion waste was not substantially implemented by existing report on coal combustion byproducts or other disclosures associated with the impacts of coal where reports did not provide the specific information requested in the proposal); *3M Company (March 2, 2005)* (proposal seeking actions relating to eleven principles on human and labor rights in China was not substantially implemented despite the fact that the company had its own set of comprehensive policies and guidelines on these issues); *ConocoPhillips* (January 31, 2011) (the proposal's objective that the company prepare a report on public safety, including "the Board's oversight of" a variety of related issues, was not substantially implemented where company had taken a significant number of steps to reduce the risk of accidents and reported to stockholders and the public, but only made passing reference to the Board's role).

Misleading Communications Do Not Substantially Implement a Proposal

The Company's efforts to assert substantial implementation, in this instance, fail for an additional reason. To the extent that the Company would assert to investors that its existing disclosures fulfill the Proposal,

they would be significantly misleading. For a proposal to be substantially implemented by a company's actions, there is an underlying assumption that the information provided to investors should be materially complete and non-misleading.[42] In this instance, any assertion that the Company's actions are in fulfillment of the Proposal and in alignment with the external benchmarks would be misleading, given the clear statements from both IEA and UNEP FI that alignment and credibility necessitate no new fossil fuel development.

In sum, Morgan Stanley's publicly disclosed commitments, targets and policies fail to substantially implement the Proposal's request. Nothing in the company's statements and reports indicate a plan to limit financing for new fossil fuel development either immediately or in the future. Therefore, it cannot be credibly asserted that the Company has substantially implemented the Proposal under Rule 14a-8(i)(10).

CONCLUSION

As demonstrated above, the Proposal does not violate Rule 14a-8(i)(7) or Rule 14a-8(i)(10). It is not excludable under Rule 14a-8. It is consistent with the rights and responsibilities of investors to assess the congruence of portfolio companies' performance with their climate pledges. It is an investor due diligence action for the fiduciaries who have adopted ESG principles. Ultimately, the ability of a shareholder proposal to produce beneficial change at a corporation is grounded in a fundamental test – whether shareholders vote in favor of the proposal. This inevitably turns on shareholders' assessment of whether the proposal will advance value on a short- or long-term basis, whether at the individual company or across the economy. We urge the Staff to deny the Company's no action request.

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[42] See *The Coca-Cola Co.* (Feb. 21, 2019). In particular, the company's ostensibly "implementing" communications should not raise significant issues under Rule 14a-9, the prohibition against false or misleading statements and omissions in conjunction with the publication of the proxy statement. § 240.14a-9 False or misleading statements. No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting or other communication, written or oral, containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.

THE PROPOSAL

Resolved: Shareholders request that the Board of Directors adopt a policy by the end of 2022 committing to proactive measures to ensure that the company's lending and underwriting do not contribute to new fossil fuel development, consistent with fulfilling the United Nations Environmental Program Finance Initiative recommendations to the G20 Sustainable Finance Working Group, and the International Energy Agency's Net Zero Emissions by 2050 Scenario, for credible net zero commitments.

Supporting Statement

Morgan Stanley "recognizes that climate change is occurring, and acknowledges the scientific consensus…that greenhouse gases emitted by human activities are the primary driver. We recognize the benefits of helping to reduce greenhouse gas emissions as climate change poses significant risks to the global economy."[43] Morgan Stanley is a member of the Net Zero Banking Alliance (NZBA), for which our CEO committed to align with pathways consistent with a maximum temperature rise of 1.5 degrees Celsius above pre-industrial levels, utilizing decarbonization scenarios from "credible and well-recognized sources."[44]

However, membership in the Alliance does not necessarily equate with alignment with global climate goals. The United Nations Environmental Program Finance Initiative (UNEP FI), which convenes the NZBA, published an Input Paper to the G20 Sustainable Finance Working Group which defines credible net zero commitments of financial institutions, including: "A financial institution establishing a net-zero commitment should begin aligning with the required assumptions and implications of IPCC 1.5°C no/low overshoot pathways as soon as possible….All no/low overshoot scenarios indicate an immediate reduction in fossil fuels, signalling that investment in new fossil fuel development is not aligned with 1.5°C."[45] Another of the world's most credible sources, the International Energy Agency (IEA), in its Net Zero Emissions by 2050 Scenario (NZE), states that "no fossil fuel exploration is required and no new oil and natural gas fields are required beyond those that have already been approved for development."[46] Morgan Stanley has restricted financing for new coal operations and Arctic drilling, but has no policy to halt financing any new oil and gas exploration and development. Morgan Stanley is the fifth-highest U.S. financier or facilitator of companies expanding fossil fuels, according to the Banking on Climate Chaos report.[47]

Morgan Stanley faces two associated problems: first, its prominence in asserting climate leadership flies in the face of its actions, creating reputational risk from accusations of greenwashing; second, in underwriting projects which are unneeded under the UNEP FI recommendations or the IEA NZE scenario, it is knowingly loading potentially stranded assets onto its clients' balance sheets, creating litigation risk.[48] In this regard, investors need to know that Morgan Stanley's lending and underwriting policies are consistent with its own net zero commitment.

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[43] https://www.morganstanley.com/about-us-governance/Environmental_and_Social_Policy_Statement_December_2020.pdf, at 10.
[44] https://www.unepfi.org/wordpress/wp-content/uploads/2021/04/UNEP-FI-NZBA-Commitment-Statement.pdf
[45] https://g20sfwg.org/wp-content/uploads/2021/10/2021-UNEP-FI.-Recommendations-for-Credible-Net-Zero-Commitments.pdf, at 15.
[46] https://iea.blob.core.windows.net/assets/88dec0c7-3a11-4d3b-99dc-8323ebfb388b/WorldEnergyOutlook2021.pdf, at 100.
[47] https://www.ran.org/wp-content/uploads/2021/03/Banking-on-Climate-Chaos-2021.pdf, at 38.
[48] https://www.justice.gov/opa/pr/goldman-sachs-agrees-pay-more-5-billion-connection-its-sale-residential-mortgage-acked

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February 18, 2022

Re: Shareholder Proposal Submitted by the Sierra Club Foundation

Office of Chief Counsel
Division of Corporation Finance
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Ladies and Gentlemen:

On behalf of Morgan Stanley, a Delaware corporation (the "**Company**"), we are writing to respond to a letter from Sanford J. Lewis on behalf of the Sierra Club (the "**Proponent**") dated February 10, 2022 (the "**Proponent Response Letter**") with respect to the request from the Company, dated January 14, 2022 (the "**No-Action Letter**"), regarding exclusion of a shareholder proposal (the "**Proposal**") submitted by the Proponent for inclusion in the proxy materials the Company intends to distribute in connection with its 2022 Annual Meeting of Shareholders (the "**2022 Proxy Materials**"). Capitalized terms not defined herein are used as defined in the No-Action Letter. Copies of the No-Action Letter and the Proponent Response Letter attached hereto as Exhibit A.

I. As Described in the No-Action Letter, the Proposal Impermissibly Micromanages the Company.

The Proponent Response Letter recognizes that proposals that "encroach too far" on Board and management discre[tion]" would constitute micromanagement under Rule 14a-(i)(7), but claims that the Proposal simply "benchmarks" and "encourages," that uses wording that is "neither too specific nor constraining" of Board and management discretion and provides "ample flexibility" for the "means of implementation." We disagree with that characterization, as the Proponent Response Letter in fact provides additional support that the Proposal micromanages the Company.

The Proponent Response Letter must take pains to try to depict the Proposal as giving management and the Board discretion and flexibility without rigidly dictating a single course of action because a proposal that specifically directs the Company to immediately cease any new fossil fuel financings would indubitably be excluded as impermissibly micromanaging the Company. This is consistent with the Staff's recent decision in *Seagate Technology plc* (Aug. 2, 2021), where the Staff permitted the exclusion of a shareholder proposal that asked the company to "terminate its operations" in China. A proposal requiring a company to stop undertaking a current business activity is recognized as unduly micromanaging a company.

Here, rather than asking the Company directly to stop financing new fossil fuel development because that would clearly violate Rule 14a-8 of the Exchange Act, the Proposal end-runs the rule by requesting that the Company align with external "benchmarks" that the Proponent Response Letter concedes would do exactly that – require the Company to cease any new fossil fuel investments.

The Proponent Response Letter evidences this directive is in the Proposal, by acknowledging in multiple places that asking the Company to align with the standards referenced in the Proposal is intended to cause

the Company to cease any new fossil fuel developments. The Proposal Response Letter's characterizations of these external standards include the following references:

- the UNEPFI states that aligning with its standard would include "the immediate cessation of any new fossil fuel investments" (page 3 of the Proponent Response Letter);
- under the IEA and UNEPFI standards, "it is clear that banks need to expeditiously end support for the expansion of fossil fuel extraction" (page 3 of the Proponent Response Letter);
- under the UNEPFI guidelines for ensuring financial institutions have credible commitments to net zero, "no new fossil fuel investments may be made, of any kind" (page 21 of the Proponent Response Letter); and
- "[w]hichever of these pathways the board and management should choose, new fossil fuel development is excluded." (page 16 of the Proponent Response Letter).

The Proponent Response Letter asserts that the "Proposal *only* seeks to ensure that the Company's financing does not support new fossil fuel development" (emphasis added). There is no discretion that the Board or management can exercise when the Proposal provides only one method to ensure that the Company's financing does not "support" or "contribute" to new fossil fuel development, because it must be done in a manner that would enable the Company to "ensure" aligning with standards that the Proponent Response Letter states would require "the immediate cessation of any new fossil fuel investments." The Company would be forced to cease an existing business activity to implement the "proactive measures" requested in the Proposal.

It cannot be the case that a proposal that specifically asks a company to terminate financing new fossil fuel developments would impermissibly micromanage and be excludable under Rule 14a-8, and yet a proposal that requests alignment with external benchmarks or guidelines that would require those same specific actions would not be excludable. Contrary to the statement in the Proponent Response Letter, the request of the Proposal is "directive," not "advisory." The Proposal imposes specific requirements for action, since the Proponent Response Letter asserts that there is only one method to meet the external standards referenced in the Proposal.

II. As Described in the No-Action Letter, the Proposal Delves Into Complex Matters Not Suitable for Shareholder Input.

The Proponent Response Letter further reinforces the complexity of the standards cited in the Proposal – the UNEPFI recommendations to the G20 Sustainable Finance Working Group and the IEA 2050 Scenario. The Company recognizes that it can be appropriate for shareholder proposals to reference external frameworks, but as previously explained in the No-Action Letter, the Company believes that the standards cited in the Proposal are too complex for shareholders to evaluate when making a voting decision on the Proposal. The frameworks noted in the Proposal contain highly complicated and intricate concepts that bear directly on what shareholders need to understand to make an informed decision. The Proponent Response Letter provides only the most basic of selective explanations about the standards with chosen excerpts that do not begin to delve into the full scope of those standards, and yet even that set of cherry-picked highlights from the standards took several pages for the Proponent to explain, and is already likely be beyond what many shareholders would be able to comprehend when making voting decisions.

CONCLUSION

For these reasons as well as those stated in the No-Action Letter, we believe that the Company may exclude the Proposal.

Respectfully yours,

Ning Chiu

Attachment

cc w/ att: Martin Cohen, Morgan Stanley

Paul Rissman, Sierra Club

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February 22, 2022
Via electronic mail

Office of Chief Counsel
Division of Corporation Finance
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Shareholder Proposal to Morgan Stanley regarding fossil fuel financing on behalf of the Sierra Club Foundation – Supplemental Response

Ladies and Gentlemen:
The Sierra Club Foundation (the "Proponent") is beneficial owner of common stock of Morgan Stanley (the "Company") and has submitted a shareholder proposal (the "Proposal") to the Company. We previously responded to the Company's no action request. I have been asked by the Proponent to respond to the supplemental letter dated February 18, 2022 ("Supplemental Letter") sent to the Securities and Exchange Commission by Ning Chiu of Davis Polk. A copy of this response letter is being emailed concurrently to Ms. Chiu.

First the Supplemental Letter seems to imply that asking a company to align its strategy to an external benchmark ought to be considered micromanagement, if the same request were considered micromanagement in the absence of the benchmark:

> It cannot be the case that a proposal that specifically asks a company to terminate financing new fossil fuel developments would impermissibly micromanage and be excludable under Rule 14a-8, and yet a proposal that requests alignment with external benchmarks or guidelines that would require those same specific actions would not be excludable.

In fact, the *presence of a global benchmark* has precisely the impact that the company says it cannot. The strength of a global benchmark is that it represents an agreed external global goal against which behavior of corporations is measured. A strategic reorientation imposed by an individual investor might constitute micromanagement, but when the United Nations has converged on the need for a strategic reorientation of both governments and corporations, investors echoing that external standard can no longer be said to be micromanaging the company.[1]

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[1] This does not mean that a proposal seeking a strategic reorientation in the absence of a global standard necessarily micromanages. Evaluation is still appropriate against the other related questions as to whether the strategic reorientation, as framed, represents a reasonable deliberation for investors. It doesn't require an external standard for the Staff to understand that a strategic reorientation towards safer behaviors in the face of societal needs is most

Secondly, the Company Letter asserts that such a focus is too prescriptive and the issues of strategic reorientation simply too complex for investors to consider. Again, in consideration of the evidence presented in our prior letter, there is no doubt that the questions presented by the Proposal are well within the scope of appropriate investor deliberation. Indeed, the very essence of the Proposal's ask is at the forefront of public conversations around investing, as reflected in a report published just last week. Although it principally focuses on the role of *European* banks in fossil fuel financing, the paper concludes that the Paris-unaligned financing of fossil fuels in Europe is creating substantial risk for the banks and the global economy:

> **"Current oil & gas expansion plans lead to a lose-lose scenario**. If demand decreases in line with 1.5C scenarios, prices will fall and assets that don't earn their initially promised return will become stranded (the US$145 billion in write downs in 2020 could be a foretaste of greater losses to come in an era of permanently lower demand). On the other hand, if consumption of fossil fuels does not wane to the extent necessary to limit global warming to 1.5C, the economy will suffer from severe physical impacts of climate change. Either way, value will be destroyed for companies and their financiers."[2] [emphasis added]

In this evolving arena, it is 100% evident that shareholders have a need to hold the Company accountable on this strategic issue. As noted in our prior correspondence, the Office of the Comptroller of the Currency has proposed new rules on banks' climate change related disclosures and communications. The Financial Services Forum, an organization of eight of the largest us banks **including Morgan Stanley,** wrote to the OCC on February 14[3] with recommendations to revise the OCC requirements on public communications by banks. The forum wrote:

> The Proposal calls for banks to "ensure that any public statements about their banks' climate-related strategies and commitments are consistent with their internal strategies and risk appetite statements." ….[W]e believe it would be more appropriate for each bank to ensure that public communication of its climate-related strategies is consistent with *the actions the bank is actually taking*.

Although the Forum argues that this requested change is in line with the U.S. securities disclosure

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appropriate for a shareholder proposal. As an example, it has never been seen as micromanagement or excludable ordinary business to ask a utility to end the use of nuclear power. Asking utilities to phase out nuclear power, or even particular plants, has long been understood as being directed toward fundamental strategy with major economic and safety concerns. For example, in *DTE Energy Company* (February 2, 2018) the proposal requested that the Company commission an independent economic analysis of the potential cost avoidance and the potential financial benefit to shareholders and ratepayers of closing the Company's Fermi 2 nuclear power plant prior to the expiration of the Nuclear Regulatory Commission license. The Staff rejected exclusion under rule 14a-8(i)(7) noting economic and safety considerations attendant to nuclear power plants. This followed numerous similar proposals including *Union Electric Company* (February 28, 1984) requesting the company cancel construction of the Company's Callaway Nuclear Power Plant project.

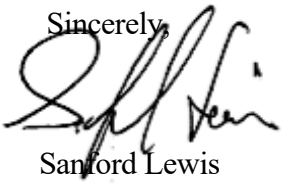
[2] https://shareaction.org/reports/oil-gas-expansion-a-lose-lose-bet-for-banks-and-their-investors

[3] https://fsforum.com/a/media/fsf---occ-climate-principles-comment-letter.pdf

regime, it also appears that this change may undercut banks' accountability for rhetoric around net zero targets. Notably, in line with this concern, the Forum's comments also sought to relieve boards of directors of responsibility for ensuring that corporate public communications are aligned with internal strategies. This legalistic push of the banks themselves, including the Company, away from accountability for consistency between policy and climate communications, with its implications for assessing whether long-term net zero targets are aligned with other policies and commitments, is the core focus of the current Proposal. This issue appears central to a continuing debate that we can anticipate for some time to come. Investors surely must maintain the right to engage through the shareholder proposal process to avoid a risk of marketwide greenwashing.

We stand by our original correspondence, and are persuaded more than ever that the Proposal is not eligible for exclusion under Rule 14a-8(i)(7). We urge the Staff to notify the Company that it is denying the no action request.

Sincerely,



Sanford Lewis