

July 30, 2020

Jeanne Klinefelter Wilson  
Acting Assistant Secretary  
Employee Benefits Security Administration  
U.S. Department of Labor  
200 Constitution Ave., NW  
Washington, DC 20210  
Via [www.regulations.gov](http://www.regulations.gov)

***RE: Comments in Response to Proposed Rule on Financial Factors in Selecting Plan Investments (RIN 1210-AB95)***

Dear Acting Assistant Secretary Wilson:

We write to oppose the approach set out in the Department of Labor’s (DOL) proposed rule *Financial Factors in Selecting Plan Investments* (“the Proposed Rule;” RIN 1210-AB95).

Given the unusually short time frame for public comment, we are unable to express our views on every aspect of the Proposed Rule. However, we write to express significant concern with the overall approach and its core components. In summary, this Proposed Rule is based on a deep misunderstanding of environmental, social and governance (ESG) investing, denies the openly espoused best interests of plan participants, imposes significant new costs and risks on plan participants, and ignores the fact that many ESG considerations are essential to reducing portfolio risk, particularly as it relates to addressing climate change. We urge DOL to withdraw it.

***Background on the Proposed Rule***

On June 23, 2020, the Department of Labor issued a Proposed Rule entitled “Financial Factors in Selecting Plan Investments.” The proposed guidance relates to the fiduciary responsibility rules under Title I of the Employee Retirement Income Security Act of 1974 (ERISA), which establishes minimum standards that govern the operation of private-sector employee benefit plans. According to the notice, guidance is aimed at providing clarity and certainty around the application of the fiduciary rules to ESG investments. The Proposed Rule is an extension of earlier guidance on ESG investing provided during the Obama Administration yet now takes a hard turn toward the opposite direction.

***The Proposed Rule Is Based on a Flawed Understanding of ESG Investing***

The Proposed Rule fails to adequately define a “problem” that the Proposal would address. However, it does clearly seek to dramatically restrict the ability of fiduciaries to consider ESG factors in their investment decisions. It appears to largely block most, if not all, ESG-focused investment products from

plans. It also appears to dramatically impact investment opportunities in investment products that are not identified as “ESG” related. This broad reach appears to be based on a flawed understanding of how ESG factors are considered in investing.

At a basic level, if the DOL is to properly regulate the consideration of ESG factors, it must first understand how ESG factors are considered by investors and fiduciaries. It should distinguish between different approaches to how ESG-conscious investing occurs. The Proposed Rule does none of this.

Increasingly, investors – like other businesses – are factoring so-called ESG considerations into the very fabric of their decision-making processes. For example, a large asset manager may factor ESG-issues into its evaluation of stocks for its standard “Small Cap Stock Fund.” This fund may not be branded or advertised as an “ESG” fund but is rather just the manager’s standard offering. Based upon the prudence of the fiduciary tasked with overseeing the fund, the overall investment decisions for the adviser across all of its funds reflect consideration of ESG factors.<sup>1</sup> This is common across asset managers of all sizes, across asset classes (e.g., equities and fixed income), and across different jurisdictions.

Additionally, there are also self-identified ESG-specific investment products. These may include investment funds that exclude certain types of holdings based on ESG-related factors (such as fossil fuels). It may include investment funds that specifically weight or favor certain types of holdings based on ESG-related factors. And it may also include so-called impact investment fund vehicles, which are often very targeted on specific technologies or processes. These ESG-focused investment products are often used by investors to provide the specific types of investment options they prefer.

The Proposed Rule must gather relevant evidence regarding how investors consider ESG issues when making their investment decisions, analyze that evidence, and establish how its approach would reasonably address the problem it has identified.

The Proposed Rule has identified no problem. It has not gathered the relevant evidence. It has not analyzed how its solution would reasonably address a specific problem. Instead, the proposal adds extra burdens onto fiduciaries who consider ESG factors—burdens not imposed on investments in risky fossil fuel firms and funds, for example.

### ***ESG Integration Has A Track Record of Performance and Investors Want It***

Integrating ESG factors into investing is first and foremost, about the relevance of ESG factors to financial performance.

Attacks on ESG integration into prudent investing are misguided and would in particular make it harder to invest retirement savings with a view to long-term risks. CalPERS, the country’s largest pension fund, recently found that 20% of its \$394-billion portfolio bears climate-related financial risk. Managing these risks is not about simply adding a “Green” fund option to a portfolio, it is about having an entire portfolio that is constructed with the recognition of the importance of ESG factors. Some of the largest asset managers in the world are already integrating ESG factors into all of their investment decisions. And the world’s largest investment manager, BlackRock, announced it will avoid investments in companies with significant climate risk.

Luckily, there are also specific ESG investment products as well. And those are also very commonly held.

A quarter of all professionally managed investments in the U.S. are tied to ESG factors. Beyond a desire to put money toward socially responsible funds, this volume signifies that investors are recognizing that addressing climate change is an important way to manage risk.

Specific ESG investment products have also proven to be safe, well-performing investment vehicles. Research from S&P Global Market Intelligence found that ESG funds are particularly reliable during times of economic downturns. Analyzing 17 ESG-focused funds, it found all but three of them outperformed the S&P 500 in 2020 through May 15. Frankly, the energy sector, which has been dominated by the fossil fuel industry, has been the worst performing sector in the S&P 500 for over a decade. Looking at the long term, Morningstar found that most Europe-domiciled sustainable funds outperformed their average traditional peer over the course of 10 years. These findings suggest that adding ESG investments to retirement savings funds, whether defined benefit plan or 401(k), could mitigate financial risks and could potentially improve longer-term returns.

Investors are obviously clamoring for ESG integration and options. And in Europe, ESG integration is required by law.

The Proposed Rule would put US-based asset managers at a competitive disadvantage to those in Europe. Essentially, US asset managers would be prohibited from broad-based ESG integration for their DOL accounts, but then compelled to do that—integrate ESG—in Europe. As a practical matter, would they then have to have two different, “US Small Cap Stock” funds, one that includes ESG factors and one that does not? What are the costs of these different investment processes? And on whom will the new costs and burdens fall? The Proposed Rule ignores these pesky realities.

Further, to the extent that consideration of ESG factors has been shown to lead to better long-term performance, the DOL’s strong discouragement against considering ESG factors may lead to materially worse outcomes for plan participants.

Put simply, the Proposed Rule would substitute the informed desires of investors with the uninformed politically driven judgment of the DOL.

### ***ESG Integration Should Be the Norm Rather Than Stymied***

The Proposed Rule’s requirements to perform additional analysis and documentation build in an unnecessary cost to pursue ESG options and bring about compliance risks for fiduciaries who must operate with caution, ultimately artificially limiting returns. Given the track record of performance and risk management, especially given the coming risks of climate change, ESG integration should be – and is otherwise rapidly becoming -- the norm. The Proposed Rule would seek to undo that progress.

While the Proposed Rule appears, in certain aspects, to reflect legitimate concerns around greenwashing (where investments purport to be ESG without solid foundation therein), the DOL would better serve retirement savers by instead pushing retirement funds to publicly disclose the ESG-related information about the companies in which they invest in a manner that can be compared easily across firms by fiduciaries, investors, and retirement savers, alike—or better yet, work with the Securities and Exchange Commission to do that across all companies and funds.<sup>ii</sup>

***The Proposed Rule Would Operate Like a Backdoor Bailout of the Fossil Fuel Industry and Contribute to Financial Instability***

Beyond the rule’s challenge to responsible fiduciary advisors, it effectively and inexplicably places a thumb on the scale in favor of fossil fuel investments at a time when investors and the public face the greatest systemic risk to our financial system – climate change. Driving investment away from more climate-friendly portfolio holdings forces retirement plan managers to subject employees to avoidable risk. The short-term impact would be to continue to misprice capital, while long-term risks are hidden to retirees. In addition, the accumulation of climate-related risks in the financial system portends financial instability.<sup>iii</sup>

***The Short Comment Period Fails To Provide Adequate Opportunity For Public Input***

The Proposed Rule is highly impactful on workers’ retirement security and yet is being proposed under an extraordinarily short 30-day comment period. The extremely limited comment period has significantly impacted interested parties’ ability to fully evaluate the impacts of the proposal, understand its economic and broader impacts, and ultimately protect statutorily-secured administrative law rights. Owing to the totality of problems in the Proposed Rule, we respectfully, but strongly, urge you to withdraw it. At a minimum, we urge you to extend the comment deadline for an addition 90 days.

***Conclusion***

ESG incorporation has the impact, in general, of steering capital toward safer, low-carbon investments, which would protect plan holders, financial stability, and the planet. The Proposed Rule misses an opportunity to advance all three interests simultaneously and instead reflects the worst kind of backsliding on all three—and, as noted above, under highly inappropriate procedural circumstances.

Sincerely,

Andy Green  
Managing Director of Economic Policy

Alexandra Thornton  
Senior Director for Tax Policy

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<sup>i</sup> See, e.g., T. Rowe Price, T. Rowe Price ESG Integration GUIDELINES FOR INCORPORATING ENVIRONMENTAL AND SOCIAL FACTORS, 2017, available at [https://www.troweprice.com/content/dam/trowecorp/Pdfs/FINAL%20GUIDELINES\\_CT0011790\\_P2\\_Approved\\_R I\\_Guidelines\\_2017.pdf](https://www.troweprice.com/content/dam/trowecorp/Pdfs/FINAL%20GUIDELINES_CT0011790_P2_Approved_R I_Guidelines_2017.pdf).

<sup>ii</sup> Andy Green and Andrew Schwartz, “Corporate Long-Termism, Transparency, and the Public Interest,” Center for American Progress, October 2, 2018, available at <https://www.americanprogress.org/issues/economy/reports/2018/10/02/458891/corporate-long-termism-transparency-public-interest/>

<sup>iii</sup> Andy Green, Gregg Gelzinis, and Alexandra Thornton, “Financial markets and Regulators Are Still in the Dark on Climate Change,” Center for American Progress, June 29, 2020, available at <https://www.americanprogress.org/issues/economy/reports/2020/06/29/486893/financial-markets-regulators-still-dark-climate-change/>