



Insured Retirement Institute
1100 Vermont Avenue, NW | 10th Floor
Washington, DC 20005

t | 202.469.3000
f | 202.469.3030

www.IRIONline.org
www.myIRIONline.org

Submitted via Federal eRulemaking Portal: www.regulations.gov

July 30, 2020

Office of Regulations and Interpretations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, NW, Room N-5655
Washington, DC 20210

Re: Financial Factors in Selecting Plan Investments Proposed Regulation - RIN 1210-AB95

To Whom it May Concern:

On behalf of our members, the Insured Retirement Institute (“IRI”)¹ appreciates the opportunity to provide these comments to the Department of Labor (the “Department”) in response to its proposed rule, Financial Factors in Selecting Plan Investments (the “ESG Proposal”).² The ESG Proposal would amend the “Investment Duties” regulation under Title I of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) to expressly require that plan fiduciaries select investments and investment courses of action based solely on financial considerations relevant to the risk-adjusted economic value of a particular investment or investment course of action. For the reasons set forth below, IRI and our members respectfully urge the Department to withdraw the Proposal.

On July 20, 2020, IRI submitted a comment letter³, along with the American Bankers Association (“ABA”), the Defined Contribution Institutional Investment Association (“DCIIA”), the Investment Adviser Association (“IAA”), the Investment Company Institute (“ICI”), the Securities Industry and Financial

¹ IRI is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, and distributors such as broker-dealers, banks, and marketing organizations. IRI members account for 90 percent of annuity assets in the U.S., include the top 10 distributors of annuities ranked by assets under management, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community.

² 85 FR 39113 (June 30, 2020).

³ Letter to Department Requesting Extension of Time to Comment on ESG Proposal, Dated July 20, 2020 (available at <https://www.ici.org/pdf/32628a.pdf>).

Markets Association (“SIFMA”), and the SPARK Institute. This letter requested an extension of the deadline for public comments on the ESG Proposal, currently scheduled to end on July 30, 2020⁴. Many IRI members are also members of these financial services trade associations. We understand that these organizations are or will also be submitting comment letters to the Department in response to the ESG Proposal, and we generally support the views and positions being expressed in those letters.

The ESG Proposal sets aside pension plan investments selected because of the non-pecuniary benefits they may further, such as those relating to environmental, social, and corporate governance (“ESG”) considerations. While the terminology used to describe ESG-related investment activities is evolving, the ESG considerations taken into account today are sophisticated, data-driven, and seek to further competitive risk-adjusted returns.

We believe the Department should maintain its long-standing principles-based approach to investment selection by ERISA fiduciaries. Singling out the ESG investment category for unique treatment and scrutiny is inconsistent with well-established, principles-based ERISA regulations. Further, the ESG Proposal will trigger unintended consequences, expose plan fiduciaries to additional regulatory scrutiny, and heighten litigation risks related to the selection of all plan investment options. We oppose a heightened regulatory standard for any specific investment category, as the Department’s principles-based standards for ERISA fiduciaries and plan sponsors effectively protects plan participants from financial risk.

In addition, the ESG Proposal should be consistent with the Department’s recently issued, Information Letter⁵ on private equity investments, which affirmed the Department’s position that plan fiduciaries should follow a principles-based approach when selecting investment options to include in their plans.

We strongly urge the Department to withdraw this ESG Proposal based on fundamental principles of prudent and responsible investment selection, rooted in both ERISA regulations and existing Department standards for plan fiduciaries, as well as the concerns we have about how the Department views ESG investments. The Department’s ESG Proposal would amend the regulations under ERISA Section 404(a), which lays out what an ERISA fiduciary must do to meet the prudent person standard of care imposed by ERISA Section 404(a)(1)(B).

The Department’s requirement that a fiduciary consider only pecuniary and objective risk-return criteria, while ignoring other factors that could be meaningful to a prudent and thorough analysis of an investment, is inconsistent with ERISA’s prudent man requirement: “a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims.” Although objective risk and return factors are the primary considerations in any fiduciary’s evaluation of investment alternatives, it is common for fiduciaries to consider other factors such as operational factors impacting administration of the plan or fees borne by participants, a firm’s reputation, or the tenure of an investment manager and team. The ESG Proposal would add new

⁵ DOL Information Letter 06-03-2020; *see also* President Trump’s Executive Order to reduce regulatory impediments to financial institutions, *Regulatory Relief to Support Economic Recovery*, Executive Order 13924.

conditions that an ERISA fiduciary would be required to satisfy to meet its duty of loyalty under ERISA Section 404(a)(1).

The ESG Proposal stands to disrupt, if not prohibit, many established investments and investment courses of action routinely selected by plan fiduciaries for inclusion in their plans. ERISA Section 404 imposes general duties on all fiduciaries with regard to every decision they make, and the statutory and class exemptions provided under ERISA Section 408 do not provide any relief from the requirements of ERISA Section 404.

IRI and its members respectfully offer the following comments to identify the potential impacts of the ESG Proposal on investment selection, successful plan financial performance, heightened risks of regulatory burdens, and inconsistencies with the Department's long-standing principle-based rules.

I. The ESG Proposal Would Adversely Impact 3(21) and 3(38) Fiduciary Services Utilized by Many Plan Sponsors.

We interpret the ESG Proposal to apply to 3(21) and 3(38) ERISA investment plan fiduciaries. As the ESG Proposal includes no clear definition of what an ESG fund is, what "other similarly-oriented considerations" is, and what represents "pecuniary factors," this raises several questions of compliance with the ESG Proposal for advisors and investment managers. For example, what if a 3(21) advisor incorrectly identifies something? How much additional analysis and research will be required to ensure any ESG consideration is uncovered? How will these additional burdens impact the fees paid by plans to 3(21) advisors and 3(38) fiduciary investment management service providers? No 3(21) advisor currently possesses the documentation capabilities necessary to justify selection of an ESG investment versus a non-ESG investment, as required by the ESG Proposal.

II. The ESG Proposal Would Increase the Burdens on Plan Sponsors to Select Investment Options to Use as QDIAs.

The ESG Proposal would not allow ESG funds to be used as Qualified Default Investment Alternatives ("QDIAs") in defined contribution plans. This presents a significant concern about how this would impact managed accounts included in plans as a QDIA. The ESG Proposal would effectively require plan fiduciaries to determine whether a particular investment would be classified as an ESG investment that would be ineligible for QDIA treatment (*e.g.*, would any fund where the investment manager incorporates ESG considerations into the selection of underlying investments be ineligible for QDIA treatment, or would this apply only to ESG-labeled funds?). However, the ESG Proposal provides no clarity or guidance to help plan fiduciaries determine whether a particular investment would run afoul of this requirement and fails to consider and account for the compliance burdens it places on plan fiduciaries to make such determinations. Moreover, we believe changes to the criteria for the selection of QDIAs should only be considered by the Department through proposed amendments to the QDIA regulation itself; doing so indirectly through amendments to Rule 404a-1 is inappropriate and incompatible with sound administrative procedure.

This proposed change to the rules for QDIAs is exacerbated by the lack of a clear definition of what constitutes an ESG investment option or investment course of action. To the extent the Department

prudently withdraws the ESG Proposal and seeks further stakeholder input, we expect this definitional topic to be thoroughly discussed in future public comments given the extensive fiduciary breach implications of this proposed QDIA requirement.

III. The ESG Proposal Would Impair Participants' Access to Insurance Company General Account Products that Provide Valuable Guarantees to Help Participants Manage Risk.

Per the ESG Proposal, the expectation is that plan fiduciaries will look to fund providers/managers to determine ESG investing components (see complications above about definitions). This would apply to mutual funds, Collective Investment Trusts (“CITs”), and insurance companies' separate and general accounts. A fund house is a company that invests the pooled money of investors to buy financial securities like stocks, mutual funds, equities, etc. These fund houses have fund managers who decide where and how to invest money. A question arises as to whether fund houses would need to create ERISA-specific funds versus non-ERISA-specific funds to avoid any legal missteps in financial regulations.

Additionally, we are specifically concerned about the implications of the ESG Proposal with respect to insurance company general account products. Many plan sponsors offer these products to provide participants with a stable value or fixed annuity plan investment option. These products typically provide interest rate guarantees backed by insurance company general assets. Often, insurance companies will credit interest in excess of the guaranteed minimum interest rate, and insurance companies invest general account assets to back these credited interest rates. These general account assets are invested for the benefit of the insurance company and all policyholders, including ERISA plan sponsor participants, and some insurance companies may use ESG principles in their general account investment strategies.

Based on the ESG Proposal, plan sponsors may be required to conduct a thorough evaluation of all plan investments and specifically make key decisions around ESG investments. How would a plan fiduciary evaluate these products? If a plan fiduciary determines the insurance company investment strategies have ESG components, and the plan fiduciary, using the tenets of the ESG Proposal, cannot justify inclusion relative to other short-term investments like money market funds and collective investment trusts, plan sponsors may be forced to remove these products from investment lineups. This would deprive millions of participants of guaranteed investment vehicles.

IV. The ESG Proposal Would Significantly Increase the Complexity Inherent in Building and Maintaining Investment Fund Lineups.

There are many moving parts to the retirement plan, including enrollment, plan education efforts, building the investment fund lineup, staying compliant with ERISA and applicable DOL rules and guidance, and making distributions. Particularly, building an ideal investment fund lineup is a multi-stage process, and for many plan sponsors, includes selecting the investments to be offered in a plan. Under the ESG Proposal, the expectation is that plan fiduciaries (and platform providers) will have to evaluate fund lineups, seek to identify ESG funds, and in many instances remove those funds from the plan. Given the breadth of the ESG Proposal's impact resulting from ambiguous and imprecise references to ESG, “ESG consideration”, and “other similarly oriented considerations,” this would entail a massive

undertaking as a majority of fund managers routinely consider at least some level of ESG factors in their investment processes. From a practical perspective, fund managers and recordkeepers may not even be able to facilitate the dramatic changes required to comply with the ESG Proposal.

The ESG Proposal also raises an important macro-economic question: what would be the aggregate economic impact if a significant number of ERISA plan fiduciaries generally decide potential ESG funds/strategies should be removed from plan lineups in a relatively short period of time? Could such a shift in money management affect the markets and economy, and if so, should the federal government pursue regulatory changes that would drive such a shift, particularly during a recession??

V. The ESG Proposal Fails to Adequately Consider the Burdens it Would Place on Plan Sponsors to Review and Amend Their Investment Policy Statements.

The ESG Proposal essentially requires every ERISA plan sponsor to immediately identify and assess investment policy statements (“IPS”) to determine whether:

1. The IPS wording could be construed to explicitly allow for ESG funds;
2. The IPS wording implies that non-pecuniary factors, ESG or otherwise, could possibly be considered in any way;
3. All “appropriate considerations” are explicitly accounted for in the IPS.

Questions arise under the ESG Proposal as to the burdens such regulatory requirements place on ERISA plan fiduciaries, including the amount of time and cost to perform the required identifications and assessments of the IPS for retirement plans. IRI looks forward to contributing to that conversation.

VI. The Department’s Cost-Benefit Analysis Omits the Vast Majority of Costs That the ESG Proposal Will Impose on Plans, Plan Fiduciaries and Other Affected Parties.

With limited exception, the Department’s cost-benefit analysis concludes that the ESG Proposal will impose virtually no costs on the thousands of fiduciary service and investment product providers to the over 700,000 ERISA-governed defined benefit and defined contribution plans that the ESG Proposal may affect.⁶ Retirement providers will expend time and incur varying legal and other costs in connection with the ESG Proposal. This will include time and expenses to, among other things, (i) read the ESG Proposal, (ii) understand its potential interpretations and determine how those interpretations may affect their particular plans or businesses (which may include multiple products within multiple business lines), (iii) review their investment policies, strategies, procedures, management agreements, marketing materials and related documentation in light of the ESG Proposal, (iv) make any necessary changes, and (v) provide notice of such changes to plan clients. Absent ongoing compliance costs, the amount of time and money necessary for fiduciary service providers and others to undertake the relevant foregoing tasks will be significant. Indeed, if one were to assume for the sake of argument that only half of the

⁶ The Department states that the sole cost of the rule will be 600 hours of total time (or \$56,818) annually for defined benefit and defined contribution plans with ESG investments that are not participant directed to maintain new documentation. “Information about Registered Investment Advisers and Exempt Reporting Advisers: July 2006 – July 2020”, available at <https://www.sec.gov/help/foiadocsinvafoiahtm.html>.

roughly 13,000⁷ registered investment advisers provide services and products to ERISA-governed plans and each spends only a modest \$10,000 in legal and other costs in addressing the ESG Proposal, that would add \$65,000,000 to the rule's costs just for registered advisers.

We emphasize that the costs discussed above are merely for providers. Plan sponsors will have to conduct the exact same analysis. However, the impact could be far greater. Not only could plan sponsors incur similar legal costs to those described above, but they would incur costs of hiring investment professionals to conduct a thorough analysis of all plan investments, making proper documentation, and potentially making lineup changes. The aggregate legal and investment professional costs could be very consequential.

Given that many ERISA plans are sponsored by small employers, these additional costs could be a significant deterrent to sponsoring a plan at all. IRI has long supported policies which promote the expansion of coverage to the tens of millions of Americans who do not have access to a retirement plan at work, leaving many ill-prepared to meet their financial needs during their retirement years. Currently, this gap is most acute among employees of small businesses, because small business owners are often reluctant to take on the complex legal, financial, and administrative risks and challenges inherent in sponsoring their own retirement savings plans. As a result, IRI does not support placing any additional regulatory burdens on small business owners which can pose significant additional risks and challenges for them and serve as further reasons to discourage rather than encourage the expansion of retirement plan coverage for their workers

VII. Conclusion

Taking into consideration the foregoing illustrative impacts on existing retirement plans and investment activities, coupled with the existing foundation of the Department's and ERISA's principles-based approach to investment selection, we urge the Department to reconsider moving forward with this proposed ESG Proposal. IRI and its members strongly and respectfully implore the Department to withdraw this ESG Proposal on the basis of existing, effective regulations for plan fiduciaries and investment managers, the unnecessary and excessive regulatory burdens the proposed rule would place on retirement plans and market activity, heightened liabilities, and barriers to a broader expanse of investment categories and options.

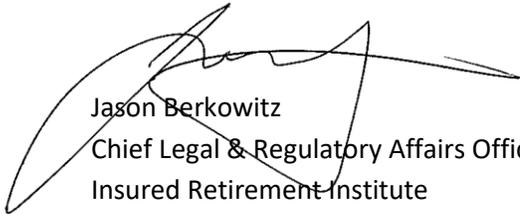
* * * * *

Thank you again for the opportunity to provide these comments. If you have questions about our recommendation that the Department withdraw the ESG Proposal, or if we can be of any further

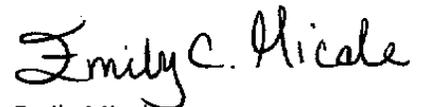
⁷ Plans will bear even greater costs. If one were to assume for the sake of argument that each ERISA plan spends an average of only \$1,000 in legal fees or other costs just to determine whether and how the rule affects it, the initial cost to all plans would total over \$700 million. Ongoing compliance costs in monitoring existing investments or options and selecting new investments or options would be additional. *See, e.g., Business Roundtable v Securities and Exchange Commission*, 647 F.3d 1144 (DC Cir 2011) (striking down SEC's proxy access rule due to defective cost-benefit analysis; *Corrosion Proof Fittings v Environmental Protection Agency*, 947 F.2d 1201 (5th Cir 1991) (striking down EPA regulation of asbestos products for defective cost-benefit analysis).

assistance in connection with this important regulatory effort, please feel free to contact the undersigned at jberkowitz@irionline.org or emical@irionline.org.

Sincerely,



Jason Berkowitz
Chief Legal & Regulatory Affairs Officer
Insured Retirement Institute



Emily Mical
Emily Mical
Director, Federal Regulatory Affairs
Insured Retirement Institute