

**Report and Recommendations
of the
Ad Hoc Advisory Committee on Tobacco Investments**

University of Michigan

March 17, 2000

Charge to Committee

From Executive Vice President and Chief Financial Officer Robert Kasdin

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Over the last several years, the University Faculty Senate Assembly has focused increased attention on the propriety of this University's owning stock issued by tobacco companies. This deliberation culminated in a resolution that urged the University to divest its holdings of such securities. In considering the proper response to this resolution, we reviewed the Board of Regents' procedural framework for weighing claims that the University should divest of its holdings in companies that do business in South Africa. In that context, the Board of Regents concluded that if any investment issue involves serious moral or ethical questions which are of concern to many members of the University community, an advisory committee consisting of members of the University Senate, students, staff and alumni would be appointed to gather information and formulate recommendations.

With the tobacco issue having been highlighted by the Senate Assembly, a number of the other leadership groups on campus joined in expressing the views that the University's ownership of tobacco stocks is of widespread concern. Some, like the Senate Assembly, urged divestiture. Others, knowing of the process described above, urged establishment of a special committee to review the process and make recommendations. After observing and participating in this constructive dialogue, we conclude that a special committee should be established to weigh the argument for this University to divest itself of securities issued by tobacco companies.

More specifically, this special committee, consisting of students, faculty, staff, and alumni, will be asked to consider whether the holding of such securities is antithetical to the core missions of the University of Michigan and, therefore, merit divestiture. Personal disapproval of smoking or disdain for those companies will not justify an institutional decision to divest.

This is a deliberately high threshold condition. The protection of the University endowment from political pressures is essential if we are to leave a University to succeeding generations with a University at least as strong as the one with which we have been entrusted. In your issuance of recommendations, the Board of Regents will be interested in the rationale for your decision, as well as the recommendation itself.

I. Preface

This committee was formed in September 1999 and given the charge set out above. We met a number of times to discuss the issues raised by the charge. In addition, we reviewed a wide variety of written materials, including but not limited to the following:

- the 1978 “Report and Recommendations of the Senate Assembly Advisory Committee on Financial Affairs on Investment and Social Responsibility” (urging divestment of stock in companies doing business in South Africa);
- the minutes of the March 1978 meeting of the Regents at which the procedural framework for dealing with moral or ethical issues related to the endowment was adopted and at which the South Africa issue was first addressed;
- the minutes of the April 1983 meeting at which the Regents adopted its South Africa divestment policy;
- the written policies of several other universities for dealing with issues of socially responsible investing;
- articles discussing the financial implications of socially responsible investing in general and of tobacco-free investing in particular;
- materials from the Investor Responsibility Research Center;
- data from the Centers for Disease Control and Prevention and other sources regarding the mortality and morbidity effects of tobacco use;
- summaries of internal tobacco-industry documents;

In addition to our private meetings, the committee held one public meeting and invited members of the University community to come and express their views on the question posed in the charge. The committee also received approximately 200 email messages from members of the University community expressing views on the University’s tobacco investments. The overwhelming majority of the responses, those received both at the public forum and via email, concluded that ownership of tobacco securities is antithetical to the core missions of the University and that divestment was appropriate.

II. Background, History, and Principles

The committee has been asked to make recommendations to the Regents regarding what the University's tobacco-investment policy should be. Before taking up that precise question, however, we first need to provide some background against which the tobacco-investment decision will be made. According to the official policy of the University, endowment investment decisions are generally based *solely* on financial factors such as risk and return. Thus, whether a given corporation has been engaged in activities that are inconsistent with the values of the University is generally treated as irrelevant. The wisdom of such a general policy is obvious. The purpose of the endowment is to generate income to support the missions of the University. Therefore, maximizing the endowment's return over time should be the principal objective of those entrusted with the management of the University's investments.

The alternative approach—of maintaining an ethically pristine investment portfolio—would be impossible, both in practice and in theory. For no company is perfect. Some pollute too much; some engage in objectionable employment practices; and some make products that cause serious injury or illness. Indeed, all businesses, even those with the best reputations, have one shortcoming or another from someone's perspective. That observation is simply a fact of the economy in the real world. And the University can only reside (and invest its endowment) in the economy that actually exists. However, that the University cannot achieve moral purity in its investments does not mean that it can never or should never take a moral position on any investment. As the authors of the seminal text on socially responsible investing put the point, “[t]hat no course of action is untainted does not mean that no course of action is preferable to

another or that we cannot choose between more or less desirable consequences.”¹

That important insight, of course, does not end the discussion; it does not tell us what course of action is preferable in any particular case. It tells us only that the impossibility of perfection should not be immobilizing. That lesson has, in a sense, been incorporated into the University of Michigan’s investment policy—specifically, through the University’s adoption of a procedural framework through which exceptional cases that raise issues involving “serious moral or ethical questions” can be brought to the attention of and addressed by the Regents. It will be useful here to review briefly how that framework came to be adopted.

In the late 1970s and early 1980s, many universities faced the question of what to do about their investments in companies doing business in South Africa. At the time, South Africa was controlled by its white minority, which was vigorously (and viciously) enforcing the infamous policy of apartheid, the forced segregation of the races in many spheres of South African life, including education, employment, and housing. That policy brought worldwide condemnation on the government of South Africa. In addition to the formal sanctions imposed on the South African government, there was a widespread movement to encourage public and private institutions—especially colleges and universities—to divest themselves of securities issued by companies doing business in South Africa. Many institutions, including many colleges and universities, did ultimately divest.

The South Africa issue was first formally addressed at the University of Michigan in the late 1970s, when, at the request of the Chief Financial Officer at the time, the Senate Assembly Advisory Committee on Financial Affairs reviewed the issue and wrote a report. In that report, the committee acknowledged that the primary responsibility of the Regents as managers of the endowment is to maximize investment return, but argued that in certain “compelling” cases exceptions should be made. Ultimately, that committee concluded that the South Africa situation presented such an exceptional case. Then, in March, 1978, the Regents passed a resolution that

¹ John G. Simon, Charles W. Powers & Jon P. Gunnemann, *The Ethical Investor* 26 (1972).

essentially tracked the Senate Assembly committee's recommendations. Among the actions taken in that resolution was the creation of a procedure for addressing future cases raising moral or ethical concerns about how the endowment is invested. The relevant language from the resolution reads as follows:

If the Regents shall determine that a particular issue involves serious moral or ethical questions which are of concern to many members of the University community, an advisory committee consisting of members of the University Senate, students, administration and alumni will be appointed to gather information and formulate recommendations for the Regent's consideration.

That is the procedure for dealing with exceptional cases. As far as we are aware, that procedure had not been invoked since the South Africa question was addressed, until now. In September 1997, the Faculty Senate Assembly voted almost unanimously to adopt a resolution urging divestment of the University's tobacco holdings. That vote, together with a nearly unanimous vote from the Student Assembly also calling for divestment as well as with the expression of concern about the University's tobacco investments from a number of other members of the University community, led to the appointment of this committee and ultimately this report.

Unfortunately, nothing in the Regent's 1978 resolution provides the committee with guidance as to what the University's policy should be with respect to tobacco investments. That resolution speaks of "serious moral or ethical questions which are of a concern to many members of the University community," but that statement appears only to be the threshold for deciding when to appoint an investigative committee. Both the 1978 resolution, which condemned apartheid, and the subsequent resolution in which the Regents ultimately decided to divest from companies doing business in South Africa state that "the system of apartheid and the oppressive practices of the Government of the Republic of South Africa" were "immoral and unconscionable." But even that language leaves unclear what besides apartheid would constitute an immoral or unconscionable practice of sufficient gravity to warrant divestment. Therefore,

although the existing policy sets up the procedure for dealing with exceptional cases, it leaves the divestment standard itself as something of an open question.

Some guidance, however, is provided by the charge to the committee, quoted in full at the beginning of the report. We found it useful to break the standard articulated in the charge into two questions:

1. What features of tobacco products and what activities of the tobacco industry warrant singling out tobacco securities for potential divestment?
2. Given the nature of the tobacco companies' products and activities, is the ownership of their securities "antithetical to the core missions of the University of Michigan" such that divestment is warranted?

The bulk of the report will be devoted to answering those two questions and to providing reasons for the committee's conclusions. Before moving to those questions, however, let us emphasize a few remaining preliminary but critical points.

First: Answering the tobacco-divestment question turns out to be a complex and difficult challenge. We emphasize this point only in response to a curiously prevalent notion that the tobacco-investment question is an "easy call." Many reasonable and intelligent people seem to believe not only that divesting from tobacco stocks is the right thing to do but also that a decision *not* to divest would be ludicrous. Interestingly, many equally reasonable and intelligent people seem to believe that a decision *to* divest would be ludicrous. Obviously, the ideas of not divesting and divesting cannot both simultaneously be ludicrous. Therefore, one service this report can perform, in addition to providing guidance to the Regents (who ultimately must make the decision), would be to provide everyone in the University community with a sense of the complexity of the issues at stake.

Second: Because of the nature of the inquiry in which we are engaged—trying to determine

if tobacco companies present a sufficiently exceptional case to warrant divergence from our normally ethically neutral investment policy—careful attention to the facts of this particular case is crucial to the enterprise. For that reason, this report devotes considerable space to setting forth and documenting the specific allegations that have been made against the tobacco industry, as well as the industry’s reply to those allegations. As a result of including this detail, however, the report goes on for some length. We apologize in advance for that fact and ask for the reader’s indulgence.

Third: The tobacco-divestment issue is not rendered moot by the fact that tobacco stocks have performed poorly of late. Many have suggested to us that the University should sell all of its tobacco securities on purely financial grounds and thereby avoid all of the difficult issues raised by the divestment question. After all, tobacco securities have declined significantly in value over the past few years. Moreover, a reasonable argument could be made that the financial future of the tobacco industry looks bleak, given that the industry has recently experienced several unprecedented setbacks in the courtroom and has agreed to pay out approximately \$246 billion over 25 years in settlement of the states’ Medicaid-reimbursement suits and given that cigarette sales in this country are on the decline.

However, a plausible case can be made that the financial future for the tobacco companies is not so dire. In the view of some tobacco-stock analysts, for example, if the tobacco industry can survive the most recent spate of lawsuits and can stave off direct regulation of their products by the Food and Drug Administration [FDA],² the future of the industry—even in the U.S.

² The FDA has asserted regulatory authority to regulate cigarettes as “drug delivery devices,” on the theory that nicotine is a drug as that term is defined in the Food, Drug, and Cosmetic Act. In that federal statute, a drug is defined as a substance, other than food, “intended to affect the structure or any function of the body.” The United States’ argument is that nicotine

market—looks encouraging. Moreover, many analysts contend that the financial future of the industry lies not the U.S. market but in the overseas markets, especially those in developing countries, where the number of potential customers dwarfs that in the U.S., where cigarette consumption is growing steadily, and where lawsuits, labeling requirements, and other safety regulation are virtually nonexistent (although such regulatory developments are beginning to emerge in some countries). Thus, in the view of these tobacco-stock analysts, if one considers only financial factors, now is the time to be *buying* tobacco-industry securities, not divesting of them.

clearly does meet this definition, given the recently disclosed evidence that tobacco companies have long known of the addictive qualities of nicotine, have expressly relied on those qualities to enhance the market for their products, and have even themselves characterized cigarettes as nicotine delivery devices. In 1998, however, a panel of the United States Court of Appeals for the Fourth Circuit decided in a 2-1 vote in favor of the industry and against the United States, holding that the FDA did not have the authority to regulate cigarettes as a drug delivery device. Essentially, the reasoning of the court was that, if cigarettes are held to be drug delivery devices, the FDA will have no choice but to ban them, given their obvious harmful effects; and that result could not be what Congress intended when it enacted the Food, Drug, and Cosmetic Act, since Congress itself had not banned cigarettes. The case was argued last fall before the U.S. Supreme Court and is currently pending final resolution.

In sum, the future of the tobacco industry is uncertain and making predictions about the tobacco industry's expected future stock prices is a risky enterprise, one for which this committee is not especially well suited. What is more important, even if we could reliably predict the industry's financial future, that ability would be irrelevant to the committee's assignment. There would remain the principle that this committee has been asked to address: Should the University adopt a policy of not owning tobacco securities, regardless of their performance, and if so, why? Providing answers to those questions is the aim of this report.³

We ultimately conclude that the University of Michigan should divest of its tobacco securities. In the next Part we explain the reasoning that underlies that conclusion and articulate principles that might be used in future divestment cases. Then, in Part IV, we state briefly our precise recommendations regarding what the University's tobacco-divestment policy should be. The committee is unanimous in its conclusions and in its endorsement of this report.

³ For similar reasons, we regard as irrelevant the fact that the University's tobacco holdings represent only a minuscule fraction of the overall endowment. Based on data made available to the committee in September 1999, and applying the Investor Responsibility Research Center's most recent definition of tobacco-product manufacturers, it is our understanding that tobacco-related securities amount to roughly 0.3 percent of the University's total portfolio value and roughly 1.4 percent of the common stock managers' portfolio value.

III. The Tobacco-Divestment Question

1. *What features of tobacco products and what activities of the tobacco industry warrant singling out tobacco securities for potential divestment?*

An important initial question is why, of all the many industries whose products or manufacturing processes or employment practices might raise objections, the University of Michigan has singled out tobacco companies for special scrutiny? What distinguishes tobacco companies from other companies? If no company or industry is perfect, why pick on tobacco? We answer this question in two parts. The first has to do with the nature of the tobacco product itself. The second has to do with the conduct of the companies, the way they have gone about their business.

1. The nature of tobacco products

Tobacco companies make a product that is unique in its capacity to cause death in its intended use. According to the Centers for Disease Control and Prevention [CDC], between the period 1990 to 1994, smoking caused roughly 430,000 deaths per year in the United States, or one in every five deaths.⁴ Tobacco use kills more people in this country each year than alcohol, illicit drugs, automobile accidents, violent crime, and AIDs combined.⁵ Furthermore, it is estimated that, worldwide, more than 4 million people die annually from tobacco use, a number

⁴ CDC, *Cigarette-Smoking-Attributable Mortality and Years of Potential Life Lost—United States, 1990-94*, 46 Mortality & Morbidity Weekly Rep. 448-51 (1997). In terms of average years of potential life lost, that amounts to 5.7 million years of life over that period alone, or an average of 13.4 years of life lost for each person whose death was attributable to smoking. Unless otherwise specifically stated, our information regarding the mortality and morbidity effects of smoking are taken from data put out by the CDC, some of which is available on their web site. <http://www.cdc.gov>. All web site references in this report were accurate as of the date of the report.

⁵ J. Michael McGinnis & William H. Foege, *Actual Causes of Death in the United States*, 270 JAMA 2207-2212 (1993).

that is expected to increase to 10 million by 2030, owing principally to the anticipated expansion of the cigarette market in developing countries.⁶ It is also estimated that, globally, smoking will cause 150 million deaths in the first quarter and another 300 million in the second quarter of the new century.⁷ The CDC nicely summarizes the current state of the overwhelming scientific consensus regarding the health effects of tobacco use: “[I]t is now well documented that smoking can cause chronic lung disease, coronary heart disease, and stroke, as well as cancer of the lung, larynx, esophagus, mouth, and bladder” and can contribute to cancers of the cervix, pancreas, and kidney. In addition, smokeless tobacco and cigars have been found to contribute to lung, larynx, esophageal, and oral cancer. And smoking causes nearly 90 percent of all lung-cancer deaths and has made lung cancer, which is the cause of 36 percent of cancer deaths, the leading cause of cancer mortality in both men and women.

⁶ World Health Organization, Press Release, October 12, 1999.

⁷ Dr. Gro Harlem Brundtland, Director-General, WHO, Speech to the World Health Organization International Policy Conference on Children and Tobacco, Washington, D.C., 18 March 1999.

Moreover, the risks of smoking are not limited to the smoker. The evidence continues to accumulate demonstrating the causal connection between “passive” or “sidestream” cigarette smoke and various serious diseases, including lung cancer, other respiratory ailments, and heart disease. At least since the Surgeon General’s Report on this question in 1986, passive smoke has been linked to lung cancer in adults and serious respiratory ailments in children.⁸ Then, in an influential report, the U.S. Environmental Protection Agency [EPA] concluded that passive smoke is responsible annually for 3000 lung-cancer deaths, and between 150,000 and 300,000 lower respiratory ailments in children.⁹ In the years since that report, the findings with respect to lung cancer and respiratory ailments caused by passive smoke have been confirmed in numerous studies. Moreover, a strong link between passive smoke and heart disease has now been established. According to the recent report from the California Environmental Protection Agency, compiling the results of a number of studies, 62,000 coronary-heart-disease deaths per year are attributable to passive smoke.¹⁰

⁸ U.S. Dep’t of Health & Human Services, Surgeon General Report, The Health Consequences of Involuntary Smoking (1986).

⁹ EPA, Respiratory Health Effects of Passive Smoking: Lung Cancer and Other Disorders (1992).

¹⁰ Health Effects of Exposure to Environmental Tobacco Smoke: The Report of the California Environmental Protection Agency (1999) (available at the National Cancer Institute’s web site: [http://rex.nci.nih.gov/NCI Monograph/INDEX.HTM](http://rex.nci.nih.gov/NCI_Monograph/INDEX.HTM))

Not only is tobacco by far the deadliest product on earth (according to the current overwhelming scientific consensus), it is, because of the effects of nicotine, also one of the most addictive. It is now well documented that nicotine has addictive properties similar to those found in other drugs, such as heroin and cocaine.¹¹ The following discussion, which paraphrases the conclusions of a 1995 FDA report,¹² provides some insight into the addictive properties of nicotine. First, tobacco users consume tobacco products regularly and compulsively.¹³ Second, the failure rate of those who attempt to stop or reduce their smoking is dramatic, even in the face of life-threatening tobacco-related illnesses. For example, although nearly 15 million people, almost one-third of all smokers, in the United States try to quit smoking each year, only about 10 percent of those would-be quitters (or 3 percent of all smokers) achieve long-term success. Indeed, cigarettes and smokeless tobacco products may be the only major consumer product that a majority of users want to quit using, but cannot.¹⁴ Moreover, tobacco use persists despite its harmful and often deadly consequences. Third, consumers who abstain from tobacco products experience withdrawal symptoms; and nicotine has been shown to produce tolerance (the lessening of the desired effect over time or the need for higher doses to produce the same effect) among tobacco users. Given these findings, nicotine clearly satisfies the classic criteria for an

¹¹ U.S. Office on Smoking & Health, Dep't of Health & Human Services, *The Health Consequences of Smoking: Nicotine Addiction, A Report of the Surgeon General* (1988) (references omitted).

¹² FDA, *Analysis Regarding The Food and Drug Administration's Jurisdiction Over Nicotine-Containing Cigarettes and Smokeless Tobacco Products*, 60 Fed. Reg. 41453 (Aug. 11, 1995).

¹³ For example, over 80 percent of people who smoke cigarettes smoke every day.

¹⁴ In response to the 1993 National Health Information Survey, 70 percent of current smokers reported that they would like to stop smoking cigarettes completely.

addictive substance.¹⁵ Indeed, the FDA report concludes that “a large body of compelling and widely accepted scientific evidence now exists that establishes that nicotine is addictive.”

¹⁵ According to a national household survey conducted by the U.S. Department of Health and Human Services in 1991-92, between 83 percent to 87 percent of cigarette smokers who smoke more than 26 cigarettes a day believe they are addicted. (At the time of the survey, the average smoker smoked more than 30 cigarettes a day.)

All of these facts about tobacco products—the ill-health effects and the addictive qualities—are especially troublesome when one considers that most nicotine addiction, and thus most long-term smoking, begins when smokers are teenagers, at an age when they are least likely to understand the full, long-term implications of their decision to start smoking. According to the CDC, 82 percent of adult smokers in this country began smoking before they reached the age of 18.¹⁶ Similarly, according to several studies summarized in a 1994 Surgeon General’s report, of people who have ever smoked daily, around 70 percent were smoking daily by the time they reached the age of 18.¹⁷ And according to the Monitoring the Future study, conducted by the University of Michigan’s Institute for Social Research, although smoking among teenagers appears to have declined slightly over the last two years, the drop has been quite small; and the levels of teenage smoking remain near their all-time-high levels in 1996 and 1997.¹⁸ Finally, consider the following much-quoted statement from Secretary of Health and Human Services Donna Shalala:

Today, nearly 3,000 young people across our country will begin smoking regularly. Of these 3,000 young people, 1,000 will lose that gamble to the diseases caused by smoking. The net effect of this is that among children living in America today, 5 million will die an early, preventable death because of a decision made as a child.¹⁹

¹⁶ CDC, *Trends in Smoking Initiation Among Adolescents and Young Adults*, 44 Morbidity & Mortality Weekly Rep. 521 (1995).

¹⁷ Preventing Tobacco Use Among Young People: A Report of the Surgeon General (1994).

¹⁸ Press Release, Cigarette smoking among American teens continues gradual decline, Dec. 17, 1999: <http://monitoringthefuture.org/pressreleases/99cigpr.html>

¹⁹ CDC, Targeting Tobacco Use: The Nation’s Leading Cause of Death—At a Glance (1999).

Not only is tobacco by far the deadliest product on earth, not only is its deadly effect felt most often by adults who became regular smokers when they were children, but also tobacco is deadly in its normal and intended use. Put differently, the problem is not that smokers are misusing tobacco products; that is, they are not using tobacco products in a manner contrary to the intentions of the manufacturer. They are using those products precisely as the manufacturer intends that they be used. They are smoking lots of cigarettes over long periods of time. And it is *that* pattern of use which kills.²⁰ The problem, of course, is that there is no safe way to smoke a cigarette, at least as cigarettes are currently designed.

2. The conduct of the tobacco industry

In 1954 the major tobacco companies placed a full-page advertisement in 448 newspapers across the country. The ad, entitled “A Frank Statement to Cigarette Smokers,” stated that there was no proof that cigarettes cause lung cancer and, further, included the following assurance from the tobacco industry:

We accept an interest in people's health as a basic responsibility, paramount to every other consideration in our business.... We always have and always will cooperate closely with those whose task it is to safeguard the public health.... We are pledging aid and assistance to the research effort into all phases of tobacco use and health.²¹

²⁰ Tobacco companies, of course, will argue that they do not intend for people to begin smoking when they are under the legal age of 18. As we explain below, however, given the available evidence about tobacco companies’ marketing strategies, that assertion simply is not credible. And in any event, even if no one started smoking until they were of legal age, if lots of people smoke lots of cigarettes over a long period of time—which even the tobacco industry would admit is, from the industry’s perspective, the whole point—the death toll would remain enormous.

²¹ A full copy of this advertisement can be viewed at www.tobacco.org/History/540104frank.html.

In conjunction with this pledge, the industry founded the Tobacco Industry Research Committee (later called the Council for Tobacco Research) ostensibly for the purpose of fulfilling the promise laid out in the “Frank Statement.” However, according to the overwhelming evidence that has come to light in recent years, which will be summarized in this Section of the report, it is now clear that the industry never had any intention of fulfilling the above-quoted commitment to the public’s health and that, in fact, the Research Council was formed as a public relations front designed to placate smokers’ concerns about the health effects of smoking. Indeed, according to allegations in many of the state Medicaid suits as well as in the recently filed federal suit against the tobacco industry, both the Frank Statement and the creation of the Research Council were parts of a unified “enterprise” on the part of the tobacco industry to suppress research about the health hazards of tobacco use.²²

Since its first public statement about the safety of cigarette smoking back in 1954, the tobacco industry has, until very recently, consistently and adamantly taken the position that (a) there is no conclusive proof that smoking causes diseases such as cancer and heart disease; (b) smoking is not addictive; and (c) tobacco companies are committed to determining the scientific truth about the health effects of tobacco, both by conducting internal research and by funding external research.²³ As discussed in Section A above, there has long been little doubt in the scientific community that smoking causes numerous diseases and that nicotine is powerfully addictive. Given such a general scientific consensus, it seems reasonable to assume that the industry must have known those facts as well, despite their protestations to the contrary. Over

²² The allegations in the federal suit are summarized below.

²³ Stanton Glantz et al., *The Cigarette Papers* (University of California Press) (1996) (<http://www.library.ucsf.edu/tobacco/cigpapers/book>).

the past five years, evidence has been disclosed indicating that, in fact, the industry has known these facts about their products for many years. As the result of the testimony of several “whistle blowers” (including ex-industry research scientists) and the internal tobacco-industry documents that have been made available, the last few years have produced considerable evidence to support the following conclusions:²⁴

²⁴ The following summary is taken largely from *The Cigarette Papers*, id., which is based on an analysis of the Brown & Williamson and its parent corporation, British American Tobacco, documents made public in 1994. These documents are available at <http://www.library.ucsf.edu/tobacco>. Other sources include written summaries of testimony before Congressional committees by former tobacco-industry scientists, including some scientists from Philip Morris, as well as by former FDA Commissioner Dr. David Kessler.

- At least by the early 1960s (and perhaps as early as the 1950s), the industry's own research revealed a causal connection between cigarette smoking and various diseases, including cancer and lung disease. During this same period, of course, independent researchers had come to the conclusion that smoking causes lung cancer, heart disease, and other respiratory ailments.²⁵ Despite all of this research, however, the industry continued in all of its public statements to deny that any such causal link had been established.
- In the 1970s, tobacco companies concluded *privately* that the causal link between cigarette smoking and various diseases was no longer a matter of controversy—but was irrefutably established. However, all of the industry's public statements continued to deny any causal link.
- At some point in the 1970s and early 1980s, the tobacco companies not only stopped doing research into the health effects of tobacco use, they consciously decided not to disclose to the public the evidence that had previously been gathered establishing such a link. What's more, in some cases they even *actively suppressed* those findings by shipping files out of the country.

²⁵ See, for example, the Surgeon General's 1964 report.

- Also by the early 1960s, the industry had developed a sophisticated understanding of the addictive properties of nicotine.²⁶ The scientific community was slower to appreciate nicotine addiction. It was not until 1988 that the Surgeon General reported definitively that tobacco was addictive, that nicotine was the addictive agent, and that the addictive properties of nicotine were similar to those of heroin and cocaine. Throughout all of this, the tobacco industry consistently maintained publicly that nicotine is not addictive. In fact, in their infamous appearance before a House subcommittee in 1994, the chief executives of the top seven tobacco companies again testified specifically, and under oath, that they did not believe nicotine was addictive.
- The tobacco companies have long been able to, and regularly do, artificially enhance the level of nicotine in their products through patented techniques of genetic-engineering. The industry has now admitted this, although they continue to insist publicly that they enhance the nicotine levels (and refrain from eliminating nicotine altogether, which they could do) not to addict smokers or to maintain their addictions but to improve or maintain the “taste” of cigarettes.

There is also substantial evidence that tobacco companies have, for many years, focused their marketing efforts on children and have explicitly tried to get children hooked on smoking.

This conclusion, which the industry continues to deny, is supported by the following quotations

²⁶ Consider the following three examples of documents supporting this conclusion: (1) “There is increasing evidence that nicotine is the key factor in controlling, through the central nervous system, a number beneficial effects of tobacco smoke, including its action in the presence of stress situations. In addition, the [nicotine] appears to be intimately connected with the phenomena of tobacco habituation (tolerance) and/or addiction.” From “The Fate of Nicotine in the Body,” a report describing results of contract research conducted for British American Tobacco by a Swiss research institute (1963). (2) “Moreover, nicotine is addictive. We are, then, in the business of selling nicotine, an addictive drug effective in the release of stress mechanisms.” Statement of Addison Yeaman, vice president and general counsel, Brown & Williamson (1963). And finally, the following is among the most telling quotes regarding the industry’s view of nicotine:

The cigarette should be conceived not as a product but as a package. The product is nicotine.... Think of the cigarette pack as a storage container for a day’s supply of nicotine.... Think of the cigarette as a dispenser of a dose unit of nicotine.... Think of a puff of smoke as the vehicle of nicotine.... Smoke is beyond question the most optimized vehicle of nicotine and the cigarette the most optimized dispenser of smoke.”

From an internal Philip Morris memorandum, written by Vice President William L. Dunn, Jr., entitled “Motive and Incentive in Cigarette Smoking” (1971).

from internal tobacco industry documents, of which there are many more in the thousands of such documents found at various addresses on the world wide web:

- “Evidence is now available to indicate that the 14-18 year old group is an increasing segment of the smoking population. RJR-T must soon establish a successful new brand in this market if our position in the industry is to be maintained in the long run.” From a 1976 RJR internal report entitled “Planned Assumptions and Forecast for the Period 1977-1986.”
- “Today’s teenager is tomorrow’s potential regular customer, and the overwhelming majority of smokers first begin while still in their teens... The smoking patterns of teenagers are particularly important to Philip Morris.” From a 1981 Philip Morris internal document.
- "The teenage years are also important because those are the years during which most smokers begin to smoke, the years in which initial brand selections are made, and the period in the life cycle in which conformity to peer group norms is greatest." From a 1975 Philip Morris memo entitled “The Decline in the Rate of Growth of Marlboro Red.”
- "Smoking a cigarette for the beginner is a symbolic act. . . 'I am no longer my mother's child, I'm tough, I am an adventurer, I'm not square.' . . . As the force from the psychological symbolism subsides, the pharmacological effect takes over to sustain the habit. . . ." From a 1969 draft report to the Philip Morris Board of Directors.
- "[Project LF is a] wider-circumference nonmenthol cigarette targeted at young adult male smokers (primarily 13-24-year-old male Marlboro smokers)." From a 1987 RJR memo describing the Camel Wides brand, under the code name Project LF.

Additional circumstantial evidence of the industry’s focus on children is that 86 percent of the kids who smoke prefer the three most heavily advertised brands of cigarettes; whereas, only about one-third of adult smokers choose those brands.²⁷

The revelations over the last few years about the industry’s long history of egregious misconduct, of the sort sampled above, have spawned a massive new wave of litigation against

²⁷ CDC, *Changes in the Cigarette Brand Preference of Adolescent Smokers*, U.S. 1989-93, Morbidity & Mortality Weekly Report, August 1994. Many more documents with similar quotes can be found at various sites on the web. For example, see <http://www.tobaccofreekids.org>.

tobacco companies. In addition to the individual suits that have long been brought by smokers and their families against tobacco companies, numerous groups of smokers as well as victims of second-hand smoke have banded together to bring class-action suits against the industry. Some of those suits continue to be litigated. Perhaps the most important development in tobacco litigation, however, is the series of lawsuits brought by the state attorneys general seeking reimbursement from the tobacco industry for the states' tobacco-related Medicaid expenses. Those suits were eventually settled under terms that, among other things, call for the big tobacco companies to pay the states roughly \$246 billion over the next 25 years and impose some restrictions on tobacco-industry advertising (such as forbidding the use of cartoon characters, such as Joe Camel).²⁸

Also relying on the recently released internal industry documents, the United States Department of Justice last September filed a civil lawsuit against the eight largest tobacco companies, as well as against the industry-run organizations—the Council for Tobacco Research (mentioned above) and the Tobacco Institute. This suit seeks recovery for the billions of dollars the federal government spends each year on smoking-related health care costs, which the complaint alleges to be in the neighborhood of \$20 billion per year. The government's suit is based on three statutes: the Medical Care Recovery Act, the Medicare Secondary Payer Act, and

²⁸ The settlement of the state suits took place in two major parts. First, four states—Mississippi, Florida, Texas, and Minnesota—reached their own, separate settlement agreements with the industry, which provided, among other things, that those states would receive a total of \$35 to \$40 billion over 25 years. (According to one estimate, Mississippi was to receive \$3.5 billion, Florida \$11.3 billion, Texas \$15.3 billion, and Minnesota \$6.6 billion, for a total settlement cost of \$36.8 billion over 25 years, with some additional unspecified payments to Mississippi, Florida, and Texas to continue thereafter.) In the November 23, 1998, Multistate Master Settlement Agreement, the other 46 states agreed to release their claims against the tobacco industry in exchange for a number of concessions from the industry, including an agreement from the industry to pay those states approximately \$206 billion over 25 years. For a summary of the terms of Master Settlement Agreement, see <http://www.tobacco.neu.edu/msa/index.html>.

the civil provisions of the Racketeer Influenced and Corrupt Organizations (RICO) statute. In the complaint, the government alleges, among other things, that the tobacco industry:

- made false and misleading statements to create a false controversy about whether smoking causes disease, even though they knew that smoking did cause disease;
- made false promises that they would undertake or sponsor research to determine whether smoking causes disease;
- sponsored research that was designed not to answer the question of whether smoking caused disease, promoted biased research that would assist in defending lawsuits brought by injured smokers, and suppressed research that suggested that smoking causes disease;
- denied that nicotine was addictive;
- failed to warn consumers about the effects of smoking, including that cigarettes are addictive;
- refrained from developing, testing, and marketing potentially less hazardous products; and,
- denied that they marketed and/or targeted products to children, although they actively sought to capture the youth market.²⁹

²⁹ Press Release, United States Sues Cigarette Companies to Recover Federal Health Care Costs, September 22, 1999. Available at: <http://www.usdoj.gov/01whatsnew>

How the court will rule on the federal government's claims—or whether the parties will settle before the case reaches trial—remains to be seen. However, it is clear that the lawyers in the Department of Justice, after combing through all of the tobacco-industry documents now available, have concluded that the above-listed allegations are true.³⁰

3. Conclusion

In sum, tobacco companies can be distinguished from other companies by the nature of the product they make and sell—including the unrivaled death toll attributable to tobacco use, the powerful addictive qualities of nicotine, the fact that most smokers become addicted when they are teenagers, and the fact that cigarettes are deadly when put to their normal use. In addition, based on what has been learned over the past few years from internal industry documents, it is clear that the tobacco industry over the past 45 years has engaged in dishonest, deceptive, and generally reprehensible conduct unparalleled in the history of American business and at a cost of millions of lives. Thus, given the evidence reviewed in this part, there is little mystery why the tobacco industry was singled out for this committee's scrutiny.

B. *Given the nature of the tobacco companies' products and activities, is the ownership of their securities "antithetical to the core missions of the University of Michigan" such that divestment is warranted?*

The committee found it useful to subdivide this question into two parts: First, are the attributes of tobacco products and the activities of the industry antithetical to the core missions of the University? Second, is the ownership of securities in such companies antithetical to the core missions of the University such that divestment is called for? We also address separately, and briefly, the question whether some response other than divestment might be appropriate as well

³⁰ In the appendix to its complaint, the government lists 116 separate "racketeering acts" that were allegedly perpetrated by the defendants.

as the slippery-slope concern, which is often raised in discussions of divestment.

1. Are the attributes of tobacco products and the activities of the industry antithetical to the core missions of the University?

We had little difficulty concluding that the answer to this question is unequivocally yes. The core missions of the University, as described in the University's mission statement and by-laws, are: teaching, research, and service. In our view, the tobacco companies' activities can easily be seen as antithetical to all of those missions. If there is anything that unifies the three core missions, it is the pursuit and dissemination of truth and knowledge: We conduct research to find truth and create knowledge; we teach as a means of disseminating that knowledge, encouraging its pursuit, and instilling respect for its value; and we put that knowledge to public use in various areas of service to the community.

The brazen dishonesty of the tobacco industry for so many years about a matter of such enormous public-health significance is, in the view of this committee, unquestionably antithetical to the core missions of the University. The industry's refusal to reveal the results of its own research linking tobacco use and disease, its efforts actively to hide its own damning research results, its persistent public denials of any link between tobacco and disease (despite its knowledge to the contrary), and its cynical and hypocritical attempt for years to cloak itself with the mantle of scientific legitimacy combine to constitute the most blatant and deplorable contradiction of academic values by a single business or industry in modern history—again, at a cost of untold misery and death.

What's more, the actions of the tobacco industry, when coupled with the nature of tobacco products, are especially antithetical to the missions of *this* University, given our commitment to teaching, research, and service in the fields of health care and public health. The

committee will not try to provide an exhaustive list of all the schools, colleges, and departments in this University that have, as part of their mission, the pursuit of some aspect of health care or public health. Nor will we offer a count of all the members of the University community who have devoted all or a portion of their careers to the pursuit of teaching, research, or service in those fields. But the list would be long, and the number would be large. In addition, Michigan has, as a central part of the University community, one of the great research and teaching hospitals in the world, whose central purpose, almost by definition, is teaching, research, and service for the benefit of human health.

Thus, when we realize that tobacco use has often been called the greatest human health disaster of the 20th century and continues in the new century to be considered “public health enemy number one,” the phrase “antithetical to the core missions of the University” seems a profound understatement. We emphasize, however, that our conclusion on this point depends on *the combination of* the establishment beyond a scientific doubt of the harmful effects of tobacco use *and* the overwhelming evidence of dishonest conduct by the tobacco industry over many years in a manner that is directly contradictory to this University’s most central values. In other words, without both of these elements, the committee would not have reached the conclusion that it did.

2. Is the ownership of securities in such companies antithetical to the core missions of the University, such that divestment is called for?

The difficulty in the analysis comes when we ask the precise question that has been put to the committee: whether *owning securities* in tobacco companies is antithetical the core missions of the University. Normally ownership of a company’s securities does not imply endorsement of that company’s behavior. As discussed in Part I above, that conclusion follows from the sensible

observation that no corporation can be perfect, even from the perspective of the University's "core missions," and therefore no investment can be pure. Indeed, every company in which we might conceivably invest could, at some point, do something that might be considered inconsistent with, or even antithetical to, the highest ideals of the University. Therefore, we are inevitably faced with questions of gravity and magnitude. For example, it seems likely that many companies in many different industries have on occasion been guilty of dishonest, even fraudulent, business practices, including dishonest or fraudulent commercial research activities that could be considered antithetical to the core academic values described above. However, for *ownership* of such a company to be antithetical to the University's core missions, the question of gravity or magnitude becomes essential.

In our view, to justify such a finding, the magnitude of both the misbehavior in question and the harm caused by that misbehavior must be so extreme that the company or industry would be considered a clear outlier in the corporate community. In our view, the evidence discussed in Part A, concerning the reprehensible nature of tobacco industry's conduct and the extraordinary harm caused by tobacco products, is sufficient to meet this magnitude test. Thus, the committee unanimously concludes that the ownership of tobacco securities is antithetical to the University's core missions such that divestment is called for. In Part IV below, we spell out precisely what we mean by "divestment."³¹ We emphasize again that our conclusion rests on the combination of the industry misbehavior and the irrefutable evidence of tobacco's harmful effects. Neither alone would be sufficient.

In reaching the conclusions just summarized, however, the committee was forced to

³¹ Also, in Section III.B.3 below we explain why, in our view, a response by the Regents short of divestment would not be sufficient in this case.

address a number of difficult questions. For example, what about the fact that tobacco products and smoking are legal in this country? If our democratically elected government has decided that smoking should not be prohibited, or even seriously regulated (as is currently the case, with the exceptions of warning labels, television advertising, and sales to minor), why should the University feel the need to take a public stand against the tobacco companies? Although reasonable people could certainly disagree on this issue, we conclude that the current legal status of smoking should not be considered a decisive factor in our deliberations. Indeed, one could argue that it is irrelevant. The procedure that the Regents adopted for dealing with divestment-related issues presumably has application *only* in cases involving legal activities. That is, if smoking and tobacco-product manufacturing were illegal (in the sense of being completely prohibited under threat of criminal penalty), there would be no divestment issue, because there would be no tobacco securities. That is, it would be illegal for tobacco companies not only to exist, but to issue stock. And it would be illegal to own any interest in such companies, whatever form that interest might take. Thus, it is only with respect to companies that are engaged in legal activities, but activities that may be considered antithetical to the University's core missions, that the divestment issue arises.³²

Moreover, although neither the use (by adults) nor the manufacture of tobacco products is illegal, it would be an overstatement to claim that our democratically elected government is indifferent or neutral with respect to the tobacco industry. The lawsuit that was recently filed by

³² For example, if the U.S. government had in the 1970s or 1980s passed a law prohibiting ownership of securities in companies doing business in South Africa, the divestment question would not have been an issue. As it turns out, the state of Michigan did pass a law prohibiting state educational institutions, including public universities, from investing in companies doing business in South Africa or in the old Soviet Union. That law, however, was held to be unconstitutional as applied to the University of Michigan, because of the University's independent status under the state constitution. See generally *Regents of the University of Michigan v. State of Michigan*, 166 Mich. App. 314, 419 N.W.2d 773 (1988).

the Justice Department reveals that at least the federal government has determined that the tobacco companies themselves have been guilty of nearly criminal conduct. Although the Department decided not to pursue a criminal case against the industry, the allegations within the civil complaint (summarized above) are as close to alleging criminal activity as one can get without invoking the criminal label (and the higher standard of proof associated with a criminal prosecution). And the cases brought by the state attorneys general made similar allegations. Although for the purpose of determining liability, innocence is assumed until guilt is proven, the facts on which the allegations are based are not seriously in dispute. Indeed, we can go to various sites on the worldwide web and read the documents for ourselves. Passages from some of them are quoted above. What is important to remember is this: For the University of Michigan, the issue is not the criminality or even the civil liability of the companies; the issue is whether the industry's conduct (taken together with the inherent effects of tobacco use) is antithetical to the University's core missions. And we conclude that it is.

A second difficult question involves the recent efforts of some tobacco companies to polish their public images. For example, several tobacco-company executives have, when recently confronted with the documents of the sort quoted in the previous section, expressed regret that any such statements could ever have been made by employees of their companies. They further insist that those statements (whatever they say about the tobacco companies of old) do not accurately portray the current corporate culture at *their* tobacco companies.³³ For another

³³ For one example, Philip Morris CEO Geoffrey Bible, in the Minnesota Medicaid suit, gave the following response when asked about a 1969 internal Philip Morris report about why 16-year-olds start smoking: "I'm ashamed at that. I don't like to see something from the company talking about 16-year-olds. We do not market cigarettes to underage people." Similarly, during the same lawsuit, in response to evidence indicating that former Philip Morris officials had lied to the public, Mr. Bible gave the following pledge: "I can give you a solemn undertaking, so

example, in late 1999, Philip Morris put on its corporate web site a statement regarding the health effects of smoking, a statement that explicitly acknowledges the scientific consensus that smoking causes disease.³⁴ Specifically, Philip Morris now says “[t]here is an overwhelming medical and scientific consensus that cigarette smoking causes lung cancer, heart disease, emphysema and other serious diseases in smokers.” Moreover, as to the question of addiction, Philip Morris now says that “[c]igarette smoking is addictive, as that term is most commonly used today. It can be very difficult to quit smoking but this should not deter smokers who want to quit from trying to do so.”³⁵

What are we to make of all this recent evidence of a “change of heart” within the industry? It could, for example, be argued that, whereas divestment might have been appropriate a few years ago, it no longer is, because the industry has mended its ways. In our view, however, the recent steps taken by the tobacco companies to polish their public images, even if taken at face value, are far too little and too late. That is, given the nature of tobacco products and given the industry’s long history of dishonesty regarding the health effects of their products, we are unmoved by an eleventh-hour assertion that the companies have turned over a new leaf.

Moreover, we do not take the industry’s recent assertions at face value. We regard it as significant that the industry’s recent statements were made only after the incriminating documents were made public and after, largely as a result of those disclosures, the threat of

long as I'm watching this company, these things won't happen." A similar sentiment is captured in the following from Brown & Williamson CEO, Nicholas Brookes, who said to the House Committee on Commerce in 1998: "We ask you to judge us not by looking at the past, but rather by looking at what we have committed to do in the future."

³⁴ http://www.philipmorris.com/tobacco_issues/health_issues.html.

³⁵ This characterization of the addictive qualities of nicotine—“addictive as that term is normally understood”—is consistent with the view expressed by several tobacco company CEOs in 1998 testimony before Congress.

bankrupting lawsuits became a serious possibility for the industry. We also regard it as significant that the industry has worded its recent “admissions” in a manner that can be (and has been) interpreted as cynical and manipulative. For example, Philip Morris’s concession regarding the “overwhelming medical and scientific consensus” that smoking causes disease is not an admission that, in fact, smoking does cause those diseases. To the contrary, company executives have stated, when pressed, that they will continue to employ the same strategy in lawsuits against them that they have employed all along: denying that a causal relationship between smoking and disease has been proven.

In addition, the company’s “official” statement on the web regarding this causal connection might be understood as an effort to enhance the industry’s litigation position in future cases by strengthening the industry’s so-called “assumption of risk” defense. Under the assumption-of-risk doctrine in products liability law, if an injured plaintiff is found to have known of the specific risk associated with a particular product and to have nevertheless voluntarily assumed that risk in using the product, the manufacturer of the product in question can escape tort liability. Thus, in future product-liability cases brought by or on behalf of individuals who started smoking after 1999, tobacco companies may, as a result of the Philip Morris web site, have a somewhat stronger argument that those individuals “assumed the risks” associated with smoking.

Interestingly, one can also interpret the industry’s latest position on nicotine addiction to be consistent with an attempt to strengthen (or avoid weakening) the industry’s assumption-of-risk defense. If juries around the country begin to take seriously the conclusion of the scientific community that nicotine has addictive properties similar to those of heroine and cocaine, the industry’s assumption-of-risk defense weakens significantly. That is to say, if nicotine is *that*

highly addictive, given that most long-term smokers get addicted to smoking when they are teenagers (when they are most likely to overestimate their own ability to overcome nicotine addiction and least able to make rational, long-term decisions about what sorts of life-shortening risks to “assume”), the tobacco industry’s assumption-of-risk defense loses much of its force. Thus, it is likely no coincidence that Philip Morris, and apparently the rest of the industry, still do not concede that nicotine is addictive in the way that cocaine and heroine are addictive.

Finally, in deciding to take the industry’s recent public posturing at less than face value, we were influenced by the fact that the industry has a long, well-documented history of successfully using its vaunted public-relations machinery not to produce real change (such as the reduction of smoking among teenagers) but to protect itself from the threat of lawsuits or serious regulatory restrictions.

For all these reasons, we view the industry’s recent public relations efforts with skepticism and certainly not as exculpatory for all the harm they have caused. Although we concede that, in theory, the tobacco industry might someday so transform itself—that is, not only change the nature of its product but also its corporate culture—that the concerns prompting this report would be reduced or even eliminated, that time has certainly not yet arrived and does not, to us, appear to lie in the foreseeable future.

The third difficulty presented by the question whether ownership of tobacco securities is antithetical to the University’s core missions is the fact that many members of the Michigan community, including many current employees of the University, are smokers. In addition, there are some in the Michigan community who regard divestment from tobacco stocks as inappropriate. Would the University, by taking a stand on the issue of tobacco (either through divestment or some other action), be in effect silencing those people or encroaching on the rights

of the smokers? After all, a core value of the University certainly is the freedom of expression, especially the freedom to hold and express controversial views; and the last thing the University should do is to discourage debate or freedom of thought on these issues. However, we see nothing inconsistent with the University's, on one hand, deciding that ownership of securities in tobacco companies is antithetical to its core missions and, on the other hand, maintaining an environment of free exchange of ideas on the tobacco issue. Surely, if the University's official smoking policy—which bans smoking in all University facilities (including parking structures and University vehicles) and even bans smoking within 50 feet of outer door entrances—is not considered a problem from the perspective of squelching debate on tobacco-related issues, a decision by the Regents that the University will no longer profit from the sales of cigarettes would not present insurmountable freedom-of-expression difficulties. For example, that the University has taken a strong position regarding affirmative action is not intended to, nor does it in fact, quell discussions of the merits of affirmative action in classrooms or elsewhere in the University community.

In sum, notwithstanding these difficult issues, we conclude that owning securities in tobacco companies is antithetical to the core missions of the University.

3. What about responses other than divestment?

As the charge framed the question to the committee, the conclusion just stated would seem to imply necessarily a recommendation to divest. However, we assume that the Regents are also interested in our views as to whether, given our conclusions regarding the “core missions question,” some response by the University other than divestment might be more appropriate.³⁶ Put differently, even if the conclusion is reached that ownership of tobacco securities is antithetical to the University’s core missions, should the “voice” option be chosen over the “exit” option. For example, in the South Africa case, before deciding ultimately to divest, the Regents began exercising the voice option, that is, by instructing the CFO to send out letters urging the companies doing business in South Africa to adopt something comparable to the Sullivan Principles. The Sullivan Principles, originally proposed by the Reverend Leon Sullivan, called for the companies to adopt strict policies of racial equality and to take steps to improve the job prospects and the lives of all their South African employees, including those of all races.

³⁶ This report, however, is first and foremost a response to the divestment question posed explicitly in the charge to the committee. Therefore, nothing in the report should be interpreted to foreclose the possibility that, in future cases presenting “serious moral or ethical questions which are of concern to many members of the University community,” some action short of divestment might be taken by the University, even if those cases do not meet the exceedingly high divestment thresholds (described in sections III.B.1 and III.B.2 above) that are met in this case.

The University could do something similar in this case. It could, for example, send letters to the tobacco companies urging them to stop marketing to children (or, because of the impossibility of preventing their advertising from affecting children, to stop advertising at all); it could also urge the companies to eliminate nicotine from their products, to invest more money in research efforts to develop a “safe” cigarette, and to place warnings on tobacco products being sold in developing countries. Or the University could vote their proxies for such proposals when and if they are raised at shareholder meetings. Some institutions, including universities, have taken such an approach.³⁷

In our view, however, such efforts would be extremely unlikely to have any effect on the tobacco companies’ practices. Other institutions, whose ownership stake in the tobacco industry far exceeds that of this University, have been sending such letters and voting their proxies in such a manner for years, with no discernible effect. Indeed, of the institutions that have already divested of tobacco securities, several did so only after attempting first to influence the industry in the ways suggested, only to discover that the industry was unresponsive to such attempts.³⁸

³⁷ For a recent and thorough survey of what other institutions, including insurance companies and public pension funds as well as colleges and universities, have done with respect to the tobacco-investment question, see Investor Responsibility Research Center [IRRC], *Tobacco Divestment and Fiduciary Responsibility: A Legal and Financial Analysis* (Douglas G. Cogan, editor) (2000).

³⁸ For example, Harvard University, which divested in 1990, did so only after first sending letters to the tobacco companies asking them to address the university’s concerns regarding, among other things, the industry’s marketing practices in developing countries and the problem of underage smokers. Some companies did not respond. Those that did insisted that they planned to continue their existing marketing practices in developing countries. Some responded by denying the link between tobacco use and disease. In announcing the Harvard Corporation’s decision to divest, University President Derek Bok stated that the Corporation “was motivated by a desire not to be associated as a shareholder with companies engaged in significant sales of products that create a substantial and unjustified risk of harm to other human beings.”

Some activist organizations have gone so far as to purchase stock in the tobacco companies for the sole purpose of going to shareholder meetings and urging the companies to take such steps, again to no avail. Thus, we conclude that it would be pointless to try to influence the tobacco companies in that way. Our only serious option, if we choose to act at all, is to disassociate ourselves from the industry; and the only way to do that effectively is by divestment.³⁹

4. The slippery-slope concern

³⁹ Among the educational institutions, besides Harvard, that have divested from tobacco securities expressly for ethical reasons are the City University of New York, Johns Hopkins University, and Wayne State University. All of these institutions divested in 1990 or 1991. Starting in the mid-90s, a number of other educational institutions followed suit, including Pomona College, Santa Clara University, Smith College, Mt. Holyoke College, Haverford College, and Bryn Mawr College. In 1998 Stanford University also divested its tobacco holdings, but it did not issue a public statement explaining precisely the reasons for this decision. A large number of educational institutions, of course, have not adopted tobacco divestment policies or at least have not done so publicly. Two prominent examples are Yale University and Cornell University, both of which have considered the tobacco-divestment question several times and have explicitly decided not to divest. The Yale Corporation reaffirmed its decision as recently as April 1998.

Before stating our precise recommendations regarding divestment, there is one final issue that needs to be addressed. It is this issue that, for many people, is the most powerful reason not to divest from tobacco securities. It is the so-called slippery-slope problem. According to this argument, the University should not divest from tobacco, because tobacco products cannot be distinguished from many other products that cause disease or injury and because the behavior of tobacco companies cannot be distinguished from that of any number of other industries. If we decide to divest from tobacco, therefore, we will set into motion a process that has no clear stopping point. And although divesting from tobacco securities will have essentially no effect on the riskiness and return of the University's investment portfolio,⁴⁰ the slippery slope created by the tobacco-divestment decision may pose a real threat. This is certainly a legitimate concern, one worthy of careful consideration. In the committee's view, however, the slippery-slope concern should not prevent the Regents from acting in this case to approve the committee's divestment recommendation, for several reasons.

First, the procedure adopted by the Regents in 1978 for dealing with cases that involve "serious ethical and moral questions" not only assumes the possibility of overcoming the slippery-slope concern, it creates a process that minimizes that concern. That is, if the Regents decide to divest from tobacco, any future case in which someone has a complaint about immoral or unethical behavior by a company that the University invests in and wishes to pursue the divestment option will have to go through all of the same steps that the tobacco case did.

Second, and related, the ultimate decision regarding whether to divest in this case or any future case ultimately rests with the Regents themselves. Therefore, the final, and perhaps best, check against the slippery slope is the judgment of this Board and future Boards of Regents who

⁴⁰ This conclusion regarding the effects of tobacco divestment on the endowment comes to the committee from Executive Vice President and CFO Kasdin.

can evaluate each case on its own merits.

Third, if the tobacco case is taken seriously as a precedent (as the slippery-slope argument assumes it will be), this report should help to allay slippery-slope concerns. To reiterate, it is this committee's conclusion that divestment is appropriate in this case because of *the combination of* the extraordinary death toll attributable to tobacco products (a fact that is now beyond scientific dispute) *and* the deplorable and unparalleled conduct of this industry for decades that directly contradicts the core missions of the University. If future divestment cases are held to a similar standard, the slippery-slope concern would seem to be quite small.

And finally, the slippery-slope concern is probably exaggerated in any event. The Regents voted in 1978 to take action in the South Africa case (divesting finally in 1983), and that decision did not open a floodgate of "next cases" in which the University was subject to significant pressure to divest from companies doing business in every other country in the world that violated human rights. Some 20 years later, the Regents are now asked to divest from tobacco stocks. In this committee's view, a decision to divest in this case likewise is unlikely to open a floodgate of next cases.

IV. The Committee's Recommendations

For all the reasons set forth above, we recommend that the Regents adopt a policy of divestment with respect to tobacco-company securities. More specifically, we recommend that the Regents adopt a resolution directing the Chief Financial Officer to instruct the University's portfolio managers to sell all of the University's currently owned shares of stock (and not to purchase any new shares) in companies that, either themselves or through their subsidiaries, manufacture significant quantities of cigarettes or other tobacco products. For the task of identifying which companies qualify under this definition of tobacco-company securities, we recommend the use of the IRRC's most recent list of tobacco-product manufacturers. The resolution should also state that the process of divestment be carried out as soon as possible, consistent with the goal of minimizing the financial effect of the divestment on the University's portfolio and, in any event, should be completed no later than one year from the approval of the resolution.

In formulating these recommendations, it was necessary for the committee to make some judgment calls regarding implementation of the divestment policy. For example, it could be argued that the divestment policy should be expanded further to apply not only to securities in tobacco-product manufacturers but also to securities in companies that own stores in which tobacco products are sold or to companies that make products, such as paper, that are used in the production of cigarettes. Similarly, it could be argued that the policy should be applied not only to tobacco-company securities owned directly by the University but also to tobacco-company securities owned derivatively through managed pooled funds, hedge funds, and the like.

In the committee's judgment, however, little if anything would be gained (in terms of symbolic value) by extending the divestment policy to such companies or to such derivative

investments. Moreover, from what we are told by the University's investment officers, expanding the divestment policy in that way would come at extraordinary administrative expense and could potentially have serious consequences for the riskiness and profitability of the endowment. Therefore, we conclude that extending the divestment policy to those situations would, on balance, do more to undermine the core missions of the University than to protect them. It is worth noting also that our judgments on these questions of implementation are, to the best of our knowledge, in accord with the judgments reached by other institutions that have decided to divest from tobacco securities.⁴¹

Our recommendations regarding divestment from tobacco-related securities assumes that a decision by the Regents to divest would be legal under applicable state and federal law. That assumption is supported by an informal, preliminary analysis of the issue provided to the committee by the General Counsel's office. It is also supported by the fact that no successful legal opposition has been raised to prevent any other educational institution that sought to divest of its tobacco securities from doing so, including Wayne State University, which divested in 1991. Nonetheless, in the interests of prudence and caution, we recommend that, before the Regents vote to adopt a resolution along the lines described above, they request, either from the General Counsel's office or from an outside law firm, a full, formal analysis of the legality question.

⁴¹ We also note that, beyond the question of whether the University should own tobacco securities, there are a number of other issues involving tobacco companies that might potentially be of relevance to the Regents, such as whether the University should accept charitable gifts from tobacco companies. Because such questions are clearly beyond the scope of this committee's charge, we offer no views as to how they should be resolved.

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