



# CITY OF SOMERVILLE, MASSACHUSETTS

## LAW DEPARTMENT

January 11, 2016

Somerville Retirement Board  
City Hall Annex  
50 Evergreen Avenue  
Somerville, MA 02145

Re: Fossil Fuel Divestment Questions

Dear Honorable Board Members:

You have requested a legal opinion on several questions regarding “the fossil fuel divestment request received by the SRB”. I address these questions in turn below.

**1. If the SRB decided to divest fossil fuels from its portfolio, what legal options are available?**

In my opinion, the Somerville Retirement Board (“SRB” or “Board”) has the responsibility to set investment policy of retirement system funds, subject to (1) legal and fiduciary duties; and (2) public employee retirement administration commission (“PERAC” or “Commission”) oversight, as discussed in detail herein. Generally, MGL c. 32 does not specifically address “fossil fuel investments” or divestment therefrom. To provide a legal opinion on whether taking any specific proposed action is “legal” would require detailed information as to what the specific proposed investment or divestment action is and how it meets legal and fiduciary requirements discussed herein. Factual circumstances to consider include: guidance of any investment manager or consultant; financial performance of implementing any change in investment versus maintaining the status-quo; and the initial and ongoing cost of divestment and the impact on benefits. See Bd. of Trs. v. Mayor & City Council of Balt. City, 317 Md. 72 (1989).

Under MGL c. 32, each contributory retirement system<sup>1</sup> shall be “managed by a retirement board which shall have the general powers and duties set forth in subdivision (5)”. MGL c. 32, s. 20(4). The board “shall provide for the payment of retirement allowances and other benefits and for all other necessary expenditures...and shall have such other powers and shall perform such other duties and functions as are necessary to comply with such provisions.

<sup>1</sup> “System”, is defined as “...any county, city, or town contributory retirement system, as the case may be...” GL c. 32, § 1.



Id. The board shall prepare an annual report to include a “summary of the board’s investment policy, a summary of the system’s investment portfolio...” Id. at (5)(i).

MGL c. 32, s. 23(2)(b) provides that the “board of each system shall invest and reinvest the funds of the system in the PRIT Fund under subdivision (8) of section 22, in the PRIT Fund by purchasing shares of the fund, as provided for in the trust agreement adopted by the PRIM board under subdivision (2A), or under the standards in subdivision (3)... (emphasis added). MGL c. 32, s. 23(3) provides as follows:

*Fiduciary Standards.* — A fiduciary as defined in section one shall discharge his duties for the exclusive purpose of providing benefits to members and their beneficiaries with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims and by diversifying the investments of the system so as to minimize the risk of large losses unless under the circumstances it is clearly prudent not to do so... (emphasis added).

There is nothing in section 23 which expressly addresses divestment from fossil fuels. In my opinion, the board may consider amendment of its investment policy or changes to the investment of the system’s funds, so long as prior to doing so, board members take all necessary, required, and prudent steps, to ensure any action would satisfy all of the applicable legal and fiduciary standards, that apply to all system investments. These requirements will include those set out in MGL c. 32 and in PERAC regulations.

PERAC has general responsibility for the administration of the public employee retirement systems under G.L. c. 32. See Barnstable County Retirement Bd. v. Contributory Retirement Appeal Bd. 43 Mass. App. Ct. 341, 345 (1997). Several PERAC regulations derive from its role in oversight of investment management decisions made by local retirement systems. 2001 Mass. AG LEXIS 2. Prior to 1983, local retirement boards “were allowed to invest in a limited group of investments” on an approved list. With the establishment of the pension advisory unit of PERAC, the Legislature “also relaxed the prior restrictions.” G.L. c. 7, § 50; 2001 Mass. AG LEXIS 2, \*9-10. “While the revised statute is less confining than the prior list of approved investments, the statute nonetheless limits the range of possible investment vehicles by the local boards.” Id. It should also be noted that under MGL c. 32, s. 21(1)(a), PERAC conducts field examinations of local boards, and has authority to review and evaluate the board’s investment management decisions, in order to monitor the board’s performance and the retirement system’s effectiveness in achieving the statutorily intended results. See 840 C.M.R. s. 25.01.

## **2. How can the SRB divest fossil fuel investments from its entire portfolio?**

In my opinion, the board would have to consider, and ensure, that in acting to divest from fossil fuel investments, board members can satisfy all applicable legal and fiduciary duties. For example, the board would need to follow investment and analysis procedures, including use of

any qualified investment manager or consultant, as set forth in the applicable provisions of MGL c. 23, and PERAC regulations<sup>2</sup>.

There are various actions that the board may be required to address in considering divestment, including, but not limited to the following. The board may “adopt by-laws and make rules and regulations consistent with law, which shall be subject to approval [by PERAC]” as set forth in MGL c. 32, s. 21(4). MGL c. 32, s. 20(5); 840 CMR 14.02. The board may be required to update its statement of investment objectives as filed with PERAC (i.e. investment policy, rate of return, risk, asset mix, or diversification). 840 CMR 18.00-18.03. The board may require the services of a qualified investment manager (840 CMR 1), or a consultant (840 CMR 26), subject to the procedures and approval of PERAC, as required by law. In carrying out any change in investments, the board is still subject to all existing legal duties and fiduciary requirements which apply to the system under MGL c. 32, and 840 CMR.

### **3. If challenging the PERAC letter, how does SRB challenge the letter?**

In my opinion, I do not find a law requiring PERAC to post a request for proposals in order for the SRB to issue a request for proposals for an investment advisor/consultant. Therefore, I do not believe a challenge to the June 15, 2015 letter from PERAC’s Executive Director to the Board’s Executive Director letter is necessary if the board decided to divest system funds from fossil fuels, as long as the board satisfies all legal requirements for procuring and contracting with an investment manager or consultant.<sup>3</sup> See MGL c. 32, s. 23B, s. 23(2)(c); 840 CMR 16-17, and 840 CMR 26. Notwithstanding, the board may be able to request posting

---

<sup>2</sup> MGL c. 32, s. 23(2)(c) states that no investment of funds shall take place until the board has received from PERAC an acknowledgement of receipt of the following: “(i) certification that, in making the selection, the board has complied with the process established in section 23B; (ii) a copy of the vendor certification required under section 23B; (iii) copies of disclosure forms submitted by the selected vendor; (iv) a certification that the investment is not a prohibited investment as set forth in regulations of the commission; (v) if the board has retained a consultant, a copy of the consultant reports pertaining to the investment and the selected vendor; and (F) a copy of the board certification required under section 23B.

Prior to the retention of an investment consultant the board shall have received from the commission an acknowledgement of receipt of the following: (i) certification that, in making the selection, the board has complied with the process established in section 23B; (ii) copy of the vendor certification required under section 23B; (iii) copies of disclosure forms submitted by the selected consultant; and (iv) copy of the board certification required under section 23B. GL c. 32, § 23(2)(d). The board may employ any qualified bank, trust company, corporation, firm, or person to advise it on the investment of the fund and may pay for such advice. GL c. 32, § 23(2)(f).

<sup>3</sup> MGL c. 32, § 23B; 840 CMR 16.08 (selection of investment managers, consultants, must be by competitive process which satisfies boards’ fiduciary duty and meets the requirements of MGL c. 32 and 840 CMR. The “retirement board or its procurement officer shall give public notice of the request for proposals and... shall: (3) remain posted, for at least 2 weeks, in a conspicuous place in or near the offices of the retirement board until the time specified in the request for proposals; and (4) be published at least once, not less than 2 weeks prior to the time specified for the receipt of proposals, in a newspaper of general circulation within the area served by the retirement board and in the case of a procurement for investment, accounting, actuarial or legal services in a publication of interest to those engaged in providing such services...[and] also place the notice in a publication established by the state secretary for the advertisement of such procurements.” MGL c. 32, s. 23B.

of a notice of request for proposals using the online form, on the PERAC's compliance unit website.<sup>4</sup>

A challenge to the PERAC letter would be subject to the provisions of MGL c. 32, s. 16, which provides as follows:

...any person when aggrieved by any action taken or decision of the...public employee retirement administration commission rendered, or by the failure of...the public employee retirement administration commission to act, may appeal to the contributory retirement appeal board by filing therewith a claim in writing within fifteen days of notification of such action or decision of the retirement board or the commission, or may so appeal within fifteen days after the expiration of the time specified in sections one to twenty-eight, inclusive, within which a board or the commission must act upon a written request thereto, or within fifteen days after the expiration of one month following the date of filing a written request with the board or the commission if no time for action thereon is specified, in case the board or the commission failed to act thereon within the time specified or within one month, as the case may be.” (emphasis added).

**4. If home rule petition, could multiple retirement boards utilize the same petition?**

In my opinion, a home rule petition may be filed to authorize the SRB to divest fossil fuel investments from system funds, subject to the procedures in Section 8(1) of the Home Rule Amendment (i.e. petition approved by the mayor and the board of aldermen of the city of Somerville). I note that a home rule petition relates only to a single city or town.

**5. Does MGL c. 32, s. 23(3) apply to divestment of fossil fuels?**

Yes, in my opinion, MGL c. 32, s. 23(3) applies to the investment of funds in the system (other than those in the PRIT Fund). MGL c. 32, s. 23(2)(b) provides that the “board of each system shall invest and reinvest the funds of the system in the PRIT Fund under subdivision (8) of section 22, in the PRIT Fund by purchasing shares of the fund, as provided for in the trust agreement adopted by the PRIM board under subdivision (2A), or under the standards in subdivision (3) provided that: (i) no investment of funds shall be made in stocks, securities or other obligations of a company which derives more than 15 per cent of its revenues from the sale of tobacco products; (ii) in investing funds the board shall employ an investment manager or investment managers who shall invest the funds of the system; and (iii) no funds shall be invested directly in mortgages or collateral loans.” (emphasis added).

**6. What impact does 840 CMR 1.01 have on divestment of fossil fuels?**

---

<sup>4</sup> <http://www.mass.gov/perac/compliance-investments/request-for-proposal-posting-request-form.html>

In my opinion, a retirement board member must perform his or her duties in accordance with all applicable laws, including 840 CMR 1.01, when considering divestment. A board member “shall discharge all of his/her duties solely in the interest of members and their beneficiaries...[and] for the exclusive purpose of: (a) providing benefits to members and their beneficiaries...(2) With the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims.” 840 CMR 1.01(3) states the members duties include “diversifying the investments of the system so as to minimize the risk of large losses, unless under the circumstances is it clearly prudent no to do so.” (emphasis added). Similar, to MGL c. 32, s. 23(3), 840 CMR 1.01 sets forth fiduciary standards which would apply to any performance of duties or investment decisions of retirement system funds. Also See MGL c. 32, s. 1.

**7. What is your legal opinion regarding potential restrictions pertaining to divestment in accordance with the fiduciary standard outlined in MGL c. 32, s. 23(3)?**

In my opinion, MGL c. 32, s. 23(3) does not address restrictions specific to divestment from fossil fuels. The board’s investment of system funds is subject to the fiduciary standards set forth in section 23(3). Certain investment restrictions are established in MGL c. 32, s. 23(2)(b), that apply when investing under the standards in subsection 3, including: (i) no investment of funds shall be made in stocks, securities or other obligations of a company which derives more than 15 per cent of its revenues from the sale of tobacco products; (ii) in investing funds the board shall employ an investment manager or investment managers who shall invest the funds of the system...<sup>5</sup> (emphasis added).

**8. If the SRB were to divest fossil fuels from its portfolio and this decision results in a negative impact on the portfolio return, would the SRB be exposed to liability?**

In my opinion, whether the SRB or its members have breached any legal or fiduciary duty to members, that would create a liability due to “negative impact on the portfolio return” will depend upon the factual circumstances associated with the decision and the application of the above-referenced legal and fiduciary standards. Factual issues would likely include: (1) how the investment policy is drafted and defined; (2) the guidance of any investment manager or consultant; (3) the financial performance of implementing any change in investment versus maintaining the status-quo; and (4) the initial and ongoing cost of divestment and the impact on benefits. See Bd. of Trs. v. Mayor & City Council of Balt. City, 317 Md. 72 (1989).

Retirement boards “do not owe any general fiduciary duty to their members, *Benoit v. Bristol County Retirement Bd.*, CR-04-291...except as regards the investment of the boards’ funds.” Thorburn v. Worcester Regional Retirement Bd., CR-07-424 (DALA, 2008). The Appeals Court referenced the *Benoit* decision stating that “[t]here is no general fiduciary duty to

---

<sup>5</sup> PERAC may determine that a local board is not subject to certain investment restrictions upon showing a record of investment management “which merits broader investment powers. MGL c. 32, s. 23(2)(g)(still subject to restrictions on investments in military products for use in South Africa, Northern Ireland, and other restrictions).

members in the trust sense. The duties and responsibilities of a retirement board are statutorily defined in Chapter 32." Geary v. Plymouth County Ret. Bd., 87 Mass. App. Ct. 1126 n.5 (2015). Under c. 32, § 25 (5), the "pension rights and benefits of §§ 1-28 are contractual ones of which members may not be deprived." State Bd. of Retirement v. Boston Retirement Bd., 391 Mass. 92, 96 (1984)(analysis referencing testimony as to whether a person's pension "would be in danger" as result of a transfer of funds).

840 CMR 1.02(1) provides that failure to "comply with the fiduciary standard set forth in MGL c. 32, s. 23 and in 840 CMR 1.01 may subject the fiduciary to personal liability for any losses to the system resulting from such failure." (emphasis added). Also See 840 CMR 1.04. To the extent a member of the retirement board may be subject to liability, I note the provisions of MGL c. 32, s. 20A<sup>6</sup> which provide for indemnification in limited circumstances, but specifically excluding where there "is shown to be a breach of fiduciary duty, an act of willful dishonesty or an intentional violation of law by such a member." (emphasis added).

For analogous discussion of a trustee's duties under Massachusetts law relative, see footnote seven below.<sup>7</sup> There are few judicial decisions on the issue of whether divestment conflicts with a trustee's duties to beneficiaries, and while not binding in Massachusetts, these decisions may be informative and are discussed in the legal treatise referenced in footnote eight.<sup>8</sup>

---

<sup>6</sup>Municode indicates this local option statute was accepted by Somerville on November 22, 1983.

<sup>7</sup>Diversification of investments is considered a central component of prudent investment because it both moderates and reduces risks. See G. L. c. 203C, § 4; Chase, 383 Mass. at 363. Standard recognizes that in some circumstances, it may not be prudent to diversify an investment portfolio, particularly where "the objectives of both prudent risk management and impartiality can be satisfied" without diversification. Restatement (Third) of Trusts, § 90 comment g. Receipt of sound investment advice and dismissal or wilful ignorance of it, where the advice was at the time prudent and consistent with the trust beneficiary's needs and goals, may be indicative of a lack of prudent investing. But such action or inaction in and of itself does not rise to the level of imprudent investing. The Woodward Sch. for Girls, Inc. v. City of Quincy, 469 Mass. 151, 160-163 (2014).

<sup>8</sup>Restat 3d of Trusts, § 227, comment (c). Lower court decision concluded that an Oregon Board of Higher Education directive could not be enforced because it violated the state's prudent investor statute, but the appellate court did not reach the merits of this ruling. Associated Students of University of Oregon v. Oregon Investment Council, 82 Or.App. 145, 728 P.2d 30 (1986), review denied, 303 Or. 74, 734 P.2d 354 (1987). "The Maryland Court of Appeals upheld the validity of a city ordinance requiring certain public employee retirement funds to divest from certain companies. See Board of Trustees of Employee's Retirement System v. Mayor and City Council of Baltimore et al., 317 Md. 72, 562 A.2d 720 (1989), cert. denied sub nom. Lubman v. Mayor et al., 110 S.Ct. 1167, 107 L.Ed.2d 1069 (1990). But compare Regents of the University of Michigan v. State, 166 Mich.App. 314, 419 N.W.2d 773 (1988), which held that legislation purporting to require divestment by public universities and other educational institutions could not regulate university investments under the state constitution. See also 38 Op.Ore.Att'y Gen. 2017, 2031 (1978) and Op.Fla.Att'y Gen., No. 85-30 (1985) limiting fiduciaries to financial rather than social or political criteria. Earlier decisions in Blankenship v. Boyle, 329 F.Supp. 1089 (D.D.C.1971), aff'd mem., 511 F.2d 447 (D.C.Cir.1975), and Withers v. Teachers' Retirement System, 447 F.Supp. 1248 (S.D.N.Y.1978), aff'd mem., 595 F.2d 1210 (2d Cir.1979), involved pension funds, looking to general, non-ERISA trust law principles. Although neither suggests the propriety of non-financial criteria in investment decisions, their results and reasoning have attracted considerable attention and debate in subsequent literature."

Legal commentators have expressed varied opinions on the issue of whether divestment based on a particular social issue may create liability.<sup>9</sup>

Please contact me if you have any additional questions.

Very truly yours,



Jason D. Grossfield  
Assistant City Solicitor

---

<sup>9</sup> See e.g., *Divestment of South Africa Investments: The Legal Implications for Foundations, Other Charitable Institutions, and Pension Funds*, 74 Geo. L.J. 127 (“...social considerations are permissible only if they are incidental – that is, if they have no adverse effect on the fund’s finances. However, if, after careful investigation, it reasonably appears that a fund can divest without additional costs, income loss, or increase in overall financial risk, a court may find that the social benefits of the divested portfolio are incidental.) If “social investment yields economic competitive returns at a comparable level of risk [and the cost is *de minimis*], the investment should not be deemed imprudent. See III *Scott on Trusts*, § 227.17 (W. Fratcher 4th ed. 1988).