MINNESOTA BREAK THE BONDS

TWENTY YEARS OF FAILURE -- A Report on the MN State Board of Investment's Neglect of Human Rights

Issued September 11, 2013

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By investing in Israeli securities, the Minnesota State Board of Investment (SBI) has been violating its own Guidelines on International Investing. The Guidelines were drafted in the early 1990’s by a task force led by then State Auditor Mark Dayton and adopted by the SBI in response to human rights concerns raised by Minnesota’s two major labor unions. This paper exposes the inherent weaknesses in the ability of the Guidelines to achieve the objective of restricting investments in countries, like Israel, that are documented human rights violators and it reveals the SBI’s long standing failure to enforce the Guidelines which has exposed Minnesota to accusations of financial complicity in international human rights violations. It makes recommendations that, if implemented, would bring the SBI into compliance with the original intent of the Guidelines.
In 1988, as the result of SBI lobbying efforts in the Minnesota Legislature, statutory changes were made which authorized the SBI to invest in international securities. Despite this authorization, with no guidelines addressing human rights, labor rights and environmental considerations, the investment of state retirement funds outside the United States and Canada was opposed by powerful voices in the community.

At the SBI’s regular quarterly meeting on September 9, 1992, the President of the Minnesota AFL-CIO told the Board that his union’s greatest concerns “fell into the broad headings of labor rights, human rights and environmental standards.” He made pointed reference to the “abuses and atrocities that are brought to the attention from time to time by the media world-wide.” The legislative director for AFSCME Council 6 emphasized the importance of adopting investment guidelines that would address violations of human rights, labor rights and environmental standards. In response to these concerns, Board member and then State Auditor Mark Dayton moved for the formation of an International Investment Guidelines Task Force. The motion passed and the Task Force was formed.

Membership on the Task Force included representatives of each SBI Board member, the statewide retirement system, the Investment Advisory Council, organized labor and environmental groups, but it lacked the participation of an organizational or individual member with any noted human rights expertise. The inclusion of international human rights issues as an imperative in the SBI’s investment decisions, however, was not without precedent. In 1985, the SBI had adopted a divestment strategy concerning its holdings in U.S. companies doing business in apartheid South Africa. In 1988, the legislature had directed the SBI to take actions designed to encourage U.S. companies doing business in Northern Ireland to take affirmative steps to eliminate religious and ethnic discrimination. These actions served as important examples for the Task Force in the fall of 1992 when it embarked on its mission to develop human rights guidelines for the SBI.

On December 1, 1992, the Task Force submitted its recommended human rights guidelines to the SBI based on five key articles in the United Nations Universal Declaration of Human Rights:

- Freedom from political killing or disappearance;
- Freedom from torture;
- Right to a fair public trial and due process;
- Right to vote and effect governmental change; and
- Freedom from discrimination based on race, religion, sex or social status.

Applying these five key universal rights, the Task Force then summarized the human rights laws and practices of countries based on the U.S. State Department’s annual Country Reports on Human Rights, and grouped countries into three broad categories. Group I countries were rated “Acceptable” with legal protections that generally respected worker and human rights. Group II countries were rated “Questionable.” Group II countries had legal protections for worker and human rights but continuing violations of these rights had been cited by the State Department. Group III countries, the worst, were rated “Unacceptable.” Group III countries included those that lacked basic protections for worker and human rights and did not appear to be making progress in establishing an appropriate legal structure to address these issues.
The Task Force rated Israel as a “Questionable” Group II country, even though it had determined that Israel was violating all five of the key universal rights, including engaging in political assassinations and torture and violating the right to association, fair public trials, due process and freedom of speech. Israel was also violating the right to vote, the right to affect government change and the right to be free from discrimination. All of these violations were documented by the U.S. State Department, the sole source of human rights data reviewed by the Task Force. In fact, Israel was in violation of every single human rights category which should have merited a Group III rating. By comparison, the Task Force had rated Pakistan as a Group III country, yet Pakistan had fewer categorical violations than Israel. There was no explanation for awarding Israel a less onerous rating than Pakistan other than the fact that each of the rights that were being continuously violated by Israel with impunity was a protected right under Israeli law. See Task Force Report, dated December 1, 1992, from the “International Investing Guidelines Task Force” to “Members, (Minnesota) State Board of Investment,” pgs. 2, 4, 9.

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SBI Historical Background
Based on the three broad country groupings, the Task Force recommended that the SBI adopt the following investment guidelines for international investing:

- No restrictions on investing in the “markets of countries” included in “Group I – Acceptable;”
- The SBI’s active managers were permitted to invest in the “markets of countries” under “Group II, Questionable” but only if the manager believed that it would be a breach of fiduciary responsibility not to do so and notified the SBI in writing.
- The SBI’s active managers were permitted to invest in the “markets of countries” included under “Group III, Unacceptable” but only if the manager believed it would be a breach of fiduciary responsibility not to do so and appeared at a meeting of the SBI to present the reasons for the decision to invest.

At its meeting on December 9, 1992, the SBI adopted the recommendations of the Task Force. The Board directed the Task Force to review the country groupings periodically and reconvene after new annual reports from the State Department became available.

Israel has consistently been rated as a Group II country by the SBI since the guidelines were adopted in 1992. Yet, since 1993, without making the determination that it would be a breach of fiduciary duty not to invest in the Israeli market and without providing formal notice in writing to the SBI, SBI fund managers have invested millions of dollars of Minnesota’s state retirement funds in Israel Bonds.

The minutes of the December 9, 1992, SBI meeting confirm that the adopted guidelines hinged on country groupings, not definitional differences between types of securities. The SBI was concerned that violations of human rights created the potential for political, social and economic unrest adversely affecting the stability of the financial markets within the foreign countries. The relevant concern was investment in the financial markets of a foreign country with a record of human rights abuses, not the specific types of international securities that the SBI purchased.

Israel Bonds are a form of international investment sold in the Israeli market. The SBI characterizes foreign sovereign bonds, including Israel Bonds, as international securities. More recently, the SBI’s executive director issued a sworn statement that the investment guidelines were not intended to address government bonds, but, instead, were created in response to concerns that private companies doing business in countries with dismal human, labor and environmental rights records would gain a competitive edge over American businesses. Thus, he claimed, the guidelines served only to restrict investments in private securities.

The assertion that the guidelines were only intended to restrict investments in the stock of international companies is not supported by the historical record. Recalling the statement from the President of the Minnesota AFL-CIO that his “greatest concern” included “abuses and atrocities,” a key purpose in creating the guidelines was the promotion of rights guaranteed in the Universal Declaration of Human Rights. Indeed, it would be ludicrous to restrict investments in the stock of international companies doing business in countries with dismal human rights records and not restrict investments in the very governments committing the abuses and atrocities.
Despite the efforts of the 1992 Investment Guidelines Task Force to develop a manageable system designed to restrict investments in those countries engaged in human rights abuses, and despite the incorporation of the Task Force’s proposed guidelines by full Board passage as part of the body of laws and administrative rules that control the Board’s investment decisions, for more than twenty years the SBI’s administrators and managers have paid little more than lip service to these rules, prominently displaying versions of the rules in the SBI’s annual reports but otherwise essentially ignoring them. Notably, Israel has continued to be categorized as a Group II country while the SBI’s investment fund managers have continued to pour millions of dollars into the purchase of Israel Bonds.

In 2008, the SBI began to purchase private Israeli securities. The decision to begin purchasing the stock of Israeli companies was not based on any determination that Israel was no longer abusing human rights, or that Israel’s human rights abuses no longer gave Israeli companies a competitive advantage over U.S. companies. Instead, it was based on the expectation that Israel would soon be reclassified from an emerging market country to a developed country under the MSCI (Morgan Stanley Capital International) Index. MSCI thereafter added Israel to its benchmark of developed nations in May of 2010. In purchasing private Israeli securities, the SBI only instructed its fund managers not to purchase more than 10% of an account’s market value pending the MSCI reclassification decision. No instructions were given to the SBI’s fund managers that they could purchase private securities in the Israeli market only if they complied with the International Investment Guidelines for Group II countries until the Spring of 2012, after the SBI had been sued by several community groups, human rights activists and retirement fund beneficiaries for its complicity in Israel’s human rights violations by spending millions of dollars of Minnesota state retirement funds purchasing Israel Bonds.

The instructions given to the fund managers in the spring of 2012 were contained in an email, dated June 25, 2012, from the SBI’s international equities manager which characterized the guidelines as “new.” According to the SBI manager, “This new language was added to the developed markets manager’s investment guidelines because Israel, a Group II country, moved into the MSCI ex US Index. In order to satisfy the requirement of the new guideline, if your firm currently invests in or prospectively plans on investing in an Israeli security in Minnesota’s portfolio because you feel it would be a breach of fiduciary duty not to do so, please make a one-time written (and signed) notification to the SBI (addressed to me) of your firm’s intention to do so.” (Emphasis added.)

Eager to satisfy the SBI’s need to suddenly document its file, and with no apparent concern with how credible, or incredible, a statement would be that claimed that it would be a breach of fiduciary duty not to buy Israeli securities, several fund managers returned perfunctory letters to the SBI, ambiguously attesting to a required fiduciary duty to invest in the Israeli market. Thus, the SBI now holds Israeli stocks and bonds in its portfolio worth tens of millions of dollars predicated on the foolish assertion that the failure to invest in Israeli securities would violate the fiduciary duty the SBI and its fund managers owe under Minnesota law to Minnesota’s taxpayers and state retirement fund beneficiaries. By following this course of action, the SBI has actually violated its fiduciary obligations by disobeying its own international investment guidelines and soliciting false and inadequate investment justification letters from fund managers.
The intent in drafting the guidelines in 1992 which were designed, in part, to restrict the investment of Minnesota’s public funds in countries with dismal human rights records was commendable. Unfortunately, implementation and enforcement have proven to be ineffective. If the community cares any about restricting the investment of Minnesota’s state retirement funds in countries that do not adhere to key articles of the Universal Declaration of Human Rights, the guidelines must be revamped to not only ensure compliance, but to ensure greater objectivity in the country grouping process as well.

U.S. State Department reports, although a good source of some data, should not be the only source used in grouping countries based on their human rights records. As a federal agency, the State Department is restricted from making available to the public information considered to be sensitive or classified. The State Department is also subject to the pressures of domestic politics and may withhold information pending the outcome of various diplomatic initiatives. Information that is withheld or omitted may be the very type of information the SBI needs to make a sound assessment.

In addition to State Department reports, the SBI should review, at a minimum, United Nations
Heavy emphasis should be given to the reports of United Nations agencies whose purpose is to monitor human rights conditions in all countries. The United Nations Human Rights Council, a United Nations agency that did not exist until 2006, should now be the primary source of information for the SBI. Unlike State Department reports that lack significant depth and may be politically driven and less than complete, the sole purpose of the United Nations Human Rights Council is to promote and protect human rights around the globe, address human rights violations and make recommendations. The SBI should also consider the reports of credible and respected non-governmental organizations like Human Rights Watch, Amnesty International and Defence of Children International in the process of establishing its periodic country groupings.

A key mechanism of the United Nations Human Rights Council is the Universal Periodic Review (UPR) which assesses the human rights situations in all United Nations member states. The UPR is a country-driven cooperative process which provides each country the opportunity to declare what actions they have taken to improve the human rights situations in their own countries and to fulfill their human rights obligations. No other universal mechanism of this kind exists. A country’s refusal to cooperate is proof enough that the country is resistant to any change and does not appear to be making any progress that would improve the human rights condition within its borders and the territories under its control. Accordingly, the SBI’s guidelines should establish, at a minimum, that any investment of public retirement funds in the market of any country refusing to cooperate in the UPR process should automatically be considered a breach of fiduciary duty. The only UN member state that has refused to cooperate in the UPR process is Israel.

In addition to the thin source materials used by the SBI to establish its country groupings, the SBI’s actual process of grouping countries appears to be less than completely objective. There is simply no reasonable explanation for Israel’s consistent ranking by the SBI as a Group II country, instead of a Group III country, other than bias or inappropriate subjectivity. Even without reference to other sources, State Department reports alone sufficiently qualify Israel for the SBI’s Group III ranking. Despite its tone of banality, the State Department’s 2012 human rights country report for Israel is shocking:

“Human rights problems [in the occupied West Bank] related to Israeli authorities included reports of excessive use of force against civilians, including killings; abuse of Palestinian detainees, particularly during arrest and interrogation; austere and overcrowded detention facilities; improper use of security detention procedures; demolition and confiscation of Palestinian property; limitations on freedom of expression, assembly, and association; and severe restrictions on Palestinians’ internal and external freedom of movement.”

The SBI’s country review process is obviously broken if this level of human rights misconduct only merits a Group II ranking and no deeper examination. Objective human rights experts would have been alerted to major and systemic violations, including war crimes.
In continuing to grant Israel a soft Group II ranking, the SBI did not consider any human rights reports issued by the United Nations, the very organization responsible for establishing the Universal Declaration of Human Rights, the very document upon which the SBI’s human rights review process is built.

The SBI did not consider the recent United Nations report that concluded that Israel would be subject to prosecution in the International Criminal Court for its unabated and illegal settlement expansion in the Palestinian West Bank if the jurisdiction of the Court were to be invoked. In 1992, when the SBI’s guidelines were formulated, approximately 250,000 Israelis resided in illegal West Bank settlements. Over the course of the next twenty years, while the SBI continued to rank Israel in Group II, Israel’s illegal settlements grew in population to well over 600,000, displacing even more Palestinians, causing the demolition of even more Palestinian homes and farms and resulting in the mass confiscation (theft) of even more Palestinian land and resources, all of which were accomplished with brute military force.

The UN Report, issued pursuant to UN Human Rights Council Resolution 19/17, further concluded that Israel has consistently violated the Palestinians’ rights of self-determination,
freedom of movement, equality, due process and fair trial, the right not to be arbitrarily detained, and the rights to liberty and security of person, freedom of expression, freedom to access places of worship, education, water, housing, adequate standard of living, property, access to natural resources and effective recourse to lawful remedies. In short, Israel is in violation of nearly every key provision of the Universal Declaration of Human Rights.

Notably, the UN report also found that various financial operations were helping to develop, expand or maintain Israel’s illegal settlements. When this portion of the UN’s report was brought to the attention of the SBI by the Minnesota Break the Bonds Campaign earlier this year, the SBI simply ignored it. More recently, on July 16, 2013, the European Union imposed restrictive guidelines that directed its 28 member nations not to award any type of funding to any entities in any Israeli settlements in the West Bank of Palestine, including East Jerusalem. The UN Report, annual State Department reports and now the actions of the EU, however, have fallen on either deaf or less-than-objective ears at the SBI. The SBI continues to cling to its Israel Bonds knowing that approximately 10% of the millions of dollars it has paid to the Government of Israel to purchase the Bonds has been and will be used to promote and support illegal Israeli settlements.

The SBI has also purchased the stock of Israeli Banks that openly finance occupation activities. And despite the findings of a 2009 UN fact finding mission to Gaza that found that the Israeli military had committed grave breaches of the Fourth Geneva Convention by directly targeting and killing Palestinian civilians, the SBI purchased the stock of a notorious Israeli arms manufacturer responsible for providing the very drones that were part of Israel’s killing spree in Gaza, in addition to participating in the construction of the electronic surveillance system and separation barriers that encircle Palestinian communities. If the SBI had followed its own human rights guidelines, these investments could never have been made.

Among the types of human rights violations that should fall within the definition of “moral obscenity”, state victimization of children, including the torture of children, must necessarily qualify. On June 20, 2013, the United Nations Committee on the Rights of the Child issued a report that found that Palestinian children are routinely denied registration of their birth and access to health care, decent schools and clean water. “Palestinian children arrested by (Israeli) military and police are systematically subject to degrading treatment, and often to acts of torture, are interrogated in Hebrew, a language they did not understand, and sign confessions in Hebrew in order to be released,” it said in the report, which also found that children are brought in leg chains and shackles before military courts and held in solitary confinement, sometimes for months. (Emphasis added.) The UN Committee voiced deep concern at the “continuous use of Palestinian children as human shields.”

Israel’s human rights abuses are not limited to the occupied Palestinian areas. There are more than 50 Israeli laws that discriminate against Palestinian citizens of Israel in all areas of life, including the right to participate in the political process and access to land, education, state budget resources and criminal due process. A list of existing and pending discriminatory laws and bills has been compiled by a UN consultant organization, Adalah, the Legal Center for Arab Minority Rights in Israel, which can be found on the Adalah website at http://adalah.org/eng/Israeli-Discriminatory-Law-Database. One such bill, the Prawer-Begin Plan, currently pending final approval in the Israeli Knesset, calls for the forced displacement of up to 40,000 Bedouins from their ancestral homes in the Negev. On July 25, 2013, the UN High Commissioner for Human Rights charged that the Israeli government “continues to actively pursue a discriminatory policy of forced displacement against its own Arab citizens.”

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SBI Human Rights Guidelines are Ineffective
“I do not regard a broker as a member of the human race.” ---Honore de Balzac

As well-intended as the SBI’s investment executives and managers may be, it is unfair to ask financial analysts to make critical and objective international human rights determinations and to do so based on imperfect sources of data. This is the system that currently exists and for twenty years it has failed. Israel is the example.

At a minimum, changes are required to reverse the appearance of financial complicity in Israel’s human rights violations. The United States Government, for several years now, has stopped giving direct foreign aid to the Government of Israel in the form of cash or loan guarantees to avoid any possible involvement in Israel’s illegal settlement activities. Yet, Minnesota continues to directly support Israel’s illegal settlement activities by purchasing Israel Bonds. The very act of purchasing Israel Bonds is a defiant statement of solidarity and bias in support of Israel’s government which should disqualify the SBI from comparatively ranking Israel’s human rights record. The SBI clearly lacks the objectivity or political will necessary to more accurately rank Israel as a Group III country.

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Conclusion
The SBI’s efforts to document its files after the fact with contrived and thoroughly insupportable fiduciary obligation letters to support its investments in the Israeli market is unacceptable for a state agency entrusted to manage public funds.

Israel’s consistently soft ranking by the SBI as a Group II country despite continuing and worsening violations of nearly every right guaranteed by the Universal Declaration of Human Rights shows that the SBI’s International Investment Guidelines are not working.

We recommend the following:

a) The SBI should adopt a rule that states that no funds under SBI control can be invested in the market of any country that refuses to cooperate in the UN’s Universal Periodic Review Process and any such investment would be a breach of fiduciary duty;

b) The SBI should base its country group rankings on a review of the most credible sources of international human rights data in the following order: reports and resolutions issued by the UN and the UN Human Rights Council, reports issued by the United States Department of State, reports issued by the most respected and recognized international human rights organizations (e.g., Amnesty International, Human Rights Watch and Defence of Children International), and, finally, reports issued by non-governmental human rights organizations operating in the country (e.g., Adalah);

c) The SBI should re-evaluate its country group rankings no later than every two years, it should submit proposed country group rankings for public comment and it should consider all timely submitted public comments in response to its proposed rankings;

d) The SBI should appoint a blue ribbon panel of international human rights experts representing diverse political, religious and ethnic backgrounds to review and propose country group rankings;

e) The SBI should clarify that the international investing guidelines apply to all securities;

f) To invest in the market or securities of any Group II or III countries, the SBI should require the following sworn written statement from the fund manager: “I declare under penalty of perjury under the laws of the United States that I believe that it would be a breach of fiduciary responsibility not to invest in the securities of companies domiciled in [country shown under Group II or III] and in the bonds issued by that country, including the debt obligations of any of its agencies and political subdivisions.”

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Conclusion
The Minnesota Break the Bonds Campaign is recognized by the Internal Revenue Service as a 501(c)(3) non-profit organization. Donations are tax-deductible to the fullest extent allowed by law.