Rights CoLAB

Fight Finance with Finance

A Guide to Using Your Investment Power

March 29, 2022

Editor's Note:

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Introduction

Politically active citizens vote, organize, attend meetings, rallies, and protests, write letters and make telephone calls to their elected representatives. As citizens, these are our political rights. We exercise them in order to have a say over decisions that affect our lives. We also have financial rights granted to us as participants in retirement and benefit plans, as customers of fund families, as shareholders, and even as policy holders of insurance companies. How many of us exercise these financial rights? Widening our focus to include our financial rights along with our political rights has several strong advantages.

First, corporations are powerful, and their decisions affect our lives just like political decisions do. Maybe even more so if you believe that corporations have hijacked our political system through lobbying and political contributions. As investors and beneficiaries, we can alter these decisions.

Second, while we can affect political decisions in our own country, it is much harder to influence the Brazilian government to improve its deforestation policies or stop the Indonesian government from building coal-fired power plants. But corporations have global reach, and a U.S. citizen can become a citizen of the world by influencing corporate behavior.

Third, in our polarized society it's increasingly difficult to exercise our political rights. For example, a progressive who lives in a blue district of a blue state may not be able to effect much change if all her representatives already agree with her. A progressive in a red state has perhaps given up on activism, tired of banging his head against the wall. And at the federal level, we can pretty much forget about accomplishing much of significance. Yet an investor or beneficiary has financial power no matter where they live.

Fourth, while it may be getting harder to be an effective political influencer, it is actually becoming easier to be an effective financial influencer. You may not think of yourself as an investor. During a recent webinar, progressives were asked who they pictured when they thought of an investor. The most popular answer was "an old white man in a business suit." It would have been more accurate if they said "I see an investor when I look in the mirror!"

This guide will discuss your rights as an investor or beneficiary and show you how to exercise those rights. Finance is complicated, and the level of financial literacy in the U.S. is low. It's almost as if "the Man" prefers it that way, so that the sleeping giant of the citizen shareholder never wakes up. Navigating the financial system to create positive change isn't always easy, but it is so powerful that it is always worthwhile to try.

Not only that; citizen investors are now racking up victory after victory, and the trend is accelerating. The most important thing to remember is that you don't have to do this all by yourself. There are many non-profit advocacy organizations and for-profit responsible

businesses that can help you make your efforts more effective. The next section shows a few success stories of what we can accomplish.

Recent Success Stories

Shareholders create change by filing resolutions

One thing that the pandemic has reinforced is the damage that inequality has wreaked upon our society. Corporations can help heal economic inequality by preventing racial, ethnic, and gender discrimination as they hire and promote their workforce. They can also pay their employees a living wage. But if they don't report relevant metrics about their progress, citizens don't have a way to hold them accountable. One way to hold companies accountable is to force them to report their progress through resolutions that shareholders can file at a company's Annual General Meeting (AGM). Companies are accountable to their shareholders, and only a shareholder can file a resolution.

In 2019 a citizen shareholder, assisted by the non-profit shareholder representative As You Sow, filed a resolution with the Fortune 500 used car superstore CarMax, asking for it to report minimum wage and racial, ethnic, and gender representation in the workforce and among executives. CarMax simply agreed, without the resolution ever being voted upon, and that information is now available on the company's website. Citizen shareholders advised by As You Sow achieved similar gains, just by filing resolutions, at Ulta Beauty, the beauty superstore, and high-tech storage company Western Digital.

The power and progress of shareholder resolutions has accelerated rapidly in just the past two years. In 2021, a resolution filed with Yum! Brands — the company that operates Taco Bell, KFC, and Pizza Hut — asked for an accounting of the global health impacts of antibiotic use in Yum!'s animal supply chains. Yum! simply agreed to do the study. A resolution filed with the oil refiner Valero asked the company to tie executive compensation to efforts to reduce climate change, and Valero complied! In fact, almost half of social and environmental-related proposals filed in 2021 received favorable responses from the targeted corporations, without ever being voted on.

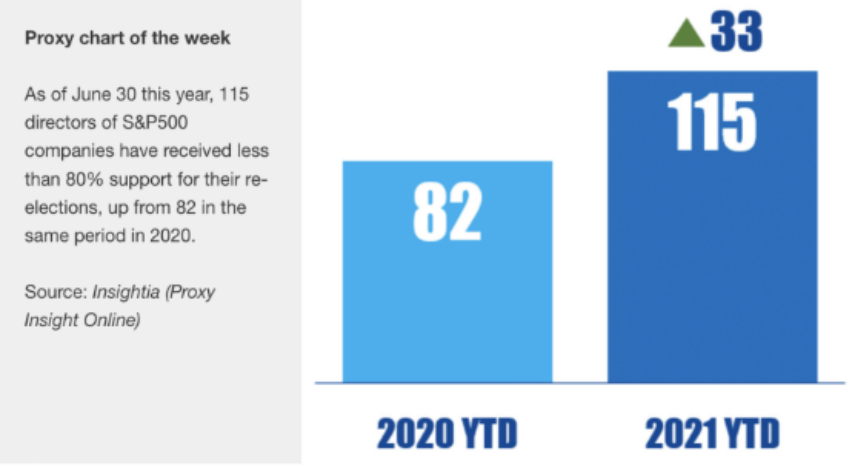
When companies don't agree with a resolution, they generally ask that shareholders vote it down at the company's annual meeting. A noteworthy first in 2021 was that four companies actually recommended that their shareholders vote *for* a resolution. These resolutions concerned greenhouse gas emissions at GE, a racial equity audit at IBM, a deforestation report at the agricultural processor Bunge, and the rights of agricultural workers at Wendy's. All received overwhelming support, and all of these corporations agreed to implement the requests.

Shareholder resolutions aren't binding on U.S. companies, but this doesn't mean that they aren't powerful tools. Companies are always interested in keeping their shareholders

happy. Typically, management takes any resolution receiving 30% or better support seriously. The money manager BlackRock studied resolutions about environmental and social topics and found that two thirds of them were at least partially implemented even with only 30-50% support. In this respect, in the first half of 2021, support for the average environmental or social shareholder resolution exceeded 30%.

Shareholders create change through Board of Director elections

You may think that companies are run by their CEOs and top executives. But who hires (and fires) the CEO? The Board of Directors. Directors also decide how CEOs are compensated, determine overall corporate strategy, and approve the company's financial reports. Directors must be elected to join or stay on a board. Who elects them? The company's shareholders.



Citizens' financial power witnessed another first in 2021: three new directors, nominated by a progressive hedge fund, beat out the management slate at ExxonMobil with the goal of improving its approach to climate change. Among some of the prominent shareholders supporting the new directors were pension funds with citizen beneficiaries (maybe you!) representing New York State public employees, California public employees, and California teachers.[1]

ExxonMobil Annual Meeting, May 26, 2021
Shareholder Proposal Item 10

Shareholders request that the Board of Directors conduct an evaluation and issue a report within the next year…describing if, and how, ExxonMobil's lobbying activities (direct and through trade associations) align with the goal of limiting average global warming to well below 2 degrees Celsius (the Paris Climate Agreement's goal). The report should also address the risks presented by any misaligned lobbying and the company's plans, if any, to mitigate these risks.

[1] "Notice of 2021 Annual Meeting and Proxy Statement," ExxonMobil, 16. Mar. 2021, https://corporate.exxonmobil.com/-/media/Global/Files/investor-relations/annual-meeting-materials/proxy-materials/2021-Proxy-Statement.pdf, page 87

Many of us are enrolled in pension and benefit plans. These plans are very significant shareholders and can advocate for our interests. Through their votes for both resolutions and directors, these citizen shareholder representatives are changing corporate behavior for the better.

Customers and shareholders create change by influencing fund companies

While you may own stock in individual companies, chances are you have more clout as a customer of a mutual fund or exchange-traded fund (ETF). Seventy percent of stock in American companies is owned by "institutional investors." These are mainly mutual funds/ETFs and employer-sponsored retirement plans. Fund families are household names like Vanguard and Fidelity. When you own a mutual fund/ETF, you don't vote directly; your fund votes instead. But you can influence how your fund votes!

Most people have heard of BlackRock, the world's largest fund company. If you own iShares then you are their customer. BlackRock has made significant progress in forcing the companies it owns to be more environmentally and socially friendly (it has further to go!). It didn't decide to do this on its own, though. It faced a great deal of pressure to change.

BlackRock itself is a public company, and representatives of citizen shareholders have filed their own shareholder resolutions with BlackRock to make it vote more progressively. Socially responsible pension funds — who are among BlackRock's largest customers — have threatened to pull their money away. Advocacy groups have protested at BlackRock meetings and offices and delivered petitions, often signed by BlackRock customers. They have persuaded Democratic U.S. Senators to write letters to BlackRock CEO Larry Fink. All of this has borne fruit. In 2020, BlackRock announced important changes to its policies making the company much more active than before in policing corporate behavior.

Investors create change through indirect pressure

Citizen shareholders don't have to own stock in the companies they target, whether through direct ownership or indirectly through funds. They can also partner with advocates who can mobilize shareholders.

The Arctic National Wildlife Refuge has been threatened with oil and gas drilling since a law authorizing drilling was passed in 2017. Not only would this damage a vast tract of pristine land, but it would interfere with a migrating caribou herd upon which a nearby indigenous group depends for its livelihood.

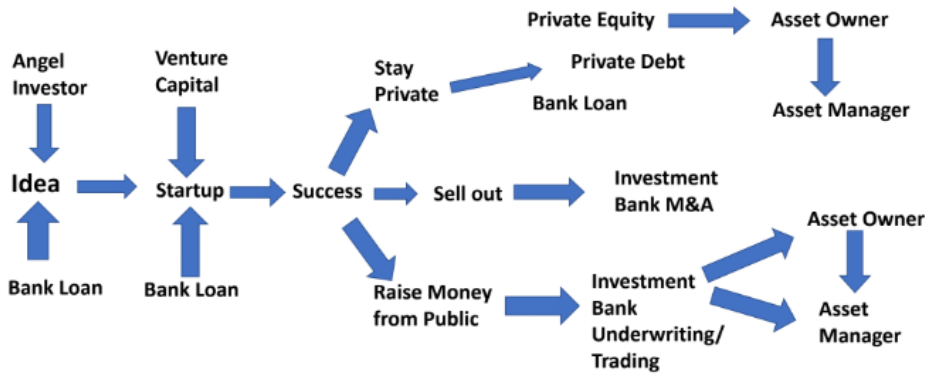
This indigenous group partnered with Sierra Club to lobby banks to commit not to provide loans for Arctic Refuge drilling. Together they not only organized shareholder protests, they also combined their outside and inside strategies by meeting with bank managers to explain their positions. Through these joint efforts, the largest U.S. banks and more than a dozen international banks have made this commitment. It is increasingly unlikely that the refuge will ever see drilling.

These four success stories illustrate that shareholder power works through a tangled web of influence. Shareholders can have direct impact by filing their own resolutions and speaking at annual shareholder meetings. Direct shareholders can vote for resolutions filed by other shareholders. They can even lend their shares to non-shareholders who wish to speak out at meetings. Customers of funds can influence their fund companies to enforce better corporate behavior. Pension fund beneficiaries and 401(k) participants can influence their pension trustees to be responsible investors themselves. And advocates are always standing by to help citizen shareholders accomplish their goals.

These four recent examples of success reflect a strategy called engagement, in which only those who own shares, directly or indirectly, can participate. They mark a growing source of power for social change as citizen shareholders come into their own.

Untangling the Web of Financial Relationships and Rights

Finance is complicated. Each of the many varieties of financial instruments has its own bundle of rights and engagement strategies. I will lay out several them in this section. If you are financially sophisticated, you can probably skip to the next section. Or maybe it will stimulate you to come up with your own actions!



It may be useful to begin by thinking about the origins of corporate finance. In other words, if someone wants to start a company, how do they get the money to do it? Suppose you are thinking of starting a business. While you may have a great idea, it may not take off right away (it hardly ever does). You might have to advertise. You may want to hire staff to help you. You may need to buy supplies and inventory, and pay rent. This

may all be required before your business generates any revenue. If so, what does your business need to survive? It needs an infusion of money, or capital. Maybe it comes out of your own pocket. Or maybe you need, or choose, to get some capital from outside sources. This is investment, or corporate finance. I find it useful to conceptualize corporate finance along three dimensions. Perhaps you will, too.

The Three Dimensions of Corporate Finance

The first dimension of corporate finance is the primary versus secondary dimension, which gives rise to markets. When an individual needs outside financing to start a business, they have two choices: they can take out a loan, or offer a piece of the company to an investor in exchange for cash. The first alternative is also known as debt. The second alternative is termed equity. An infusion of cash directly into a company, whether a debt or equity investment, is a primary investment.

If there were only primary investments, a problem would rapidly arise. Financiers would run out of capital, because they had already committed all of it to their primary investments. They would have nothing left for additional investments, and that would mean very few businesses would be able to access enough capital. If financiers could sell these investments to someone else, though, they could replenish their capital and invest in yet more businesses.

The need for primary investors to sell their investments to others, so that they can replenish their capital and make more investments, gave rise to markets. Markets are simply a way for primary investors to replenish their capital by selling their debt or equity to other, secondary market participants. These participants are then free to buy and sell to other investors. When participants buy and sell in secondary markets, cash goes to market participants, not to businesses. Progressives may consider this simple speculation. But more businesses can access financing because this secondary market exists.

The second dimension, touched upon above, is debt versus equity. Corporate management makes decisions about how much of the business to finance with debt and how much with equity. Sometimes financing with debt is very expensive, as when interest rates are high, or when the business doesn't have a good credit profile. Currently, interest rates are low, which incentivizes companies to finance with debt.

Financing with equity can be more desirable because a company can access capital without having to pay interest on its debt. For this reason, young companies with little cash may prefer equity financing. Equity financing, however, comes with a big disadvantage: dilution. When a business sells an equity stake, all of its current shareholders now own less than before, so they have less say in how the company is run and a smaller stake in its profits. Many companies hope to make enough money to buy back shares from their direct investors, or from secondary investors on the market, in order to avoid dilution.

When you buy a stock, you own a piece of the company. You become an "equity holder" — a synonym for shareholder or stockholder. Equity holders have certain governance rights. Only equity holders can attend Annual General Meetings, vote for the Board of Directors, or vote for resolutions. Only equity holders have standing to sue a company for securities fraud.

Citizens can also purchase debt on the secondary market. They can do this by buying and selling corporate bonds. Debt holders don't have governance rights. This doesn't mean, however, that they have no influence over corporate behavior. As we will see later, debt holders can have a great degree of influence!

The third dimension of corporate finance is public versus private. Young companies start out as private companies, unless they are "spun out" of an existing company. They are too small to meet the listing requirements of stock exchanges. As they grow, they may need more equity investors than just the founders and their small circle. To finance with public equity ("go public"), they must have grown large enough to list on a stock exchange (secondary market) in an Initial Public Offering (IPO). Sometimes companies that are already public want to issue additional equity. This is called a "secondary offering," not to be confused with an initial offering, nor with a secondary market!

Another alternative is to turn to "private equity." Some fund managers form private partnerships with a group of other investors and amass a pile of cash to purchase equity stakes in private companies. The manager of the fund is called a "general partner" (GP) and the fund's other investors are called "limited partners" (LPs). Many companies find it desirable to remain private, keeping company control within a small circle rather than diffusing it to the public.

Private companies don't issue public equity, so they don't have citizen shareholders. But who are the LP's? They are most often pension funds. LP's can influence GP's, since they provide the capital. GPs most assuredly influence the private companies they invest in. Often this influence ends badly, as they siphon money from a struggling company until it goes bust, leaving employees jobless.

And who influences the LPs? The citizen shareholder does. Workers and retirees have ways of influencing pension funds to invest responsibly. College endowments are often limited partners, as well. Are you an alum? Colleges love their alums, who form their biggest pool of donors. Have you ever communicated with your alma mater about their responsible investing practices?

And to complicate things even more, some private equity managers are actually public companies. In that case, citizen shareholders can have a direct impact on the behavior of private companies by influencing the GP itself.

Every citizen shareholder should be familiar with one final concept related to corporate finance: the cost of capital. Why would any going concern — successfully selling its products or services, paying its bills, and meeting its payroll — ever want to raise more money? To grow, or invest, in its business: a new factory, more research and development, or improved production processes. Maybe it's a smokestack industry needing an expensive transition to less-polluting facilities. How does management decide whether it is worth spending the money it needs to invest in its future? By comparing the expected benefits of the new investment to the company's cost of capital.

Cost of capital comes in two flavors. One is the cost of debt. If I can make an investment that produces a 7% annual profit, but to get the capital I must borrow at 10% interest, should I go ahead with the investment? Probably not! What if I could borrow at 4%? Then, no problem. The cost of debt is straightforward.

The other flavor of the cost of capital is the cost of equity capital. This is a trickier concept. Basically, the cost of your equity capital is the ratio of your stock price to your profits. Why this is true may best be illustrated with an example: let's say your company wanted to develop a whizzly-gig. You could set up a laboratory and hire people to get the whizzly-gig going, and then build a factory to produce it. On the other hand, there may be a company that already makes whizzly-gigs. It would save a lot of time if you simply bought that company. If you don't have enough cash, and your credit is tapped out, you could issue equity and buy the existing company with your stock.

How do you decide what to do? It all comes down to the concept of dilution, discussed above. If you issue stock, you will dilute the power and profits of your existing shareholders. They won't like that. But, since you are using your stock to acquire the profits of another company, that additional profit may make up for the profits that your existing shareholders lost through dilution. And the way to measure that is to see how much profit gets diluted per share of your equity. If a share comes with lots of profit, there will be a lot of dilution. If a share comes with only a little profit, there won't be much dilution and your existing shareholders will be happy that you used new stock to buy that whizzly-gig company. So the cost of equity capital is measured by the ratio of your stock price to your profits, or what we call the price/earnings ratio (or P/E).

Why does this matter? Some companies have high P/E ratios. That means their shares don't come with much profit, so their cost of equity capital is low. They can easily issue stock to invest in new projects. Suppose a company's stock price goes down, even though its profits remain steady, because shareholders have decided that they don't like owning the company anymore and they sell en masse. Then its P/E ratio declines (P goes down, but E doesn't), and its cost of equity capital rises. It can't invest by issuing equity the way it used to.

Divestment

Most of us already know about the divestment movement, directed largely at fossil fuel investors. Divestment occurs when an investor sells their stock and walks away. This movement has yielded important benefits in raising awareness about the imminent danger of climate change. Divestment proponents often disparage citizen shareholder engagement as a weak strategy. Strictly speaking, divestment and engagement are polar opposites since the less stock a shareholder controls, the less influential their engagement becomes. Stock market divestment and engagement, therefore, are like the two ends of a seesaw.

The cost of capital concept is a pillar of the divestment movement. If everyone sold their Exxon stock, then Exxon's P/E ratio would decline and Exxon wouldn't be able to invest as much in pumping oil, provided they intended to do it by issuing equity. There are, however, two major complications to this argument. First, some companies in bad industries are actually trying to get better, and they can't if the high cost of capital prevents them from investing. Second, the stock market is a secondary financing market. When you buy stock, you aren't sending your cash to the company; you're sending it to someone in the market.

Likewise, when you sell stock, the equity of the company isn't canceled; it goes to another shareholder. You don't know the identity of the new buyer, and you can't control who it is. It could be someone who thinks like you do, or not. These two problems can come together in a seriously damaging way, illustrated by a tale of European oil companies, which I will tell later in this pamphlet. Stay tuned!

Specific Channels of Citizen Influence: Ownership, Indirect Ownership, and FiduciaryRelationships

By now you understand enough about corporate finance that the specific channels where the citizen shareholder can use their influence will become apparent. Let's start with the most direct methods of influence and proceed outwards.

Direct stock ownership

If I owned lots of stock in a company, I could definitely influence that company. But I can still influence a company with only a little bit of stock. In fact, the current rules state that I can file a shareholder resolution with as little as $2000 worth of stock if I have owned it for at least three years. I have personally filed two shareholder resolutions with companies whose stock I own. Both companies agreed to my demands before the resolutions ever came to a vote, so I withdrew them. But I would not recommend that you undertake this course of action on your own.

Submitting a resolution is Byzantine. You must research the right things to ask for or your target can have the resolution legally excluded from the Annual Meeting. It must be the right length. You must be prepared to defend your resolution to the SEC and, if you get far enough, to your fellow shareholders. It can certainly be done, but you must be very committed. If you want to take it this far by yourself, there are helpful guides to consult.

There are much easier ways to use your direct stock holdings, however. There is a well-developed network of shareholder representatives, socially responsible investors, and financial advisors that you can access for help. If you keep your stocks in a brokerage account (rather than a safe deposit box) you can use your brokerage account manager to file shareholder resolutions. For example, Wetherby Asset Management works with shareholder advocates on environmental and social issues, offering their clients opportunities to sponsor resolutions that address these issues. Parametric Portfolio Associates offers a similar service.

Other things you can do with your direct stock holdings include voting for resolutions that other citizens have sponsored, attending annual meetings to comment and question, and even lending your right to speak to activists who speak on your behalf. Your financial advisor can and should be able to help with all of these tasks. There are also financial advisors, like OpenInvest, who keep track of shareholder resolutions for companies you own and send you push notifications when important votes come up that you may be interested in.

Do you have a financial advisor? Are they providing these services for you? Have you asked them about it? If you aren't satisfied with their answers, let them know that 60% of financial advisors' clients switch during their lifetimes, and that you know how to join the majority!

Indirect ownership through mutual funds and ETFs

You may own mutual funds or ETFs outright, or in your IRA or 401(k) or other retirement account. Mutual funds and most ETFs have the same structure: they are formed as investment companies that buy shares of stock or bonds. Individuals in turn buy shares in the fund. We as individuals can't submit resolutions or vote at meetings of the companies in the fund. We can, however, submit resolutions to the fund itself, vote on them, and elect fund directors. In this way, owning a share of a fund gives you identical rights to owning a share of company stock. For example, the same $2000 minimum and three-year minimum holding period requirements apply for filing a resolution at your mutual fund or ETF.

Anti-Genocide Shareholder Proposal Earns up to 25% of Votes at Fidelity

Second year of strong support despite Fidelity's active opposition "stacking the deck against the proposal"

PUBLISHED 07-10-09 SUBMITTED BY INVESTORS AGAINST GENOCIDE

[2] I am a Fidelity Contrafund investor. One day I received an email from the fund announcing a shareholder meeting. I was quite surprised that one of the items I was asked to vote on was a resolution requesting that the Board of Directors avoid holding investments in companies that contribute to genocide or crimes against humanity. This isn't the first time I've heard of such a fund shareholder resolution. In 2017, resolutions were filed with two Vanguard funds requesting a report on their voting policies related to climate change. A similar proposal was also filed with Vanguard in 2020.

While there aren't nearly as many fund shareholder proposals filed as company shareholder proposals, there should be. One reason there are so few is that hardly anyone knows that it can be done (did you?). Another reason is that, in contrast to the shareholder meetings of corporations held each year, fund shareholder meetings are only held when needed. Fund companies generally accumulate all sorts of miscellaneous governance issues over time. Eventually they ask their customers to vote on many items for many funds, but this might only happen once every five to ten years.[3]

Thankfully, this isn't an impediment to influencing fund companies. Corporations like to have happy shareholders, but they don't try very hard to compete for them with other corporations. For funds, though, their shareholders are also their customers. If corporations want to keep their shareholders happy, funds want to keep their customer-shareholders *extremely* happy! Unhappy customers were one of the main reasons that BlackRock promised to place more emphasis on policing bad corporate behavior.

In short, citizen shareholders can influence their fund companies to be better proponents of corporate responsibility. Fund customers can support fund shareholder resolutions when they learn of them; vote for them when they come up; and call and write to their

[2] : "Anti-Genocide Shareholder Proposal Earns Up to 25% of Votes at Fidelity," Investors Against Genocide, 16. Jul. 2009, https://www.csrwire.com/press_releases/27344-anti-genocide-shareholder-proposal-earns-up-to-25-of-votes-at-fidelity

[3] "Top 10 Reasons to Protest BlackRock," CodePink, https://www.codepink.org/top_ten_reasons_to_protest_blackrock

funds asking them to emphasize these social and environmental considerations when they meet with the companies they own in their portfolios, as they do regularly.

Mutual funds/ETFs invest in all sorts of assets, including bonds. Although bond holders don't have voting rights at corporate meetings, bond funds can be powerful. Because interest rates are low, debt is the preferred financing mechanism for companies these days. Every week all sorts of companies issue bonds that are purchased by fund managers.

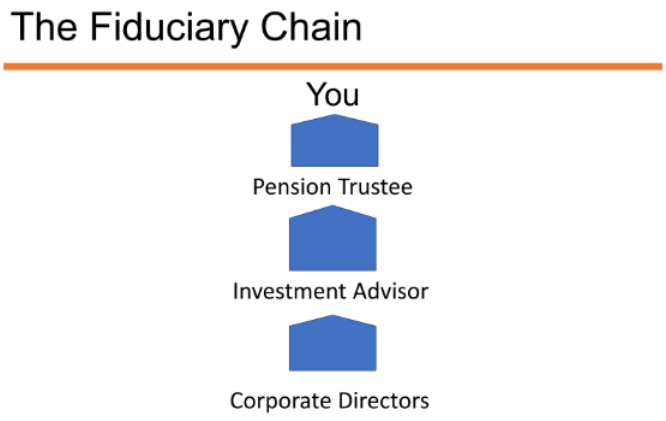
This is where the citizen fund shareholder can exercise leverage. Let your mutual funds know that you don't like it when they finance fossil fuel exploration or private prisons. Bond mutual funds have a great deal of clout in getting companies to behave better when they need debt financing. The citizen fund shareholder can take advantage of that clout.

Many citizen shareholders also have investments in municipal bond funds. These bonds finance public projects that may hurt or help you directly. If you own shares in a municipal bond fund, you can influence government, not just corporations, through your fund ownership.

If you become increasingly frustrated with your fund, you might want to move your money. But be careful; you may incur significant capital gains taxes. If your fund is in an IRA, however, you can dump your mutual fund and switch to another without incurring any tax liability. Several schemes rate mutual funds based on how sustainable they are. Citizen shareholders can pressure their funds to become more sustainable, either by filing and supporting fund resolutions, threatening to move their money, or by exercising their fiduciary relationships, which we will examine next.

Citizen shareholders and their fiduciaries

A fiduciary is essentially a person or organization, like a money manager or mutual fund/ETF, to whom you give money in the hope of getting a financial return, but without actually being sure that you'll ever get it back. This type of business relationship is obviously open to abuse, and that is why your fiduciary has special obligations to you. For example, your fiduciary can't put their own financial interests ahead of yours. You always come first. This is called the duty of loyalty. Another obligation is that your fiduciary must guard against taking imprudent risks with your money. This is called the duty of care. Because fiduciary duty involves both ethical and legal considerations, the fiduciary obligation is "the highest known to the law" (*Donovan v. Bierwirth*, 680 F.2d 263, 272 n.8 (2d Cir. 1982)).



The duty of care is important to the citizen shareholder because if your money manager, mutual fund, or retirement fund trustee isn't protecting you from undue risk to your investments, that is a breach of fiduciary duty. Risk comes in many flavors, such as idiosyncratic risk. This is risk to one or a few of the holdings in your portfolio. For example, if oil prices decline, your oil stocks will go down also. But idiosyncratic risk doesn't affect all companies in the same way. Some, such as airlines, may even benefit when the price of oil goes down. So if you have lots of different kinds of stocks in your mutual fund or 401(k) — also known as being well-diversified — then you can pretty much eliminate idiosyncratic risk.

Another flavor is systematic risk, which affects *all* the holdings in your portfolio. Even if you are well-diversified, you won't be safe. One source of systematic risk is climate change. Climate change will damage the planet enough that at some point global economic activity will decline. This will affect the entire stock market. Another recognized systematic risk is economic inequality. Yet another is the threat to the rule of law. If your fiduciary can prudently protect your fund, 401(k), or pension from these risks, they are obliged to do so.

In 2020 a large Australian pension fund settled with one of its beneficiaries who sued because the fund violated its fiduciary duty to protect against the risk of climate change. Pension trustees in the U.S. are sued constantly for fiduciary breach, meaning it is never far from their minds. You may not be able to move your money from a fund because of tax reasons. You may feel that it isn't worth the effort to start or join a lawsuit. But your voice still matters to your fiduciary, no matter how small or insignificant you think it might be. This is a result of part of the duty of loyalty, known as the duty of impartiality. [4]

Australian climate change lawsuit a 'shot across the bow' of directors and trustees worldwide

DEC 06, 2020

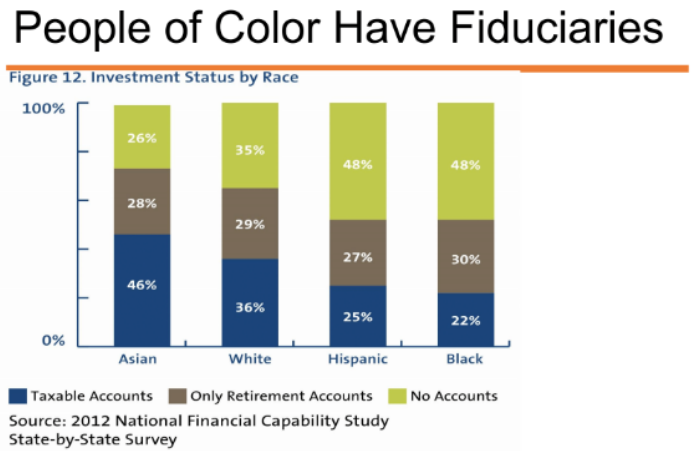
Pension funds, sovereign bonds, banks and mining companies in the crosshair of climate change activists

A 25-year-old Australian who sued his A$57 bn ($42 bn) pension fund over climate change has settled out of court in a case widely seen as a wake-up call for trustees and company directors.

[4] Caroline Byrne, "Australian climate change lawsuit a 'shot across the bow' of directors and trustees worldwide," IR Magazine, 06. Dec. 2020, https://www.irmagazine.com/activism/australian-climate-change-lawsuit-shot-across-bow-directors-and-trustees-worldwide

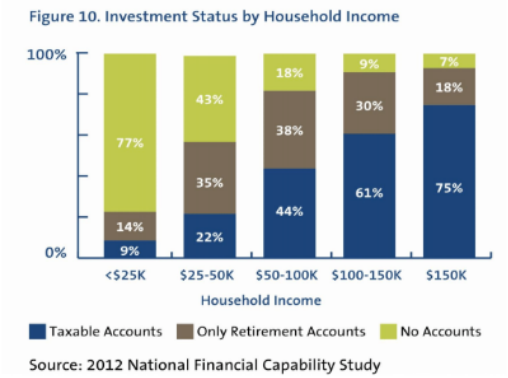
The duty of impartiality is "the specific duty to treat all trust beneficiaries impartially and not to favor one beneficiary over another." This means that your pension or 401(k) trustee, or your fund manager, must make sure that they are aware of all of their beneficiaries' or customers' concerns equally. This aspect of fiduciary duty is especially helpful for citizens who feel that they don't have financial power because they don't have much wealth. It is true that households in the bottom 50% of the income distribution pyramid have comparatively little stock market wealth, and the same is true for households of color. True, but not important in terms of the power of your voice.

Because of the fiduciary duty of impartiality, fund managers and retirement trustees cannot place their obligations to wealthier customers or beneficiaries above those with less wealth. They cannot place their obligations to their white customers and beneficiaries above those of their black and brown constituents. In this light, the less wealthy and the underserved minorities in our society have much more power.



Over half of households with incomes of $75,000 or less have a fiduciary relationship with a fund manager or retirement trustee, as do nearly one-fifth of households with incomes below $25,000. More than half of African-American and Hispanic/Latinx households do as well. A New York City sanitation worker, a teacher in California, a county employee in Tennessee, all have fiduciaries with obligations to them through their pension funds.

Poor People Have Fiduciaries



Retirement risks experienced by younger, poorer, or underserved groups are different from those with more wealth or privilege, and the duty of care requires that these retirement risks receive attention. The fiduciary relationship, which combines the duty of care with the duty of impartiality, is the most important financial relationship that a citizen shareholder will normally have. Our next sections show you how the power of fiduciary duty can be flexed in retirement funds and insurance companies.

Retirement Funds

There are three main pots of retirement money in the U.S. The largest segment is the IRA, which gives you complete choice in how you want the money invested. Defined contribution (DC) plans, like 401(k)s and 403(b)s, give you some choice in how you can invest the money. Defined benefit (DB) plans, offered by both private sector and government employers, give you no choice in how the money is invested, but that doesn't mean that you have no influence.

An IRA is normally invested in a mutual fund or ETF, and citizen IRA participants have all of the rights of any other mutual fund investor. In fact, they have more flexibility, because they can dump their existing mutual fund family if they can't get satisfaction, and move their money to a more responsible fund family, tax-free.

Defined contribution (DC) plan participants are offered a range of investment choices, normally mutual funds, along with company stock. You can typically change your mix at least quarterly. 401(k), 403(b), and other DC participants have two points of leverage as citizen shareholders: 1) they can ask their plan sponsor to vote on their behalf, and 2) they can ask their plan sponsor to add sustainable funds to their plan options.

Your 401(k) plan documents specify the party with responsibility for voting shares. In some plans, you have the right to instruct the plan sponsor how to vote. In other plans

you don't, but nevertheless your plan sponsor owes you consideration. Your plan sponsor, after all, is your fiduciary.

Influence Your Pension Fund…

PGH PRESS RELEASE

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Timothy McNulty
Communications Director
412-660-1999
timothy.mcnulty@pittsburghpa.gov
Mayor's Office

Pittsburgh Pension Fund Adopts Sustainable Investment Policy

PITTSBURGH, PA (September 17, 2020) After thorough study, the City of Pittsburgh Comprehensive Municipal Pension Trust Fund has adopted new "Socially Responsible Investing" guidelines to screen for pension investments in companies that follow environmentally friendly and socially responsible business procedures.

[5]

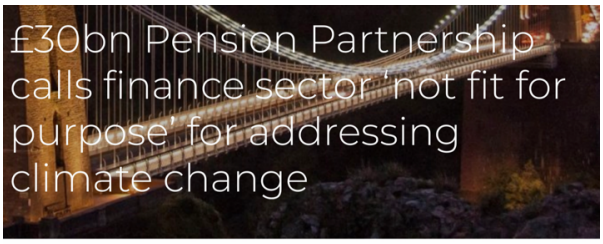
Have you ever contacted your HR department and asked to communicate with your 401(k) plan sponsor? You should! It is your right as a citizen shareholder. Ask the sponsor what its voting policy is. If the sponsor only votes with management, ask for the policy to change. If the sponsor's policy prevents it from submitting resolutions, ask for the policy to change. If you don't like the fact that you have no sustainable investment options, ask for the policy to change.

The more like-minded co-workers you can organize around the issue, the better. Start a paper trail with your plan fiduciary, questioning their commitment to reducing your retirement risk by fighting climate change, economic inequality, or threats to democracy caused by holdings in your funds. I assure you, they will take notice.

About one-third of retirement funds are in public or private defined benefit (DB) plans, what we normally think of as a standard pension fund. Although you can't choose what you invest in, your pension trustees are still your fiduciaries and still owe you specific duties. Pension trustees not only choose investments on your behalf, they also vote on your behalf. Some public employee pension funds in blue states have taken leadership positions in filing or supporting shareholder resolutions and in engaging with corporate management.

[5] Press release: "Pittsburgh Pension Fund Adopts Sustainable Investment Policy," Mayor's Office of the City of Pittsburgh, 17. Sep. 2020, https://pittsburghpa.gov/press-releases/presspdf/4315

One academic study suggests that, of all things, pension fund trustees actually pay attention to the preferences of their beneficiaries! Have you ever thought of writing or calling your pension plan sponsor to ask for more responsible investment practices? Remember, both DC and DB pension plan sponsors are fiduciaries, working for you.



In an ambitious new climate policy, Brunel Pension Partnership commits itself to push for a more climate-aware financial system, and to removing companies and investment managers that fail to perform on climate issues.
[6]

Insurance Companies

If there is any industry on the planet that should be fearful of an unsustainable future, it is the insurance industry. As social and environmental risks increase, so do the risks to the insurance business model, which relies on dependable loss trends to forecast pricing and payouts. Insurance companies take in premiums now and must hold them long-term for a potential payout much later; therefore, both your property and life insurance providers hold massive investments. If their investments do poorly because of climate change or the bad effects of economic inequality, their financial strength will suffer, which could affect you directly. In this regard the citizen shareholder becomes the citizen policyholder.

There are two types of insurance companies, mutual and stock. Stock insurance companies such as Allstate or MetLife are public companies like any other, so can receive shareholder resolutions and be subject to investor pressure. But mutual insurance companies, such as State Farm, Liberty Mutual, and Mass Mutual are owned by their policy holders. And guess what? Mutual insurance companies are fiduciaries too! In fact, there is legal opinion that *all* insurance companies are fiduciaries.

U.S. insurance company investment portfolios typically hold corporate bonds. These are potentially directly financing projects that harm the climate, which can increase disaster payouts and reduce reserves. As a policyholder of a mutual insurance company, you are a part-owner and will be negatively affected by these investments. You have the right to elect directors who — if they knowingly put risky bonds into *your* investment portfolio — may very well be acting contrary to their fiduciary duty. As a citizen policyholder, it is your right to remind them of this issue.

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[6] "£30 billion Pension Partnership calls finance sector 'not fit for purpose' for addressing climate change," Brunel Pension Partnership, https://www.brunelpensionpartnership.org/2020/01/27/30bn-pension-partnership-calls-finance-sector-not-fit-for-purpose-for-addressing-climate-change/.

And depending on your company's by-laws, you may even be able to submit a policyholder resolution to the company's annual policyholder meeting. Even as a policyholder of a stock insurance company, you are in a fiduciary relationship and can advance a similar argument that you are owed a commitment to the financial strength of the corporation.

What About Those European Oil Companies?

You have probably heard of the Paris Agreement on climate. Ratified by almost every country in the world, it forces nations to make commitments to decarbonize, so that by 2050, there will be no carbon released into the atmosphere as a global average. As countries decarbonize, they in turn make laws about how their corporations should decarbonize. Europe is ahead of the rest of the world on this issue (the U.S. severely lags).

Many big oil companies have headquarters in Europe, a vestige of the colonial era when each large European country had its own national oil champion. Prodded by government, society, and their own shareholders, each of the European oil majors is playing leapfrog to see who can best align with the Paris Agreement. None of them are perfect yet, but as a group they are far ahead of the rest of the world.

The pandemic, combined with political machinations between Russia and Saudi Arabia, caused a collapse in oil prices which drove down the stocks of all energy companies, including the European majors. This created a natural experiment to see what might happen if divestment actually achieved its financial goal of driving down stock prices, thus raising the cost of equity capital. As expected, a buyer stepped in to scoop up the beaten-down shares.

Who was the buyer? The wealth fund of Saudi Arabia, controlled by His Royal Highness Mohammed bin Salman. What did it buy? $1 billion worth of four separate European majors. We can only guess how the Saudis will vote on any shareholder resolutions that ask these companies to continue their journey of improvement.

Go Make Change!

You are a citizen of two worlds. One is the political world; you are the citizen of a nation. The other is the financial world; you are a citizen if you own stocks or funds, if you have a pension, or even if you own an insurance policy. Each world gives you rights as a citizen. Your rights are powerful in each as well. Why do most of us concentrate on our rights in one world while ignoring our rights in the other? Maybe because no one explained these rights to us before.

Once you become aware of your rights, it is up to you to act on them. Many resources are available to help with this potentially daunting task. In this pamphlet, I've provided some ideas. Many others are available with a web search. If you received this pamphlet because of your affiliation with an advocacy group, turn to that group to help magnify their efforts.

I wish you success on your journey. As a citizen shareholder, you can most assuredly make a difference!