



July 30, 2020

Office of Regulations and Interpretations US Department of Labor
Room N-5655
200 Constitution Avenue NW Washington, DC 20210

RE: Proposed rule on Financial Factors in Selecting Plan Investments (RIN 1210-AB95)

To whom it may concern:

Introduction

We are writing in response to the Department of Labor’s proposed rule, “Financial Factors in Selecting Plan Investments” (RIN 1210-AB95) (the “Proposal”).

JUST Capital is a nonprofit with a mission to build an economy that works for all Americans by helping companies improve how they serve all their stakeholders – workers, customers, communities, the environment, and shareholders. Uniquely, JUST Capital engages the American public to determine what matters most to them when it comes to just business behavior. We then define metrics that map to those issues and track and analyze the companies in the Russell 1000. The analysis helps companies benchmark and improve stakeholder performance, and incentivizes a “race to the top” through our high-profile Rankings with Forbes, as well as investment products like Goldman Sachs’ JUST ETF, which tracks our JUST U.S. Large Cap Diversified Index (JULCD), and has \$137 million AUM.

The Department makes claims about the growth and role of “ESG” investing and its appropriateness in the context of ERISA plans, and then proposes to put ERISA sponsors in the fiduciary box with a rigid understanding of the relationship between “financial” and “nonpecuniary” factors. We respectfully request that the Proposal be withdrawn.

Thoughtful long-term allocators of capital are committed to considering the corporation’s role in meeting its obligations to other stakeholders, such as the Business Roundtable’s statement of August 2019, [1] and moving beyond Milton Friedman’s iron-clad view that shareholders are the *only* stakeholder that deserves consideration, which the proposed rule the Department seeks to codify. Over the past six years, we have also surveyed over 100,000 Americans on this matter, and there is overwhelming and widespread support for stakeholder and ESG considerations in business and financial decision making.

We believe the proposed rule will ultimately result in *lower* risk-adjusted returns for ERISA plan holders, the same American people the rule is intended to protect. Research supports that long-term, risk-adjusted shareholder value is maximized when companies have good governance and managerial leadership aligned around maintaining a productive,





safe workforce to serve customer needs in the context of the health of the social and physical environment in which they operate.

What is “ESG”?

The Department states, “There is no consensus about what constitutes a genuine ESG investment, and ESG rating systems are often vague and inconsistent, despite featuring prominently in marketing efforts.” We submit that the investment community is coalescing around a definition of “ESG” that means, broadly, analyzing a company’s environmental, social, and governance characteristics, and incorporating those externalities into company valuations as part of a broadly diversified investment portfolio.

Ever since Graham and Dodd defined the field with their seminal Security Analysis text, financial analysts have gone beyond a company’s financial statements, which can only ever be backwards-looking, to investigating the company’s product offerings, its managerial quality, its social and economic environment, its relationships with suppliers and workers, and a host of other potential cues about its likely future prospects. Additionally, as companies have shifted from fixed to intangible assets, understanding how businesses are managing their human capital and market relationships with customers and suppliers takes on even more salience, and traditional accounting has failed to keep up with this shift [2]. Taking this additional information into account gives analysts the capacity to build that forward-looking view.

And financial analysts since Graham and Dodd have been estimating – and disagreeing about – company valuations ever since. Those disagreements are what “make the market” as new information is impounded into security prices.

Thus, “ESG” is part of traditional company valuation analysis and has been for decades. These considerations have been with us since the dawn of modern financial analysis, and in this regard deserve no special consideration from the Department.

Financial vs Nonpecuniary

We also acknowledge the Department’s interest in preserving the fiduciary duty of sponsors to provide plan participants with “*financial*, rather than ‘nonpecuniary’ benefits.” In this regard, the evidence [3] is mounting that companies that perform better on management of “ESG” issues certainly do not underperform their peers, and may even outperform them [4].

Our extensive public polling has identified with great specificity what the American public thinks the priorities of U.S. companies ought to be [5]. We find that since we began this work, the companies that are most aligned with the priorities of the American people actually outperform the broader market [6].

Our experience is not unique. The evidence from years of experience [7] suggests that investors in equity investment funds with “ESG” or “sustainable” goals do not need to sacrifice risk-adjusted returns. The notion that investors cannot maintain financial prudence while considering non-financial measures of performance is simply a false choice.





QDIAs

Given the evidence that “ESG” funds offer risk-adjusted performance in line with their peers, we believe they pass the “all things being equal” test and are entirely consistent with fiduciary duty as part of a well-diversified QDIA offering. As with consideration of any investment in this context, care must be given to the quality of the investment manager, the fund’s stated investment strategy and holdings, their investment process, and expected returns net of fees.

The Will of the People

The American people are the ultimate beneficiaries of American companies, through their ownership in ERISA-sponsored plans, other retirement plans and ownership vehicles, and the final taxation and regulatory power of the U.S. Government. Americans can express their will as voters, but their capacity to effect change at corporations, even as the beneficial owners in an ERISA-sponsored plan, is limited given the proxy voting process.

Our polling tells us what the American people want from corporations: They want them to build loyal, stable, continually-learning workforces and pay them fairly; establish good relationships with the communities where they operate; provide safe, honest products and services to their customers, and leave the physical environment in which they operate in the same condition or better for their being in it.

Conclusion

Denying ERISA plan participants access to investment vehicles that incorporate “ESG” considerations would be closing off access to important non-financial information that affects company, and investment, valuations. It could leave sophisticated investors the fruits of deeper analysis, while relegating ERISA participants to the crumbs of underperformance. The evidence is strong and growing that “ESG” considerations are critical factors in evaluating long-term company performance and future prospects. Incorporating those and all relevant factors in a thoughtful valuation process is the core of achieving superior risk-adjusted returns, and fiduciary duty demands that we deliver the highest available risk-adjusted returns to the American people in their ERISA-sponsored plans.

Thank you for considering these comments.

Sincerely,

Michael Kinstlick, CFA

Director, Indexes and Analytics, JUST Capital



Citations

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2. Lev, Baruch and Feng Gu. *The End of Accounting and the Path Forward for Investors and Managers*. Wiley, 2016.
3. Eccles, Robert G., Ioannis Ioannou and George Serafeim. “The Impact of Corporate Sustainability on Organizational Processes and Performance.” *Management Science*, vol. 60, issue 11, 2014, pp. 2835-2857.
4. Henisz, Witold, Tim Koller and Robin Nuttall. “Five ways that ESG creates value.” *McKinsey Quarterly*.
<https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/five-ways-that-esg-creates-value>
5. “Polling.” *JUST Capital*. <https://justcapital.com/polling/>
6. “JUST U.S. Large Cap Diversified Index (JULCD) Q2 2020.” *JUST Capital*.
<https://justcapital.com/wp-content/uploads/2020/07/JULCD-Q2-2020.pdf>
7. Khan, Mozaffar, George Serafeim and Aaron Yoon. “Corporate Sustainability: First Evidence on Materiality.” *The Accounting Review*, vol. 91, no. 6, 2016, pp. 1697-1724.