



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:

I write to provide comments in response to the Department of Labor's proposed rule, "Financial Factors in Selecting Plan Investments" (RIN 1210-AB95) (the "Proposal").

Capricorn Investment Group was born from a belief that sustainable investment practices can enhance risk-adjusted returns. Underlying this investment approach is a deep desire to demonstrate the huge investment potential that resides in breakthrough commercial solutions to the world's most pressing problems. One of the largest mission-aligned investment firms in the world, Capricorn has grown to manage more than \$5 billion in multi-asset class portfolios for families, foundations and institutional investors.

The Department of Labor fails to articulate a rational connection between the relevant facts and the proposed rule. The Proposal reveals a fundamental misunderstanding of how professional investment managers use environmental, social and governance (ESG) criteria as an additional level of due diligence and analysis in the portfolio construction process. Investment managers increasingly analyze ESG factors precisely because they view these factors as material to financial performance.

The proposed rule assumes ESG strategies sacrifice financial returns, but current research findings show ESG strategies' outperformance. Please see the attached Reference Document, Section A, which cites applicable research findings, studies and articles documenting ESG outperformance.

The proposed rule assumes ESG considerations are not widely applied, but there is a history of effective use of material ESG considerations by mainstream investors. Please see the attached Reference Document, Section B which cites data on the widespread use of ESG considerations by mainstream investors.

The proposed rule assumes ESG considerations are not material, but the Sustainability Accounting Standards Board standards adoption process is based on financial materiality legal standard. Please see the attached Reference Document, Section C which provides relevant data on SASB standards.

The proposed rule assumes ESG considerations could violate fiduciary duty, but other jurisdictions' regulatory interpretations support prudent investor consideration of ESG factors as material and within fiduciary duty. Please see the attached Reference Document, Section D which provides information on the incorporation of ESG factors as material within fiduciary duty by non-U.S. jurisdictions' regulations.

The proposed rule assumes that ESG considerations are not material to corporate success, but the Business Roundtable Statement on Corporate Purpose (<https://opportunity.businessroundtable.org/ourcommitment/>) demonstrates broad issuer acceptance of materiality as integral to corporate long-term success.

The Proposal is likely to have the perverse effect of dissuading fiduciaries, even against their better judgment, from offering options for their plans that consider ESG factors as part of the evaluation of material financial criteria. As a result, it will unfairly, and harmfully, limit plan diversification and perhaps compel plan participants to choose options that are either more risky or less profitable.

I respectfully request that the Proposal be withdrawn. Thank you for your consideration of these comments.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric Techel', written in a cursive style.

Eric Techel
Partner

Supporting Data and References

A. Current research findings on ESG outperformance

- i. From 2014-2019, sustainable funds did well in both up and down markets relative to conventional peers. “When markets were flat (2015) or down (2018), the returns of 57% and 63% of sustainable funds placed in the top half of their categories. When markets were up in 2016, 2017, and 2019, the returns of 55%, 54%, and 65% of sustainable funds placed in the top half of their categories.” - [“US ESG Funds Outperformed Conventional Funds in 2019”, Morningstar, 2020](#)
<https://www.morningstar.com/articles/973590/us-esg-funds-outperformed-conventional-funds-in-2019>
- ii. “The performance of sustainable funds relative to the fund universe is consistent with evidence from academic research, which suggests no systematic performance penalty associated with sustainable investing and possible avenues for outperformance through reduced risk or added alpha.” - [“US ESG Funds Outperformed Conventional Funds in 2019”, Morningstar, 2020](#)
<https://www.morningstar.com/articles/973590/us-esg-funds-outperformed-conventional-funds-in-2019>
- iii. Research from 2004 to 2008 on 11,000 mutual funds shows no financial trade-off in the returns of sustainable funds compared to traditional funds, and they demonstrate lower downside risk. Moreover, during a period of extreme volatility, the study found “strong statistical evidence that sustainable funds are more stable.”- “Sustainable Reality: Analyzing Risk and Returns of Sustainable Funds, [Morgan Stanley Institute for Sustainable Investing](#), 2019
[https://www.morganstanley.com/pub/content/dam/msdotcom/ideas/sustainable-investing-offers-financial-performance-lowered-risk/Sustainable Reality Analyzing Risk and Returns of Sustainable Funds.pdf](https://www.morganstanley.com/pub/content/dam/msdotcom/ideas/sustainable-investing-offers-financial-performance-lowered-risk/Sustainable%20Reality%20Analyzing%20Risk%20and%20Returns%20of%20Sustainable%20Funds.pdf)
- iv. 89% of research studies showed that companies with high ESG ratings exhibit market-based outperformance compared to industry peers; another showed that 90 companies with strong sustainability policies outperformed a similar group with low sustainability standards, with a 4.8% higher annual above-market average return between 1993 and 2011. - ["The Business Case for ESG", IEN, 2016](#)
https://d3n8a8pro7vhmx.cloudfront.net/intentionalendowments/pages/1031/attachments/original/1477713492/BusinessCaseforESG_2016_v2-Oct2016.pdf?1477713492
- v. A 2016 analysis of Morningstar Analyst Rating for funds found that funds tagged as “socially conscious” have better ‘star ratings’ than the overall universe. - [“You Don't Have to Sacrifice Returns for Sustainability”, Morningstar, August 2016](#)
<https://www.morningstar.com/articles/765799/article>

- vi. Morgan Stanley Institute for Sustainable Investing found that investing in sustainability has usually met, and often exceeded, the performance of comparable traditional investments. This is true on both an absolute and a risk-adjusted basis, across asset classes and overtime. - ["Sustainable Reality: Understanding the Performance of Sustainable Investment Strategies"](#), Morgan Stanley Institute for Sustainable Investing, March 2015
[https://www.morganstanley.com/content/dam/msdotcom/ideas/sustainable-investing-offers-financial-performance-lowered-risk/Sustainable Reality Analyzing Risk and Returns of Sustainable Funds.pdf](https://www.morganstanley.com/content/dam/msdotcom/ideas/sustainable-investing-offers-financial-performance-lowered-risk/Sustainable%20Reality%20Analyzing%20Risk%20and%20Returns%20of%20Sustainable%20Funds.pdf)
- vii. Both ESG Tilt and ESG Momentum strategies outperformed a global benchmark over an eight-year period. A significant portion of this outperformance was not explained by style factors, and may have been attributable to ESG factors. - ["Can ESG Add Alpha? An Analysis of ESG Tilt and Momentum Strategies"](#), MSCI, June 2015
<https://www.msci.com/documents/10199/4a05d4d3-b424-40e5-ab01-adf68e99a169>
- viii. Meta-study of more than 200 sources, 88% of which found that companies with strong sustainability performance had better operational performance and cashflows, and 80% of which found strong sustainability performance had positive effects on investment performance. - ["From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance"](#), Gordon L. Clark, Andreas Feiner, Michael Viehs, March 2015
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2508281
- ix. Found that 89% of research studies showed that companies with high ESG ratings exhibit market-based outperformance compared to industry peers.- ["Sustainable Investing: Establishing Long-Term Value and Performance"](#), Climate Change Advisors, June 2012
- x. 8-year study (1993-2011) showing that 90 companies with strong sustainability policies outperformed a similar group of 90 companies with low sustainability standards, with a 4.8 percent higher annual above-market average return. - ["The Impact of Corporate Sustainability on Organizational Processes and Performance"](#), Harvard Business School, July 2013
https://www.hbs.edu/faculty/Publication%20Files/SSRN-id1964011_6791edac-7daa-4603-a220-4a0c6c7a3f7a.pdf
- xi. Five year study (2014-2019) shows that Rockefeller Brothers' fossil fuel free fund outperformed traditional funds. Portfolio achieved a 7.76% return, while benchmark investment portfolio returned only 6.71% annually. - ["Investing in our mission"](#), Rockefeller Brothers, May 2020
https://www.rbf.org/annual-reports/investing-our-mission?utm_source=Rockefeller+Brothers+Fund&utm_campaign=cf20c75e77-

[EMAIL CAMPAIGN 2020 05 08 07 48&utm_medium=email&utm_term=0_d51d1fa0e4-cf20c75e77-428268393](https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199)

- xii. “U.S. companies with high (top quintile) ESG rankings in the S&P 500 index have outperformed their counterparts with lower (bottom quintile) ESG rankings by at least 3% every year for the past five years/ - [“ESG from A to Z”, Bank of America Global Research, November 2019](#)
- xiii. 30 year study showed that an emerging markets investment trust that considered relevant environmental and social factors achieved a total net asset value over 1950% against a return of about 700 % of the MSCI Emerging Markets Index.- [“Invest for Good: A Healthier World and a Wealthier You.”, Mobius Capital, 2019 \(p 200\)](#)
[https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID19_12722/ESG from A to Z.pdf](https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID19_12722/ESG_from_A_to_Z.pdf)
- xiv. NACUBO concluded that there is no evidence that ESG/SRI strategies negatively impacted the investment returns of college and university endowments in FY2019. “ESG/SRI users realized a 5.3% average 1-year return and an 8.4% 10-year return. Non-ESG/SRI users realized a 5.1% 1-year return and an 8.4% 10 year return. - “Emerging Strategies for SRI/ESG in College and University Endowments”, NACUBO and TIAA, Presentation at 2020 Endowment and Debt Management Forum, February 2020
- xv. “97% of the respondents pledging to divest in 2014, held 1% or less of their portfolio invested in fossil fuels as of 2019, all while maintaining or improving their expected risk-return profiles.” [“Divest Invest Philanthropy: Five Years After Launch.”, The Croatan Institute, October 2019](#)
<http://croataninstitute.org/total-portfolio/publication/divest-invest-philanthropy-2>
- xvi. “Sustainable funds comfortably outperformed their peers in 2019. The returns of 35% of sustainable funds placed in the top quartile of their respective categories, and nearly two thirds finished in the top two quartiles. By contrast, the returns of only 14% of sustainable funds placed in the bottom quartile, and only about one third placed in the bottom half.” - [“US ESG Funds Outperformed Conventional Funds in 2019”, Morningstar, 2020](#)
<https://www.morningstar.com/articles/973590/us-esg-funds-outperformed-conventional-funds-in-2019>
- xvii. Morningstar data shows that in March 2020, when market activity saw further downturns as countries began to implement lockdown measures, 62% of ESG-focused large-cap equity funds [outperformed the global tracker](#)
 [\(https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199\)](https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199).
- xviii. Sustainable funds loss less than their peer groups during COVID 2020 Economic Downturn. 7 out of 10 sustainable equity funds finished in the top halves of their

Morningstar Categories, 24 out of 26 ESG tilted index funds outperformed their closest conventional counterparts. [“Sustainable Funds Weather the First Quarter Better Than Conventional Funds”](#), Morningstar, April 2020
<https://www.morningstar.com/articles/976361/sustainable-funds-endure-the-first-quarter-better-than-conventional-funds>

B. Data supporting the use of material ESG considerations by mainstream investors

- i. Global survey showed that more than half of global asset owners are currently implementing or evaluating ESG considerations in their investment strategy. Investors understand that material issues such as climate risk, board quality, or cybersecurity impact financial values in positive or negative ways and must be a part of the evaluation process. [“Smart beta: 2018 global survey findings from asset owners”](#), FTSE Russell, 2018
<https://investmentnews.co.nz/wp-content/uploads/Smartbeta18.pdf>
- ii. 73% of global investors surveyed by the CFA Institute in 2015 indicated they take ESG issues into account in their investment analysis and decisions. [“CFA Institute Survey: How do ESG Issues Factor into Investment Decisions?”](#), CFA Institute, August 2015
<https://blogs.cfainstitute.org/marketintegrity/2015/08/17/cfa-institute-survey-how-do-esg-issues-factor-into-investment-decisions/>
- iii. SRI assets have expanded to \$12 trillion today, up 38% from \$8.7 trillion in 2016. Investors are increasingly realizing that ESG criteria is important when considering material risk. [Trends, US SIF, 2020](#)
<https://www.ussif.org/files/US%20SIF%20Trends%20Report%202018%20Release.pdf>
- iv. PRI signatories (showing commitment to standards of sustainable investing) increased from less than 10 in April 2006 to over 2000 in 2018. [“The Role of Investors in Supporting Better Corporate ESG Performance”](#), Ceres, February 2019
[https://www.ceres.org/sites/default/files/reports/2019-04/Investor Influence report.pdf](https://www.ceres.org/sites/default/files/reports/2019-04/Investor%20Influence%20report.pdf)

C. Sustainability Accounting Standards Board standards adoption process is based on financial materiality legal standard

- i. SASB framework is underpinned by the legal basis of materiality in the US. Its standards have undergone vetting by industry experts, comprising a balanced group of ⅓ corporate professionals, ⅓ investors, and ⅓ other stakeholders. Its determinations are guided by its core objectives to provide the users and providers of financial capital with material, decision-useful, cost-effective disclosure. - [SASB Conceptual Framework](#)
<https://www.sasb.org/wp-content/uploads/2019/05/SASB-Conceptual-Framework.pdf>
- ii. “SASB standards are designed for inclusion in mandatory financial reports. In the US, this takes the shape of the Form 10-K. [U.S. securities law firmly undergirds SASB’s work](#)

[and process](#), providing a solid foundation for the use of SASB standards by U.S. companies.” - [SASB.org](#)

<https://www.sasb.org/wp-content/uploads/2019/05/SASB-Conceptual-Framework.pdf>

D. Non-U.S. jurisdictions’ regulatory interpretations supporting prudent investor consideration of ESG factors as material and within fiduciary duty

- i. **The UK Pensions Regulator:** The Occupational Pension Schemes (Investment) Regulations require pension funds’ Statement of Investment Principles to cover “the extent (if at all) to which social, environmental or ethical considerations are taken into account in the selection, retention and realization of investments; and their policy (if any) in relation to the exercise of the rights (including voting rights) attaching to the investments.” This was strengthened by supporting guidance from The Pensions Regulator on the importance of ESG issues to prudent scheme practice. [Guide to Investment Governance – The Pensions Regulator](#)
- ii. **The Federal Government of Norway (2005, 2015):** The Government Pension Fund’s mandate commits the fund to upholding principles based on the UN Global Compact, the OECD Principles of Corporate Governance and the OECD Guidelines for Multinational Enterprises, as well as considering environmental factors in management of the real estate portfolio.⁷ The fund is also subject to an exclusions list, including companies that pose serious human rights violations, severe environmental damage, and, as of 2016, those that produce coal, or a coal-based energy source.⁸
- iii. **The European Commission (2016):** The Revision of the Institutions for Occupational Retirement Provision Directive (IORP II) requires pension funds above a certain size to consider ESG issues and disclose how related risks are considered in the Investment Policy Statement. The Directive has been approved by the European Parliament and must be transposed into Member State law within 24 months. [Article 19 Investment Rules](#)
<https://service.betterregulation.com/document/257562>
- iv. **Article 173 of the French Energy Transition Law:** Article 173 requires institutional investors to disclose in their annual report information on how ESG criteria are considered in their investment decisions and how their policies align with the national strategy for energy and ecological transition. It also places disclosure requirements on listed companies, banks and credit providers
- v. **China, Hong Kong, India, Singapore, Malaysia, and South Korea:** A summary of codes, policies, and regulations cited to demonstrate the significant growth in policy maker’s interest in ESG factors in recent years. [UNEPFI \(pg 13\)](#)
https://www.unepfi.org/fileadmin/documents/Investor_obligations_and_duties_in_six_asian_markets.pdf