



LongView
ASSET MANAGEMENT

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

July 30, 2020

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

Dear Director Canary:

LongView Asset Management, LLC, appreciates the opportunity to submit comments on the Department of Labor's ("Department") notice of proposed rulemaking ("Proposal") regarding financial factors used to select plan investments by Employee Retirement Income Security Act ("ERISA") fiduciaries.

LongView Asset Management, LLC, ("LongView") is an independent investment advisor based in Santa Fe, New Mexico. We provide financial planning and wealth management services for individuals and charitable organizations, as well as retirement plan solutions for small institutions. As of June 30, 2020, LongView had \$161,045,049 in total assets under management

Executive Summary

Let us be very clear—LongView strongly supports the Department's legal view that fiduciaries may not subordinate the economic interests of participants to collateral goals. We agree that ERISA's fiduciary requirements put the economic ("pecuniary") interests of the participants first, and that fiduciaries cannot sacrifice returns or increase risks to pursue non-economic ("non-pecuniary") interests. As a result, we agree that some investment products and strategies simply are not prudent for ERISA plans.

Nevertheless, we believe that integrating environmental, social, and governance ("ESG") factors into investment activities is essential to fulfilling fiduciary obligations to engage in appropriate risk management, and the Proposal fundamentally misconstrues the importance and role of ESG integration in reducing risk and increasing returns. Further, the Proposal is likely to lead to confusion and costs for retirement plan fiduciaries.

Despite the Proposal's stated goal of providing clarity for ERISA fiduciaries, it instead creates confusion due in part to a failure to distinguish ESG integration and Economically Targeted Investing (ETI). ESG integration is the consideration of risk factors as part of prudent fiduciary management and a strategy that takes these factors into account in investment actions. ETIs are investments that aim to provide financial returns as well as collateral, non-financial benefits. For example, ETIs often advertise job creation as a goal of the investment.ⁱ

For all of these reasons, we urge the Department to retain existing guidance and not move forward with a final rule. If the Department does choose to proceed with a final rulemaking, we urge the Department to eliminate the prohibition on ESG factors in QDIAs. The Department should be concerned with whether a factor is pecuniary, not whether it is related to ESG. This would serve the Department’s primary objective—preventing fiduciaries from using plan investments for their own collateral goals—without putting ESG factors in regulatory stasis, preventing participants from benefiting from innovative uses or changes necessitated by different market conditions.

ESG Integration

The Proposal states that ERISA fiduciaries have fulfilled their obligations if they have “selected investments and/or investment courses of action based solely on pecuniary factors” and that “ESG factors and other similar factors may be economic considerations.” In fact, there is now an extensive body of research that makes clear that ESG factors are material investment considerations.ⁱⁱ As such there exists a sound basis for integrating ESG factors into investment actions.

A policy by the Department that simply clarifies that fiduciaries must integrate material factors into their investment actions, and that ESG factors may be material, would be appropriate. We are concerned, however, that the remaining components of the proposal create confusion and are likely to cause fiduciaries to believe they are not permitted to consider material ESG factors in their investment analysis.

The “all else being equal test”

We are highly concerned that the Proposal inappropriately creates new burdens for fiduciaries under the “all else being equal test” that will lead to unnecessary costs for plan participants. It also creates confusion about what activities the Department is attempting to regulate.

Currently, under the “all else being equal test,” which has been in place since 1994, fiduciaries may select an investment that provides collateral benefits only after they have determined that the risk and return profile of that investment option is substantially similar to that of competing options that would meet the financial needs of the fund.

The Proposal proposes the retention of the “all things being equal” test but adds new and costly record keeping requirements for fiduciaries to document their conclusion that multiple options are equal and that it is, therefore, appropriate to make a decision based on collateral benefits. Below is a chart detailing three examples of traditional ETFs and their ESG counterparts. Highlights below indicate outperformance. As shown, funds that integrate ESG factors into their plans largely outperform their traditional counterparts, indicating that ESG factors can indeed be a material rather than non-pecuniary factor.

| Shareclass overview | SPDR® S&P 500 Fossil Fuel Rsrv Free ETF SPYX Profile | SPDR® S&P 500 ETF Trust SPY Profile | SPDR® MSCI Em Mkts Fossil Fuel Free ETF EEMX Profile | iShares MSCI Emerging Markets ETF EEM Profile | iShares MSCI ACWI Low Carbon Target ETF CRBN Profile | iShares MSCI ACWI ETF ACWI Profile |
|----------------------------------|---|--|---|--|---|---|
| Shareclass ticker | SPYX | SPY | EEMX | EEM | CRBN | ACWI |
| Sustainability mandate | ✓ | ✗ | ✓ | ✗ | ✓ | ✗ |
| Performance as of date | 4/29/20 | 4/29/20 | 4/29/20 | 4/29/20 | 4/29/20 | 4/29/20 |
| Annualized returns 1 month | +12.44 | +12.80 | +8.38 | +8.48 | +10.66 | +10.63 |
| Annualized returns 3 months | -8.83 | -9.16 | -10.90 | -13.10 | -11.89 | -12.02 |
| Annualized returns 6 months | -2.51 | -3.09 | -8.79 | -11.25 | -7.34 | -7.78 |
| Annualized returns 1 year | +1.99 | +0.87 | -10.73 | -12.98 | -3.93 | -5.03 |
| Annualized returns 3 years | +9.54 | +8.97 | +0.53 | -0.21 | +4.69 | +4.69 |
| Annualized returns year-to-date | -8.61 | -9.2 | -14.99 | -17.21 | -12.69 | -13.02 |
| Morningstar suggested benchmark | S&P 500 TR USD | S&P 500 TR USD | MSCI ACWI Ex USA NR USD | MSCI ACWI Ex USA NR USD | MSCI ACWI Ex USA NR USD | MSCI ACWI Ex USA NR USD |
| iShares index ETF benchmark | IVV - iShares Core S&P 500 ETF | IVV - iShares Core S&P 500 ETF | ACWX – iShares MSCI ACWI ex U.S. ETF | ACWX – iShares MSCI ACWI ex U.S. ETF | ACWX – iShares MSCI ACWI ex U.S. ETF | ACWX – iShares MSCI ACWI ex U.S. ETF |
| +/- compared to benchmark 1 year | +1.16 | +0.03 | +1.33 | -0.92 | +8.13 | +7.03 |
| +/- compared to benchmark 3 year | +0.53 | -0.03 | +0.99 | +0.25 | +5.15 | +5.14 |

Out of the 24 instances of comparison between traditional ETFs and their fossil-free ESG counterparts, ESG ETFs outperformed traditional ETFs 21 out of 24 times, or 88% of the time in the examples above. Not only do the ESG funds outperform their counterparts, they foster societal benefits, creating a win-win scenario for investors who are interested in investing their values with ESG.

The Proposal's discussion of the "all things being equal test" is cause for confusion because, while the test was originally developed to guide the consideration of ETIs, and the discussion in the Proposal appears to envision the selection of an ETI investment, the language of the Proposal does not distinguish the application of this test from the broader discussion of ESG integration, inappropriately suggesting that the documentation requirement is necessary whenever ESG factors are considered.

Defined contribution plan investment options

The Proposal states that ERISA fiduciaries may select "ESG-themed funds" as an investment option for a participant-directed plan but that an "ESG-themed fund" cannot be selected as the default investment option. This determination appears to be based on confusion between ESG integration and ETIs. In our view, all investment options should be required to integrate ESG factors as part of prudent investment decision-making. In addition, it may be appropriate for ERISA fiduciaries to offer ETIs as options that participants may select in participant-directed plans. ESG issues can have a material impact on the financial performance of securities as well as sustainability of the markets for future investors. In 2015 the Supreme Court confirmed that "a trustee has a continuing duty—separate and apart from the duty to exercise prudence in selecting investments at the outset—to monitor, and remove imprudent, trust investments."ⁱⁱⁱ Fund investors can create market volatility and undermine sustainable wealth creation when they fail to account for material ESG factors, undermining the interests of future beneficiaries.

The Department's stated rationale for prohibiting an "ESG-themed fund" from being selected as the default investment option is that it is not appropriate to select "investment funds whose objectives include non-pecuniary goals." This statement shows a fundamental misunderstanding of the purpose of ESG integration, which is to integrate all material factors into investment decision-making. In addition, it is likely to cause confusion for fiduciaries as they attempt to rationalize the Department's statements in the Proposal that ESG factors are likely to have a material economic impact with the discussion of ESG factors in this context, in which the Department has deemed them "non-pecuniary."

Conclusion

LongView agrees that ERISA imposes fiduciary obligations of prudence and loyalty on fiduciaries that prevent them from subordinating the economic interests of participants to collateral goals. In this fiduciary role, we believe that ESG factors may be financially material, and integrating ESG factors is core to investment decision-making.

The Proposal mischaracterizes ESG integration and fails to distinguish between ESG integration and economically targeted investing. This is likely to lead to confusion for ERISA fiduciaries and costs to plan savers. If the Proposal is finalized in its current form, we are concerned that fiduciaries will struggle to fulfill their obligations to integrate all financially material risk factors while also trying to respond to the language in the Proposal that appears to be aimed at preventing fiduciaries from taking account of these same risks.

The Proposal should be modified in any final rule to treat pecuniary ESG factors as any other pecuniary factor, removing any additional requirements, and making investments utilizing such ESG factors eligible for use in QDIAs.

We thank you for everything you do to protect American workers.

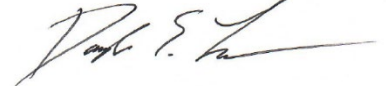
Sincerely,



David Cantor



Harlan Flint



Douglas Lynam

ⁱ For further discussion of ESG integration as an investment strategy, see Gary, S. *Best Interests in the Long-Term: Fiduciary Duties and ESG Integration*, 90 U. Colo. L. Rev. 733, 745 (2019).

ⁱⁱ See, e.g., Amato, J.V., and Dyott, I.S., *ESG Investing: An Active Approach to Long-Term Value Creation*, Neuberger Berman (2019), www.nb.com/documents/public/global/t0349_0119_wp_esg_investing_an_active_approach.pdf; Ballentine, C., *ESG Stock Resilience Is Paving the Way for a Surge in Popularity*, Bloomberg (31 Mar. 2020), www.bloomberg.com/news/articles/2020-03-31/esg-stock-resilience-is-paving-the-way-for-a-surge-in-popularity; Hale, J. *Sustainable Funds Weather the First Quarter Better Than Conventional Funds*, Morningstar (3 Apr. 2020), www.morningstar.com/articles/976361/sustainable-funds-weather-the-first-quarter-better-than-conventional-funds; Konqui, M.H, et al. *Why Using ESG Helps You Build Better Portfolios*, Lyxor Asset Management (July 2019), www.lyxor.com/why-using-esg-helps-you-build-better; Logan, L., *Commentary: Active Beats Passive in Promoting Sustainable Development*, Pension & Investments (23 Apr. 2020), www.pionline.com/industry-voices/commentary-active-beats-passive-promoting-sustainable-development; Wurtz, F., *ETFs for ESG: Why Passive Makes Sense for ESG*, IPE (2019), www.ipe.com/etfs-for-esg-why-passive-makes-sense-for-esg/10033627.article. See also Gary, S., *supra*, 90 U. Colo. L. Rev. 733 (2019).

ⁱⁱⁱ *Tibble v. Edison International*, 135 S. Ct. 1823, 1828-29 (2015).