December 13, 2021

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

RE: Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights

Attention: RIN 1210-AC03

Dear Acting Assistant Secretary Khawar,

I am writing on behalf of the Consumer Federation of America (“CFA”) to provide our views in response to the Department of Labor’s (hereafter “Department” or “DOL”) request for comment regarding its proposed changes to rules covering the duties of prudence and loyalty that apply to plan fiduciaries that are regulated by the Employee Retirement Income Security Act of 1974 (ERISA), titled Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights (hereafter, “Proposed Amendments” or “current rule proposal”). CFA applauds the Department for acting to correct the regulatory missteps of two previous rules (hereafter, collectively “2020 rules”) issued in late 2020: the Financial Factors in Selecting Plan Investments (hereafter, “Financial Factors Rule”) and the Fiduciary Duties Regarding Proxy Voting and Shareholder Rights (hereafter, “Proxy Voting Rule”).

As proposed, the amendments to the Investment Duties regulation under Title I of ERISA will provide important and necessary relief to ERISA plan fiduciaries from unsupported limitations on fiduciaries’ ability to consider climate change and other environmental, social, or governance (“ESG”) considerations when making plan decisions, including decisions regarding investment choices and voting proxies.

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1 CFA is a non-profit association of more than 250 national, state, and local pro-consumer organizations. It was formed in 1968 to advance the consumer interest through research, advocacy, and education.
1. Why this Rule Proposal is Warranted

On November 13, 2020, the Department adopted the Financial Factors Rule, which amended the Investment Duties regulation to generally require plan fiduciaries to select investments and investment courses of action based **solely** on consideration of “pecuniary factors.” Unfortunately, since the adoption of the Financial Factors Rule, and the resultant imposition of an arbitrary and artificial binary of “pecuniary” vs. “non-pecuniary” investment factors, ERISA plan fiduciaries have been forced to endure significant uncertainty, and potential legal liability, in making certain plan decisions that they judge to be in the best interest of their clients.\(^5\) This false binary, which is in reality little more than a thinly veiled prescription against consideration of ESG factors by plan fiduciaries, has placed such fiduciaries in an illogical and untenable position, at odds with science, as well as the expressed preferences of large portions of the investing public.\(^6\)

The Proposed Amendments will realign the Department’s rules with the wealth of guidance and well-understood operating practices applicable to plan fiduciaries prior to the damage and confusion resulting from the adoption of the 2020 rules.\(^7\) The Proposed Amendments are necessary because the 2020 rules have proven to be illogical, impractical, and harmful. Further, the Proposed Amendments are warranted because they reflect the reality that ESG considerations are often material considerations for corporate issuers and reasonable investors alike. Plan fiduciaries must be permitted to take them into account in the same manner they are permitted, and indeed required, to consider other relevant factors.\(^8\)

A. ESG Factors are Relevant to a Fiduciary’s Investment Decisions

The release accompanying the Proposed Amendments specifically requests comment on whether fiduciaries should consider climate change as presumptively material in their assessment of investment risks and returns.\(^9\) The release also requests comment addressing any evidence of financial materiality arising from ESG factors in various investment contexts.\(^10\) In answer, CFA reiterates its

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\(^5\) *See, e.g.*, Alex Padalka, *New DOL ESG Rule’s ‘Tone’ Implies Plan Sponsors Protection: Lawyers*, Financial Advisor IQ, (Nov. 12, 2021), [https://financialadvisoriq.com/c/3395534/431804/rule_tone_implies_plan_sponsors_protection_lawyers](https://financialadvisoriq.com/c/3395534/431804/rule_tone_implies_plan_sponsors_protection_lawyers) (*“The Department of Labor’s currently proposed rule on plan sponsors considering environmental, social and governance factors in selecting investments gives them more protection against possible 401(k) lawsuits than the rule that had come out before Trump, lawyers say.”*)

\(^6\) *See, e.g.*, CFA Institute, *Comment Letter Re: Financial Factors in Selecting Plan Proposed Regulation*, at 10 (July 30, 2020), [https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00620.pdf](https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00620.pdf) (*“From our vantage point, as the world’s largest association of investment professionals, and following the evidence we detail above, the market has already come to a consensus that certain ESG factors are material and are an integral consideration in projecting risk-adjusted returns. In that respect, the Proposal contradicts market consensus.”*)


\(^8\) *See, e.g.*, Consumer Federation of America, *Comment Letter in re: Public Input on Climate Change Disclosures*, at 26 (June 14, 2021), [https://consumerfed.org/wp-content/uploads/2021/06/SEC-Climate-Change-Disclosure-Letter.pdf](https://consumerfed.org/wp-content/uploads/2021/06/SEC-Climate-Change-Disclosure-Letter.pdf) (*“Climate change-related data, the financial risks associated with this data, and the methodologies and assumptions used to obtain and present this data are material to the decision-making processes of reasonable investors.”*)


\(^10\) *Id.*
deeply-held view that ESG factors are often directly financially relevant to investment decision making, and that the false dichotomy of pecuniary vs. non-pecuniary factors is misguided and unwarranted.

For further support of this position, the Department need not look far, as many commenters responded to the 2020 Financial Factors Rule proposal with compelling testimony and evidence that ESG factors are squarely material and relevant to a fiduciary’s decision making. Additionally, the Department may look to leading academic research, statements from the world’s largest asset managers, or leaders of America’s largest companies, which taken together state the compelling case that ESG factors have material financial impacts on companies, and therefore on the ERISA fiduciaries that invest their clients’ savings in them.

Moreover, as the Department is aware, the Securities and Exchange Commission (SEC) on March 15, 2021, elicited input from the public on ESG-related disclosures, and that agency is expected to issue additional climate and ESG-related disclosure requirements for reporting issuers, either this year or next. Although the framework for evaluating ESG-related disclosures by SEC registered issuers and ERISA plan fiduciaries differs in some respects, there are also many clear parallels. Thus, the comment file from the aforementioned SEC rulemaking, and its extensive evidence to support the financial materiality of ESG factors, should also be fully considered and treated as a resource by the DOL.

Notably, in connection with the SEC’s request for public input on ESG materiality, SEC Commissioner Allison Herron Lee made public statements on May 24, 2021, that are especially instructive. Specifically, in the context of discussing financial materiality, Commissioner Lee sought to dispel certain prevalent misconceptions about the concept.

[T]he idea that investor concerns with scientifically supported risks like those associated with climate change is grounded in “politics” turns fact-based analysis on its head. If anything, it’s the insistence that science and data must or should be ignored that appears questionable. Second, the fact that a topic may have political or social significance does not foreclose its being material, either qualitatively or quantitatively. To the contrary, we are increasingly seeing all manner of market participants embrace ESG factors as significant drivers of decision-making, risk assessment, and capital allocation precisely because of their

relationship to firm value. Finally, investors, the arbiters of materiality, have been overwhelmingly clear in their views that climate risk and other ESG matters are material to their investment and voting decisions.\(^\text{17}\)

CFA agrees with this statement. Climate change-related data, the financial risks associated with this data, and the methodologies and assumptions used to obtain and present this data are material to the decision-making processes of reasonable investors.\(^\text{18}\) Moreover, at the most basic level, if climate and ESG-related factors are material to the decision making of reasonable investors – and they are – then it follows that ERISA fiduciaries should be permitted or required to consider those same factors in their decision-making.

The Department should, therefore, undertake rulemaking to encourage and require consideration of this information by ERISA fiduciaries managing retirement investment accounts.

**B. The Previous Rules Cause Unnecessary Confusion**

\[\text{a. Fiduciary Factors Rule}\]

For decades prior to 2020, Department regulations required fiduciaries to consider all relevant factors when choosing among available investment options. The Financial Factors Rule, published in the Federal Register on November 13, 2020, displaced this demonstrably effective and well-understood legal standard with a new and ill-defined “pecuniary” test, causing considerable confusion.\(^\text{19}\)

In our assessment, a key point of confusion from the 2020 Financial Factors Rule arises in its preamble, which offers a clumsy characterization of ESG factors as being both potentially material economic considerations and, at the same time, unreliable indicators of pecuniary impact. Specifically, the rule’s preamble acknowledged that previous DOL rules and guidance dictate that there could be instances when ESG issues present material business risk or opportunities to companies,\(^\text{20}\) and that plan fiduciaries would then treat these factors as material economic considerations under generally accepted investment theories.\(^\text{21}\) But it immediately follows that line of reasoning by “caution[ing] fiduciaries against too hastily concluding that ESG-themed funds may be selected based on pecuniary factors or are not distinguishable based on pecuniary factors,” which betrays a skepticism that ESG factors are viable pecuniary factors to consider in the first place.\(^\text{22}\) Thus, while the rule purports to allow fiduciaries to consider ESG factors, in the same paragraph it directly warns against doing so.\(^\text{23}\)

\(^\text{17}\) *Id.* (Internal citations omitted).

\(^\text{18}\) See Consumer Federation of America, *Comment Letter in re: Public Input on Climate Change Disclosures*, at 58.

\(^\text{19}\) Final Rule, *Financial Factors in Selecting Plan Investments*, at 72847.

\(^\text{20}\) *Id.*

\(^\text{21}\) The rule stated that in these cases the ESG factors are not "tie-breakers," but pecuniary (or "risk-return") factors affecting the economic merits of the investment.

\(^\text{22}\) *Id.*

\(^\text{23}\) See also Proposed Rule, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*, at 57275, (The preamble to the current (2021) rule proposal identified stakeholder confusion following the previous rule as a reasonable basis for concern, stating, “rather than provide clarity, some aspects of the current regulation instead may have created further uncertainty surrounding whether a fiduciary under ERISA may consider ESG and other factors in making investment and proxy voting decisions that the fiduciary reasonably believes will benefit the plan and its participants and beneficiaries.”)}
Additionally, the 2020 Fiduciary Factors Rule dictates significant additional recordkeeping requirements whenever ESG-related considerations are included in a plan investment decision where alternative investments appear otherwise economically indistinguishable. Not only are these recordkeeping requirements burdensome, they are also confusing, and they mandate a circular analysis. For example, plan fiduciaries are required to document why pecuniary factors were not sufficient to select the investment or investment course of action; how the selected investment compares to the alternative investments with regard to the factors listed in the rule; and how the chosen non-pecuniary factor is consistent with the interests of participants and beneficiaries in their retirement income or financial benefits under the plan.\(^24\) Such requirements are unreasonable or impossible by design.

And lastly, the 2020 rule contains a “prohibition against adding or retaining any investment fund, product, or model portfolio as a qualified default investment alternative (QDIA) . . . if the fund, product, or model portfolio reflects non-pecuniary objectives in its investment objectives or principal investment strategies.”\(^25\) This aspect of the 2020 rule is conceived as a targeted prohibition against a fiduciary’s consideration of ESG factors, but as commenters point out, it also fosters confusion in other aspects of the rule, in part because it too is “driven by a mischaracterization by the DOL of the pecuniary nature of ESG factors.”\(^26\)

b. Proxy Voting Rule

The second aspect of the DOL’s 2020 rule amendments that warrants urgent revision relates to proxy voting. Specifically, the 2020 Proxy Voting Rule, published in the Federal Register on December 16, 2020, amended ERISA’s investment duties regulation to establish regulatory standards for the obligations of plan fiduciaries under ERISA when voting proxies and exercising other shareholder rights.\(^27\) The preamble of the Proxy Voting Rule expressed the (mistaken) view that environmental and social shareholder proposals have little bearing on share value or other relation to plan financial interests.\(^28\)

Like the Fiduciary Factors Rule, the Proxy Voting Rule was ostensibly intended to provide clarity,\(^29\) but in actuality was another confusing attempt to single out and stigmatize ESG factors, on policy grounds, and to create new legal liability and other impediments that would discourage and prevent plan fiduciaries from considering ESG factors in the exercise of their responsibilities. And,

\(^{24}\) Final Rule, Financial Factors in Selecting Plan Investments, at 72884.

\(^{25}\) Proposed Rule, Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, at 57272.


\(^{27}\) See Final Rule, Fiduciary Duties Regarding Proxy Voting and Shareholder Rights.

\(^{28}\) See Id., at 81658, (According to the prior rule’s preamble, the regulation was “undertaken, in part, to confirm that, when exercising shareholder rights, ERISA plan fiduciaries may not subordinate the interests of plan participants and beneficiaries in receiving financial benefits under a plan to non-pecuniary objectives.”

\(^{29}\) According to the rule, the DOL at the time was concerned that sub-regulatory guidance had resulted in a misplaced belief among some stakeholders that fiduciaries must always vote proxies where permitted, subject to limited exceptions. Thus, a key piece of language from this rule stated, “the fiduciary duty to manage shareholder rights appurtenant to shares of stock does not require the voting of every proxy or the exercise of every shareholder right.”
like the 2020 Financial Factors Rule, the unfortunate and predictable result was to cast a chill over all manner of consideration of ESG factors and create more uncertainty for ERISA fiduciaries.30

c. Unnecessary and Confusing Results of Previous Rules

Taken separately and together, the added requirements and prohibitions contained in the 2020 Fiduciary Factors and Proxy Voting rules risk engendering significant uncertainties and potential liabilities for plan fiduciaries. In effect, the 2020 Rules take what previously, and under decades of Department guidance, would have been a reasonable exercise of prudence and loyalty in investment decision making and proxy voting, and turn it on its head.31

It should be no surprise then that the confusing and contradictory rule text has proven to have a damaging and chilling effect on plan fiduciaries’ ability to prudently analyze relevant ESG-related factors, knowing that they might later be deemed “non-pecuniary,” and/or directed at collateral benefits, thereby triggering the rule’s labyrinthine documentation and analysis requirements. Several commenters responding to the rule’s proposal, in 2020, called attention to its contradictions, and noted the likely confusion and cost their adoption would cause.32

However, the most troubling aspect of the 2020 Rules is that they create confusion, cost, and inefficiency precisely because they seek to do so. As evidenced by media coverage following the 2020 proposals, and as pointed out by many that formally commented on them, it requires no stretch of the imagination for the Department to conclude that this was the intention.33 And, to the extent the 2020 Rules were designed to create difficulty, cost, and inefficiency – that is, to throw a wrench in the gears for consideration of ESG factors by plan fiduciaries, and to do so for primarily policy and political reasons – the 2020 rules were not only ill-advised and reckless, but also likely unlawful.34

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32 See, e.g., Americans for Financial Reform Education Fund, Comment Letter Re: Re: Financial Factors in Selecting Plan Investments, at 2 (July 20, 2020), https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00730.pdf, (“The discussion in the Proposal presents an inconsistent view of whether ESG factors may be considered economically material, or, pecuniary[,]’ further observing that, “as a result [of the confusion caused], ERISA fiduciaries will choose to ignore even material ESG factors because they are concerned that the DOL will disagree with their determination and they will be subject to enforcement action.”).


34 See, e.g., Max Schanzbach and Robert Sítkoff, Comment Letter Re: Financial Factors in Selecting Plan Investments Proposed Regulation, at 3 (July 30, 2020), https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB95/00693.pdf, (“[T]he Proposal and accompanying commentary could be read to suggest that all manner of ESG investing is inherently suspect, presumably on fiduciary loyalty grounds, and therefore that ESG investing by an ERISA trustee or other fiduciary is always subject to enhanced scrutiny that requires extra process relative to other types of kinds of investment strategies. Such a position is inconsistent with law and sound policy.”)
2. **What the Proposed Amendments Accomplish**

As described in the current proposal’s preamble, on January 20, 2021, President Biden signed Executive Order 13990 (E.O. 13990), titled "Protecting Public Health and the Environment and Restoring Science to Tackle the Climate Crisis." This Executive Order “sets forth the policy of the Administration to listen to the science; improve public health and protect our environment; bolster resilience to the impacts of climate change; and prioritize both environmental justice and the creation of the well-paying union jobs necessary to deliver on these goals.”

In response to this broad directive, on March 10, 2021, the Department began a re-examination of certain prior regulations that deemed incompatible, the result being that the Department stated that it would not enforce the 2020 rules relating to prudence and loyalty in ERISA plan administration and proxy voting, as had been issued by the prior administration. Later, on May 20, 2021, President Biden signed Executive Order 14030, titled "Executive Order on Climate-Related Financial Risk,” Section 4 of which directs the Secretary of Labor to consider publishing a proposed rule to suspend, revise, or rescind the two above-mentioned rules. On October 14, 2021, the Department undertook that request.

**A. Settling the Confusion Created by the Prior Rules**

The preamble of the Proposed Amendments goes into significant detail regarding the Department’s previous non-regulatory guidance covering ERISA plan fiduciaries’ decision making. The intent of this discussion is to offer clarification where the previous 2020 Rules had created uncertainty. As stated in the preamble, “rather than provide clarity, some aspects of the current regulation instead may have created further uncertainty surrounding whether a fiduciary under ERISA may consider ESG and other factors in making investment and proxy voting decisions that the fiduciary reasonably believes will benefit the plan and its participants and beneficiaries.” The Proposed Amendments appropriately replace and revise both the Financial Factors Rule and the Proxy Voting Rule to establish an ERISA framework that explicitly allows and encourages fiduciaries to appropriately consider all relevant factors in both investment decision making and proxy voting.

CFA commends the Department for developing and publishing the Proposed Amendments and agrees with the Department’s reasoning and recommendations.

**a. The Rule Proposal Appropriately Allows Incorporation of ESG Factors into ERISA’s Duties of Prudence and Loyalty**

Specifically, the Proposed Amendments provide that ESG considerations can be seen as relevant to, if not inherent in, the fiduciary duties of prudence and loyalty of plan fiduciaries, in that “consideration of the projected return of the portfolio relative to the funding objectives of the plan may often require an evaluation of the economic effects of climate change and other ESG factors on the particular investment or investment course of action.” Appropriately, the current rule proposal includes ESG and other related factors in and among the material economic factors that a plan

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37 *Id.* at 57276.
fiduciary may consider when making investment decisions, and proposes to remove the “pecuniary factors” binary that was a root cause of the confusion explained above. CFA wholeheartedly supports these aspects of the proposal.

One element of Proposed Amendments to the regulations includes the addition of a non-exhaustive list of possible ESG factors that a plan fiduciary may consider when making investment decisions. The Department has specifically requested input from commenters on whether this approach is the preferred tack, and “solicits comments on whether other or fewer examples (see paragraph (b)(4)) would be helpful to avoid regulatory bias.” In response, we offer support for the proposal’s inclusion of the list of enumerated examples in the rule text. These examples are likely to be helpful for practitioners and plan participants alike, and we see their inclusion as offering potential benefits without a clearly discernible downside.

b. The Rule Proposal Appropriately Revives the “All Things Being Equal” Test

As previously noted, the 2020 rule singled out and created burdens specifically for investments providing collateral benefits, which many rightfully perceived as targeting ESG related investment considerations. The Proposed Amendments revive the “tie-breaker” standard (all things being equal) and eliminate the 2020 regulation’s specific documentation requirements when a fiduciary incorporates ESG factors into investment decision making. Under the revived tie-breaker scenario, a fiduciary is not prohibited from selecting the investment, or investment course of action, based on collateral benefits. This standard appropriately allows plan fiduciaries to incorporate relevant ESG-related information into their decision-making process, while remaining steadfastly bound to ERISA’s longstanding and well-understood duty of loyalty that dictates that a fiduciary cannot accept expected reduced returns or greater risks by choosing to prioritize these collateral benefits instead.

While the Proposed Amendment’s “equally serve the financial interests of the plan” language is an improvement on the term “indistinguishable,” CFA is concerned that even the Proposed Amendments may be too narrow in this regard. The issue is not how closely two or more investments resemble one another, but whether they are each the product of a fiduciary’s prudent decision-making process. Fiduciaries should receive equal deference if their investment choice is the product of a prudent decision-making process. Thus, we tend to agree that it is appropriate for the collateral benefit provision in the final rule to focus on whether investments are equally prudent (i.e., the output of a prudent fiduciary process), rather than on an analysis of the equivalence of their financial characteristics.

c. The Rule Proposal Clarifies that Default Investment Alternatives May Incorporate Relevant Climate and Other ESG Factors

We endorse the Department’s rescission of the prohibition on certain investment alternatives being used as a default investment: the Qualified Default Investment Alternative (QDIA). A fiduciary’s responsibilities of prudence and loyalty are no different for a QDIA than for other plan investments, and if a participant does not wish to invest in the QDIA, they can select another investment vehicle. Any other approach would, as the Department observes in the preamble, “only serve to harm participants by depriving them of otherwise financially prudent options as QDIAs.”

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38 Id. at 57277.
also approve of the rule proposal’s requirement that any QDIA that does incorporate ESG factors into its strategy also provide relevant disclosures of that fact to plan participants.

d. The Rule Proposal Restores Fiduciary Authority to Make Prudent Decisions in Proxy Voting

CFA strongly supports the ability of plan fiduciaries to exercise their judgment to vote proxies in the best interest of plan participants and beneficiaries. ERISA’s fiduciary duties require “active ownership,” including informed proxy voting on shareholder proposals affecting companies owned by the plan.39 Fiduciaries must be given discretion to vote on these proposals, exercising critical oversight that has been shown to reduce downside risk. We support the current rule proposal’s revisions to the 2020 rule, rightfully restoring a fiduciary’s ability to vote on behalf of funds on an array of important issues, including climate change.

CFA also supports the removal of the “fiduciaries don’t have to vote” language that was included in the 2020 Proxy Voting Rule. As with other aspects of the 2020 rules, this language creates more uncertainty than clarity for fiduciaries. In our view, proxies should be voted as part of the process of managing the plan’s investment in company stock unless a responsible plan fiduciary determines voting proxies may not be in the plan’s best interest (e.g., if there are significant costs or efforts associated with voting), and that rather than just abstaining, fiduciaries should be prudent in incurring expenses to make proxy decisions. Such an approach rightfully gives fiduciaries the flexibility to vote on matters relating to ESG proposals when they prudently determine that it is in plan beneficiaries’ best interest to do so.

Further, the Proposed Amendments appropriately eliminate the 2020 Proxy Voting Rule’s added obligations to maintain records on proxy voting activities and other exercises of shareholder rights and removes two problematic safe harbors contained in the current regulation.40

3. Conclusion

The severe implications climate change, and the resultant economic, geopolitical, social, ecological, physical, and transitional risks, present an increasingly complex landscape that fiduciaries must be prepared to navigate. The gradual transition to a carbon net-zero economy will require nearly every industry to be redesigned and rebuilt, resulting in many stranded assets. However, at the same time, the transition will present major wealth and job creation opportunities. The Proposed Amendments that the Department has put forward clear the way for fiduciaries to offer retirement investors access to these investment opportunities, the benefits of which other institutional investors are now pursuing and to which retirement savers say they want access.

39 See Joseph Adams and Susan Peters Schaefer, New ERISA Proxy-Voting Guidance from the DOL, (Oct. 1, 2020), https://www.winston.com/en/benefits-blast/new-erisa-proxy-voting-guidance-from-the-dol.html, (“Prior to this latest guidance, it has been generally accepted that a fiduciary’s responsibility to manage plan assets includes the responsibility to exercise shareholder rights associated with the plan’s investments, such as proxy voting, unless it would result in the expenditures of plan assets out of proportion to the potential benefits for the plan.”).

40 The safe harbors include a policy of only voting on matters of deemed corporate significance and a policy of refraining from voting when the plan’s holdings are minimal relative to its total investment holdings.
Finally, and perhaps most importantly, adoption by the DOL of the Proposed Amendments will clear the way for fiduciaries to consider all available information in seeking to best serve the interests of the plan’s participants and beneficiaries. It will eliminate onerous and intentionally unworkable requirements and restore fiduciaries’ authority to exercise shareholder rights in the best interests of plan beneficiaries. And it will mark a return to ERISA standards that have served American workers well in the nearly 50 years since ERISA became law.

Respectfully submitted,

Dylan Bruce
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Consumer Federation of America

cc: Honorable Marty Walsh, Secretary of Labor