



Will Hild and John Meyer  
Consumers' Research  
9211 Bulls Run Pkwy  
Bethesda, MD  
(941) 302-8593  
[whild@consumersresearch.org](mailto:whild@consumersresearch.org)

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Jason A. DeWitt  
Office of Regulations and Interpretations  
Employee Benefits Security Administration  
Room N-5655  
U.S. Department of Labor  
200 Constitution Avenue NW  
Washington, DC 20210  
Attention: Financial Factors in Selecting Plan Investments Proposed Regulation.

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**Consumers' Research Comment to the Department of Labor, Employee Benefits Security Administration on RIN 1210-AB95, Financial Factors in Selecting Plan Investments**

Consumers' Research<sup>1</sup> is a 501(c)(3) educational non-profit advocating for the general interests of consumers. This comment letter is intended to present a consumer-oriented discussion of the issues relating to the Department of Labor (DOL)'s Proposed Regulation confirming that Title I of the Employment Retirement Income Security Act (ERISA) requires plan fiduciaries to 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.

**Employer-sponsored retirement plans should focus solely on pure economic benefits for their participants**

Consumers' Research supports the Proposed Regulation clarifying that ERISA fiduciary requirements mandate investment decisions related to employer-sponsored retirement plans must consider only purely economic considerations. The Proposed Regulation is right not to allow the inclusion of Environmental, Social, and Corporate Governance (ESG) considerations in investment decisions for employer-sponsored retirement plans. Furthermore, the proposed rule rightly emphasizes the longstanding ERISA policy that the fiduciaries of all such retirement plans must focus solely on maximizing the pure economic return for the plans' beneficiaries.

Regardless of the goals of ESG investing, any decision to include factors unrelated to returns in the analysis of investments in pension and employee investment accounts is a clear violation of the longstanding fiduciary duty that employers and fund managers owe employees according to the law. Part of this duty includes an unspoken agreement that plan

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<sup>1</sup> Founded in 1929, Consumers' Research is the nation's oldest consumer affairs organization. Consumers' Research aims to increase the knowledge and understanding of issues, policies, products, and services of concern to consumers and to promote the freedom to act on that knowledge and understanding.

managers must seek the highest returns consistent with safety for all ERISA-covered investments.

### **Criteria for ESG are too uncertain to be a guide to fiduciary investments**

Advocates of ESG considerations often claim ESG serves as a better guide for investment returns than straight calculations. This claim assumes that ESG investments provide greater overall social benefits, even if ESG investments are not as profitable. However, no standard exists to qualify or quantify what makes ESG investments broadly beneficial to society. Even for an individual investment, there is no collective consensus as to an investment's social benefits. These issues exist across all three components of ESG.

- 1) For environmentally beneficial, “sustainable” investments, the issues are myriad. Many environmentally oriented investments altogether avoid fossil fuel energy investments, opting instead for renewables. However, nuclear energy produces no greenhouse gas emissions, so nuclear investments may be environmentally positive after the consideration of all pros and cons. Similarly, the increasing availability of natural gas has reduced pollution by replacing more environmentally damaging coal. ESG investment principles would eschew nuclear energy and natural gas, possibly leading to worse overall ecological outcomes.

On the other hand, not all “renewable” energy investments lead to environmentally desirable outcomes when calculating the total environmental effects of all inputs needed to produce the energy. For example, corn ethanol is energy-inefficient and uses a sizable amount of excess energy from gas and oil to produce each gallon of ethanol. The energy required to produce a gallon of corn ethanol is nearly 50% of the energy it supplies on average.<sup>2</sup>

- 2) For socially desirable investments, the picture is even cloudier. What constitutes a socially desirable economic activity depends entirely on one's point of view – and often on one's economic interests. For example, investments in inner-cities are often considered socially desirable, and some may be very beneficial. Still, it is impossible to mathematically qualify whether it is more socially desirable to invest in inner cities or rural areas. There is no consensus on what investments are socially undesirable. For example, while most ESG proponents would avoid tobacco investments, there is likely no consensus on whether a company that produces some fattening foods would make for a socially undesirable investment.

Internationally, there is even more controversy. Should investments in China be avoided, due to rampant human rights violations? What about Chinese state-sponsored systematic theft of intellectual property? Are Russian investments socially undesirable

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<sup>2</sup> USDA Office of Energy Policy and New Uses February 2016 *2015 Energy Balance for the Corn Ethanol Industry* Page 18  
<https://www.usda.gov/oce/reports/energy/2015EnergyBalanceCornEthanol.pdf>

because Russia is under extensive international sanctions for its forcible seizure of Ukrainian territory?

- 3) Of the three, corporate governance considerations come closest to consensus. However, as governance considerations become more ubiquitous, it becomes nearly impossible to divorce an ever-increasing array of corporate board requirements from corporate operations. Boards are not always the most efficient and effective decision-makers. Many of the significant achievements of corporate America were and still are the result of bold, individual leaders, often largely untrammelled by board control bent on operation micromanagement. For example, Amazon's achievements in consumer delivery might have been curtailed without a strong CEO in Jeff Bezos.

Since there is no consensus on what qualifies as an ESG investment, nor is it possible to quantify the value of an ESG investment monetarily, using ESG considerations as a general guide to investment decisions for retirement plans covered by ERISA is a violation of fiduciary duty. Any fiduciary decision-maker applying ESG metrics to investing does so under his or her personal views, skewed by beliefs and prejudices. In worst-case scenarios, using ESG metrics could even be used to boost interests of decision-makers, rather than clients' interests.

**DOL should not retain the provision allowing ESG preference if two investment alternatives are “economically indistinguishable” in Paragraph (c)(2) of the Proposed Regulation**

While the proposed language of Paragraph (c)(2)<sup>3</sup> does strengthen the current protections against the substitution of ESG criteria for purely economic analysis of investment alternatives, it is not altogether sufficient to eliminate the problem of subordinating the interests of plan beneficiaries to ESG considerations. The provision allowing ESG preference if two investment alternatives are “economically indistinguishable” should not be retained. Not only is ESG an unclear criterion for investment decisions, but even worse, it is one that allows for the possibility that investment decision-makers may substitute their views for the interests of the investment clients.

As stated in the supplementary information to the Proposed Rule, it is rare for two investment alternatives to be “economically indistinguishable.” However, it is not rare for two or more investment alternatives to be economically close in value. There is usually a range of possible estimates of any investment's economic value, and the evaluation of investments very close in value is likely to be complex, leaving room for personal judgment. Thus, there is considerable opportunity in the assessment of investment alternatives for those with an incentive to favor an ESG plan to nudge the process so that a slightly economically inferior ESG investment could be considered “economically indistinguishable” from a non-ESG alternative. Indeed, such a process may not even be deliberate. It may be a result of subconscious pro-ESG biases of plan managers and fiduciaries. Once an ESG

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<sup>3</sup> See Proposed Rule 85 FR Page 39127

alternative becomes “economically indistinguishable” from a competing investment, the ESG alternative, though economically inferior, could then be selected.

Rather than set up additional review processes to ensure that an ESG alternative is truly “economically indistinguishable” from a non-ESG alternative, the DOL should move to eliminate fiduciary agency use of ESG preference altogether. This ensures only economic criteria are used in selecting ERISA-regulated plan investments. Note this does not mean considerations falling under the rubric of ESG may not be considered, but that they may be considered only for their purely economic impact on the performance of a particular investment alternative. Further, note that there are many possible non-ESG tiebreakers between the rare truly economically indistinguishable alternatives; for example, preference could be given to the investment alternative with a longer going concern or to the one with the least volatility over time.

### **Use of ESG is especially undesirable for private Defined Benefit (DB) plans**

Using ESG considerations is especially problematic for private DB plans because a significant percentage of DB plans, particularly the multiemployer DB plans, fall well short of full funding to provide all promised benefits.<sup>4</sup> DB plans often rely on high (and not always realistic) estimates of return on assets. While significant portions of the relatively sounder class of single-employer pension plans are also underfunded and vulnerable to future recessions, these plans are not in as precarious a position as multiemployer DB plans.<sup>5</sup> Therefore, DB plans need all the return on assets they can get to improve their chances of having the resources to pay promised benefits in the future.

Insolvency is not the only justification for the prohibition of ESG investing in DB plans. The beneficiaries of DB plans have no input into the DB plan’s investment policies. They are entirely involuntary participants in any use of ESG considerations that could reduce investment returns or that pursue social objectives they do not support.

Furthermore, the Pension Benefit Guarantee Corporation (PBGC) is obligated to make good a portion of the pension obligations of DB plans that cannot meet their pension obligations. Since the U.S. government backstops the PBGC, there is also a potential additional cost to taxpayers unless DB pension funds are required to invest strictly for maximum safe return.<sup>6</sup>

**For Defined Contribution (DC) plans with participant choice of investments, an adequate range of non-ESG options must be offered and ESG plans must never be a default option**

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<sup>4</sup> Multiemployer pension plans are at risk as they have declining bases of support; about 10% of them are likely not to be able to pay current benefits due within the next 20 years. See <https://www.actuary.org/content/overview-multiemployer-pension-system-issues>

<sup>5</sup> <https://www.investopedia.com/articles/retirement/08/safe-db-plan.asp>

<sup>6</sup> The PBGC’s resources are projected to run out by 2025, thereby necessitating a Federal bailout See <https://www.cnn.com/2019/07/12/these-pension-plans-are-at-risk-of-going-broke-lawmakers-need-a-fix.html>

DC plans offering plan participants alternative investment options must also provide an adequate menu of non-ESG choices. In addition to the language of Paragraph (c)(3)(i) requiring that all plans must meet strong criteria for economic return and safety, there are two additional reasons to mandate the inclusion of suitable non-ESG alternatives. First, despite clear guidance to use only economic criteria in selecting investment alternatives, there may still be some bias among some plan managers, and even in some instances political pressure, in favor of ESG alternatives. Second, even if the ESG alternatives are completely sound economic choices, some plan participants may strongly disagree with the ESG investment objectives and want a broad menu of non-ESG options. Accordingly, Consumers' Research suggests adding the following additional language to Paragraph (c)(3) after subparagraph (iii) as subparagraph iv:

*Before any ESG plans may be added to a Defined Contribution menu of investment options, the fiduciary shall ensure that a broad range of non-ESG plans that meet the general criteria laid out in subparagraph c(3)(1) is already available to participants.*

This additional language ensures a full range of choices for consumers who do not want to risk investing in any ESG plans or do not agree with an ESG plan's objectives. Any inclusion of an additional ESG plan or plans in the menu of DC investment alternatives then expands the range of consumer choice of investment plans boosting individual consumer welfare.

The Proposed Rule rightly bars ESG alternatives from being used as a Qualified Default Investment Alternative (QDIA) or being a component of a QDIA.<sup>7</sup> ESG alternatives involve considerations other than purely economic ones, and they should never be the default choice when a participant in a participant choice plan does not decide investment allocation. QDIA's are usually selected to be lower-risk alternatives in the absence of a participant decision on risk, while ESG plans, even if economically sound, carry additional risk of underperforming compared to non-ESG investments.

## Conclusion

The proposed rule is a much-needed clarification of the fiduciary duties of employer-sponsored plans under ERISA. It strongly reinforces the longstanding practice that investment decisions for employer-sponsored retirement plans should be just that – investment decisions – with the sole goal of prudently growing participants' accounts. The DOL's proposed rule is a welcome and laudable action that goes a long way toward preventing the politics of fiduciary management from undermining that foundation of financial stewardship. Employers and pension fund managers have no right to seek any other goals, however noble. They have a legal and moral obligation to boost the financial wellbeing of participants in retirement accounts. It is especially objectionable for any manager or fiduciary to make political statements, seek political goals, or yield to political pressure in making any investment decisions at the expense of retirees' market returns. The proposed rule is in the

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<sup>7</sup> See Proposed Regulation paragraph (c)(3)(iii)

best interest of consumers and, with some small adjustments as outlined above, should be adopted as a Final Rule.

Sincerely,

*Will Hild*

Will Hild, Executive Director

*John C. Meyer*

John Meyer , Senior Researcher