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President Richard Brodhead
Box 90001
Duke University
Durham NC 27708

Re: ACIR Report and Recommendations on Fossil Fuels

Dear President Brodhead:

In December 2013 you asked the Advisory Committee on Investment Responsibility (ACIR) to consider the matter raised by Divest Duke. On behalf of the (ACIR), please consider this our report and recommendations that were unanimously approved on November 14, 2014, with 12 of 14 ACIR members present (2 ex-officio members were unable to attend).

Executive Summary

All members of the ACIR express support for Duke pursuing appropriate and reasonable actions that will contribute to reducing in the effects of climate change, including but not limited to actions specific to the use and support of fossil fuels. We recognize that the University has already done much in this regard, including its pledge to become carbon-neutral by 2024, decommissioning its coal plant and replacing it with a new steam plant, investing in a North Carolina hog farm for carbon offsets, moving to natural gas and electric busses and vehicles, and many others. There is undoubtedly more that can be done, but as it relates to the role of ACIR the established guidelines for the committee set thresholds that must be met before ACIR can make recommendations on matters before it.

The recommendations set forth below call for several steps that collectively ACIR believes are consistent with how an endowment can act responsibly while maintaining holdings in fossil fuel companies. These include:

- Annual reports by DUMAC to the ACIR on Duke's fossil fuel energy and clean energy/technology holdings;
- Regularly meeting with DUMAC representatives to discuss DUMAC's programs, policies and practices designed to support through its investment activity reductions in carbon emissions and promotion of non-fossil fuel energy;

- Directing DUMAC, consistent with the fiduciary obligations of its officers and directors, to have among its strategies targeting investments that advance environmentally friendly clean energy strategies;
- With respect to significant direct equity holdings in fossil fuel companies, directing DUMAC to engage those companies to encourage their managers to develop strategies consistent with the quest for clean or cleaner sources of energy; and
- When exercising the power to vote proxies, directing DUMAC to support well-crafted and reasonable proposals that appear consistent with the objective of encouraging a firm’s managers to report on, or take action with regard to, efforts to reduce carbon emissions.

With respect to the request made by Divest Duke, however, we make the following findings:

there has not been sufficient discourse on the topic;

there is a lack of clarity that divestment will have the desired impact:

divestment, while certainly symbolic in that it communicates where Duke stands on this topic, is a single occurrence, whereas we believe other actions referenced in the report reflect the benefits of multiple acts and communications that are more consistent with the missions of a great university, and, finally;

the Trustee Guidelines to ACIR indicate that before divestment a company is to be “afforded reasonable opportunity to alter its activities.”

We acknowledge that action, even when likely to have little direct impact, divestment can make an important symbolic statement. Duke and other universities are well situated to communicate values and to raise among their audiences questions necessary to debate and advance values. However, in light of the overall weight of the above-listed findings, we do not, under the present circumstances, recommend divestment.

The ACIR also notes with great enthusiasm that although it is beyond its scope of deliberations, its members believe individually and collectively that the University can do more to foster debate and discussion on our campus and beyond. Therefore, we also include several recommended areas that may benefit from further consideration or exploration outside of the ACIR process.

Background

Concern for climate change has great resonance within the ACIR. Had there not been a request from Divest Duke pending before ACIR was reconstituted and reoriented in late fall 2013, the committee would nonetheless have engaged the question of whether fossil fuels pose the type of harm proscribed by the Board of Trustees in its “Guidelines on Socially Responsible Investing, adopted on August 20, 2004”. Although the Guidelines is included in its entirety in

Appendix B, for emphasis and clarity we set forth below, and quote directly in this report, those paragraphs of the Guidelines that framed much of our analysis. (emphasis below added):

Actions the University takes may or may not materially affect an offending corporation, but such actions may have significant symbolic value. When the University community has engaged in substantive discourse on an issue and expressed broad concern that substantial social injury is being caused by such policies or practices, the president may make a recommendation to the Board of Trustees.

Where the Board of Trustees finds that a company's activities or policies cause substantial social injury, and that a desired change in the company's activities would have a direct and material effect in alleviating such injury, it may instruct the Duke University Management Company (DUMAC) to take appropriate action, including the exercise of the University's practicable shareholder rights to seek modification of the company's activities to eliminate or reduce the injury, using such means as:

- a) direct correspondence with management
- b) proxy votes
- c) sponsoring shareholder resolutions.

If the Board of Trustees further concludes that the company has been afforded reasonable opportunity to alter its activities, and that divestment will not impair the capacity of the University to carry out its educational mission (for example, by causing significant adverse action on the part of governmental agencies), then it may instruct DUMAC and its managers to divest the securities in question within a reasonable period of time.

Process

The ACIR has had considerable deliberation on this topic since you brought it to our attention a year ago. We met with members of Divest Duke in April 2014, at the ACIR's open forum on October 6, 2014, and again on October 22, 2014. Prior to its April 2014 meeting, we benefitted from the perspective shared in the original Divest Duke proposal and materials offered that set forth its call for total divestment. Then in October they provided several alternative and interim steps that could be pursued in lieu of total divestment.

The committee has also studied the actions by our peer institutions such as Brown, Harvard, Stanford, UNC and Yale. At our September 2014 meeting, the Committee analyzed a list DUMAC prepared of the fair market value as of June 30, 2014, of direct energy holdings, both equity and derivatives¹ and was briefed on the details of the limited divestment approved by

¹ "Direct" refers to investments over which DUMAC has control that are not pooled investments; "energy holdings" are of companies set forth on the 350.Org list of top 200 fossil fuel firms. The list was only for the University portion of endowment managed by DUMAC and did not, therefore, include any holdings by the Health Systems, retirement funds subject to ERISA, or the Duke Endowment.

Stanford in May 2014. Particularly constructive in its deliberations, ACIR drew upon on several authorities within the Duke community. At its October 22, 2014, meeting, the committee had extensive discussions with Professors Brian Murray (Director of Economic Program, Nicholas Institute for Environmental Policy Solutions), Richard Newell (Gendell Professor of Energy and Environment and Director, Duke Energy Institute, Nicholas School of the Environment), William “Billy” Pizer (Sanford School of Public Policy and Nicholas Institute for Environmental Policy Solutions), Tim Profeta (Director, Nicholas Institute for Environmental Policy Solutions) and Jon Wiener (Wm. And Thomas L. Perkins Professor of Law, School of Law, Professor of Environmental Policy (Nicholas) and Professor of Public Policy (Sanford)).

More generally, since the inaugural ACIR meeting under its broadened membership and charter in December 2014, Committee members have individually become consumers of the extensive literature discussing whether fossil fuel holdings sit well, if at all, within the mission and philosophy of institutions of higher learning.

Deliberations vis-à-vis the ACIR Guidelines

The ACIR guidelines set forth very clear conditions and considerations that guide the committee’s actions regarding investment recommendations:

1. Substantive community discourse. The ACIR makes recommendations to the president who may make a recommendation to the Board after an issue has had “substantive discourse” within the Duke community, and where there has been “expressed broad concern that substantial social injury is being caused by such policies or practices.”

Even though the fossil fuel divestment movement has been on-going for several years, we believe Duke and other universities are still at the early stage of considering what is the best response to these issues. For example, we inquired of the Divest Duke representatives and others with whom we consulted whether there has been an on-campus forum on fossil fuels and the endowment or more generally a program to explore strategies that Duke might pursue to shine a light on the issues. Notwithstanding support conveyed through petitions and dialog within segments of the community, we do not believe that broad-based community programs engaging individuals on all sides of the issue in rigorous debate had occurred. For example, none of the energy experts we consulted, nor any member of ACIR, has participated in or attended any Duke community forum focused on fossil fuels and the endowment or more generally a program to explore strategies that Duke might pursue so as to address carbon emissions². Thus despite the importance and complexity of the issues related to global warming, fossil fuels and endowment holdings, the ACIR finds there has not been a significant enough level of informed engagement on campus to meet the criteria set forth in its guidelines. Specifically, without multiple, balanced forums open to all segments of the university community, we are concerned that not enough knowledge has been placed

² We note that in the final stages of drafting this report a notice was circulated by Divest Duke representatives announcing such a forum would be held the evening of November 18, 2014. This is a step in the right direction.

before the Duke community for a full understanding of these multi-faceted issue and the most effective means the University can and has implemented to address them.

2. Direct and material effect. Action by the Board of Trustees is guided by a determination that (a) companies in which Duke invests are causing social injury through their actions and (b) “a desired change in the company’s activities would have a direct and material effect in alleviating such injury.”

Energy is something that is an essential part of our daily lives.³ Without energy, most of which is produced by fossil fuels, we would struggle to exist even at a subsistent level. Not only does this fact define the present demand for fossil fuels, but makes us doubtful that the present world-wide demand will abate in the face of increasing populations, rising standards of living, and growing economies. There is every reason to believe, and studies support this as well, that the resulting demand for fossil fuels will rise, not abate and certainly not retreat. Whether in the U.S., Europe, Asia, or Africa, both inertial forces and economic realities dispel the likelihood that fossil fuels will, anytime soon, take a rear seat to other forms of energy sources. This concern was reinforced at our October 2014 meeting with faculty experts who shared estimates prepared by the Intergovernmental Panel on Climate Change and the International Energy Agency setting forth estimates of usage of coal, oil and gas, assuming successful implementation of strategies to mitigate atmospheric warming. Even assuming the contemporary goal of limiting warming to 2 degrees by 2100 is met, there will continue to be substantial use of fossil fuels (even relative to current usage levels) in the form of natural gas. And while there will be a noticeable decline in use of oil and particularly coal in such a scenario, their usage will nonetheless still be quite significant for at least the next two decades. The conclusion to draw from the study is that even with an aggressive mitigation strategy, fossil fuels will continue to have a large and indispensable role in our daily lives for many, many years.

Moreover, the above-quoted Guidelines reference that “a desired change in the company’s activities would have a direct and material effect in alleviating such injury.” Unlike prior cases for divestment that can be impacted through directed action (e.g., Apartheid, Darfur, conflict minerals), the impacts of fossil fuels in global warming can only be mitigated through global action and will not be effective through local action alone. Without a coordinated, global approach, opposing actions of another country or company may negate the benefits that result from the positive actions of any one country or company.

The ACIR, therefore, lacks any basis to believe that divestment by Duke can be expected to have any direct impact on our contemporary unavoidable dependence on fossil fuels. Thus, divestment of fossil fuels, or even of coal, if it is to be embraced, must be understood primarily for its symbolic effect.

³ In contrast, conflict minerals and apartheid, previous issues examined by this committee, are not essential to our daily lives, and in fact we can live better and longer without them.

3. Symbolic effect of actions. Notwithstanding the question of whether action by Duke would materially impact a given company, the above-quoted Guidelines references that the University might reach decisions with respect to its endowment for symbolic effect:

Actions the University takes may or may not materially affect an offending corporation, but such actions may have significant symbolic value.

Thus, the fact that Duke's withdrawal from investment in a cohort of companies would likely have little to no effect on those companies' activities is not itself disabling of a divestment recommendation. Symbolism can matter. We note that symbolism's worth is in the message that it communicates. Duke and other universities are well situated to communicate their values and to raise among their audiences questions necessary to debate and advance values. This is indeed part of the life of universities and certainly so for Duke. We contrast this role with the limited expressive power of the single-shot divestiture decision. The symbolism behind Duke's actions should be consistent with, and not be in conflict with, the values of a great university, namely open and vigorous engagement. Duke is a unique and vibrant place for engagement. And, Duke does much more than just discuss, debate, and ponder. Duke acts, and has acted, with respect to the global warming in ways we believe are far more constructive. Investing millions to convert the university's boilers to natural gas goes far beyond symbolism; it was an expensive and that nontrivial expenditure signaled the depth of Duke's concern for global warming, coal's contribution to global warming, and the overall commitment by Duke to reduce greenhouse gas emissions. Similarly, Duke's commitment to be carbon neutral by 2024 is not a slogan without effect; it's a commitment to address the seriousness of climate change and encouragement to others to follow suit. These are important messages and we believe distinguish Duke as an institution where engagement with the issues leads to celebrated results. We believe the recommendations in this report will send a message consistent with the symbolic impact of what Duke has already done in this area.

4. Affording opportunity to alter activities. The ACIR guidelines indicate that the Board may consider divestment if company has "been afforded reasonable opportunity to alter its activities" and if divestment "will not impair the capacity of the University to carry out its educational mission."

Divestment, according to the Guidelines, is to be resorted to after other steps toward engaging a company or companies that are targeted for investment. To our knowledge, there has been no initiative by Duke to engage any fossil fuel company held by the endowment and therefore jumping directly to the divestment option might harm the ability of Duke representatives to constructively engage with industry.⁴ That said, tough social issues are worthy of the focus of a great university. Universities are places of open discussion, collaboration, and path breaking innovations whether theoretical or tangible. So it should be with engaging how to address fossil fuel's contribution to global

⁴ In the recent past, substantial progress was made in reducing acid rain following a process in which industry and non-industry experts engaged to find solutions.

warming. More importantly, if global warming is to be retarded, it will come not solely by technological developments, such as carbon capture and storage techniques; this suggests that there likely will be a social/ political response needed to overcome the inertial forces so that new, albeit likely expensive, technologies can be implemented. Incentives such as cap and trade, a carbon tax, and the like each require a broad movement to fill their sails so they can move forward.

Some members of the committee are concerned that divestment could have negative unintended consequence of polarizing discussion of how best or better to respond to fossil fuel's contributions to global warming and thereby weaken the possibility for constructively address the problem and developing solutions.

We recognize the seriousness of the threat to human well-being as a result of climate change and we recognize the need to dramatically reduce carbon emissions. But we do not believe that divestment would be a politically constructive and materially effective response to the problem. There is, nonetheless, much that can be done in many areas by the University, which has already acted strongly on this issue. In that spirit, below we offer a series of recommendations that fall within the scope of our charge.

Findings

Relative to the four-above considerations available to the ACIR, the committee concludes that:

- There has not yet been substantial enough discourse on the impact and viability of fossil fuel divestment. Such discourse should engage Duke's own faculty experts in this domain.
- While fossil fuel's impact on climate change was convincing and compelling to the ACIR, it was less clear that divestment at Duke—or even divestment by scores of other universities and companies—would have the desired global impact because demand in other countries could easily offset any positive effect of those divestments.
- The ACIR was convinced that even though divestment at this time may not be effective in a material sense, the symbolic impact of action by Duke is important and notably includes Duke's 2024 pledge to become carbon neutral. Further symbolic and tangible actions may be valuable, but is considered to be outside the purview of the ACIR.
- Today, individual faculties already engage in policy discussion regarding climate change and fossil fuels, sometime with specific corporations. Further action to engage companies operating in this domain may be desirable, but is considered outside the purview of the ACIR's charter.

Because we are not persuaded that divestment is an effective strategy to hasten the processes by which we will become less dependent on fossil fuels in the near term, and because of our concern that divestment could polarize discussions surrounding strategies that could accelerate development and use of non-fossil fuel energy, we do not support the divestment options set forth by Divest Duke.

Until further and substantive discourse occurs within the Duke community, and until the effect of Duke's actions (and that of other investing bodies) can be shown to have a positive contribution at the global scale, the ACIR does not find cause for specific divestment action at this time.

Non-Investment Considerations

We believe there are likely other strategies and initiatives that Duke might develop consistent with its mission that can be expected to lead to explicit plans, policies, and practices that will accomplish far more than withdrawal via divestment of fossil fuel holdings. The committee members' expertise and our charter do not prepare or allow us to delve into what other steps might be taken that would have greater force than a one-time divestment announcement. At a minimum, therefore, we believe a fuller campus-wide discussion of what Duke, and more broadly, the nation can do to curb dependence on fossil fuels would be among the initiatives that the deans and senior officers would consider as effective responses to the concerns raised by Divest Duke.

Although the ACIR's Guidelines limit our development of recommendations to those related to investment, the committee nonetheless believes strongly that certain non-investment actions by the University would be keeping with the mission of the university and the establishment of the ACIR. Specifically, we are persuaded that certain non-investment actions can be as or more effective than divestment, which after all does not get at the heart of reducing carbon emissions and rather only offers Duke-owned investments within the market place for another willing investor to purchase, therefore only shifting the investment to another. Therefore, we encourage continued strong action by the university to reduce carbon emissions including but not limited to:

- Conservation efforts broadly on the campus, including building-level energy utilization and monitoring capabilities,
- Continued investment in new technologies (such as natural gas vehicles) and carbon offsets,
- Behavioral changes by our community such as could be provided through alternative modes of daily transportation and use of video and other technologies as a substitute for travel,

Further, we raise for consideration providing regularly and highly visible programs similar to the Provost Lecture Series that would focus broadly and deeply on the global warming and man's contribution to it.

Recommendations

Based upon our charter, ACIR's recommendations focus on issues of socially responsible investing related to the University's endowment. ACIR believes that strategies to develop, initiate and monitor the progress of initiatives such as those suggested here will be both consistent with the teaching and research mission of Duke and will enhance understanding of how an endowment can act responsibly while maintaining holdings in fossil fuel companies. While the scope of ACIR's input is to be limited to endowment-related recommendations, we

nonetheless observe in this report that there are multiple initiatives pertaining to the linkage of fossil fuels and climate change that the University can pursue.

1. We recommend that DUMAC regularly discuss with the senior officers strategies and procedures used in managing the endowment in ways that are consistent with the overall financial objectives of the endowment and that are supportive of the quest toward clean or cleaner energy sources so as to further the goal of reducing society's dependence on fossil fuels. In this regard, we recommend full consideration be given to the following:
 - i) To the extent practicable, annual reporting to ACIR by DUMAC on fossil fuel energy and clean energy/ technology holdings. Somewhat related, we urge evaluation of the development of an annual analysis of carbon exposure across the portfolio. See Alicia Selger, *Unconventional Wisdom*, Appendix F (discussing this strategy and referencing that Harvard's announcement of its intent to become a signatory to the Carbon Disclosure Project);
 - ii. DUMAC, consistent with the fiduciary obligations of its officers and directors, and to the extent practicable, have among its strategies targeting investments that advance environmentally friendly clean energy strategies (along the lines of the recent announcement by the University of North Carolina to include such efforts among its own responses for calls to divest from fossil fuels) as well as investments in energy conservation technologies with an overall goal of increasing Duke holdings in clean energy relative to fossil fuels;
 - iii) With respect to significant direct equity holdings in fossil fuel companies, engage those companies to encourage their managers to develop strategies consistent with the quest for clean or cleaner sources of energy; and
 - iv) DUMAC and the university consider other steps that can be taken as investors to influence the movement toward clean energy.
2. We recommend that ACIR, or a similarly charged committee, regularly meet with DUMAC representatives to discuss DUMAC's programs, policies and practices designed to support through its investment activity reductions in carbon emissions and promotion of non-fossil fuel energy. We believe such monitoring is within the current charge to ACIR; however, global warming is of such significance we recognize that there may well be a counterpart to ACIR that is specifically charged with a wide-range of initiatives (a matter referred to in the preamble to our recommendations) not limited to endowment related matters who the administration may believe should serve this function with respect to both investment-related and non-investment related initiatives.
3. We recommend that Duke, when exercising its power to vote proxies should support well-crafted and reasonable proposals that appear consistent with the objective of encouraging a firm's managers to report on, or take action with regard to, efforts to reduce carbon emissions.
4. Consistent with the findings of this report:

that there has not been sufficient discourse on the topic;

that there is a lack of clarity that divestment will have the desired impact;

that divestment, while certainly symbolic in that it communicates where Duke stands on this topic, is a single occurrence whereas we believe other actions referenced in the report reflects the benefits of multiple acts and communications that are more consistent with the missions of a great university, and, finally,

that the Trustee Guidelines to ACIR indicate that before divestment a company is to be “afforded reasonable opportunity to alter its activities,”

under the present circumstances we recommend against divestment.