

Fact Sheet

U.S. Department of Labor
Employee Benefits Security Administration
June 23, 2020

Notice of Proposed Rulemaking on Financial Factors in Selecting Plan Investments Amending “Investment duties” Regulation at 29 CFR 2550.404a-1

On June 23, 2020, the U.S. Department of Labor (Department) released a proposal to amend certain provisions of the “Investment duties” regulation at 29 CFR 2550.404a-1, which is applicable to plans covered by the Employee Retirement Income Security Act (ERISA), in order to reiterate and codify long-established principles of fiduciary standards for selecting and monitoring investments.

Background

- The Department has been asked periodically over the last 30 years to consider the application of the fiduciary duties of prudence and exclusive purpose under ERISA section 404(a)(1)(A) and (B) to pension plan investments selected because of the non-pecuniary objectives such as those relating to environment, social and public policy goals they may further.
- The Department’s first comprehensive guidance in this area was Interpretive Bulletin 94–1 (IB 94–1). There, the term was “economically targeted investments” (ETIs). IB 94–1 stated that ETI investments could be consistent with ERISA’s fiduciary obligations, but that fiduciaries need to make sure that an ETI investment has an expected rate of return that is commensurate to rates of return of alternative investments with similar risk characteristics that are available to the plan, and that the investment is otherwise an appropriate investment for the plan in terms of such factors as diversification and the investment policy of the plan. Some commentators have referred to this as the “all things being equal” test or the “tie-breaker” standard. The preamble to IB 94-1 explained that when competing investments serve the plan’s economic interests equally well, plan fiduciaries can use such non-pecuniary considerations as the deciding factor for an investment decision.
- The Department’s guidance in this area then went through an iterative process. In 2008, the Department replaced IB 94–1 with Interpretive Bulletin 2008–1 (IB 2008-01). In 2015, the Department replaced IB 2008–1 with Interpretive Bulletin 2015–01 (IB 2015-01).
- Each Interpretive Bulletin has emphasized that the focus of plan fiduciaries must be on the plan’s financial returns and that furthering the interest of plan participants and beneficiaries in financial benefits under the plan must be paramount. Each Interpretive Bulletin, while restating the “all things being equal” test, also cautioned that fiduciaries violate ERISA if they accept expected reduced returns or greater risks to secure social, environmental, or other public policy goals.

- IB 2015–01 also explained that “if a fiduciary prudently determines that an investment is appropriate based solely on economic considerations, including those that may derive from ESG factors, the fiduciary may make the investment without regard to any collateral benefits the investment may also promote.” In such situations, the issues are themselves appropriate economic considerations, and thus may be considered by a prudent fiduciary along with other relevant economic factors to evaluate the risk and return profiles of different investments. In other words, in these instances the factors are not “tie-breakers” but pecuniary (or “risk-return”) factors affecting the economic merits of the investment.

Overview of Proposed Amendments to “Investment duties” Regulation

- The purpose of this Notice of Proposed Rulemaking (NPRM) is to invite public comments on a proposal to codify a regulatory structure for these principles in the Department’s current “Investment duties” regulation at 29 CFR 2550.404a-1.
- The Department’s aim is to assist ERISA fiduciaries by establishing clear regulatory guideposts for plan fiduciaries in light of recent trends involving ESG investing that the Department is concerned may lead ERISA plan fiduciaries to choose investments or investment courses of action to promote environmental, social, and public policy goals unrelated to the interests of plan participants and beneficiaries in financial benefits from the plan and expose plan participants and beneficiaries to inappropriate investment risks.
- The proposal retains the core principles in the current regulation that sets forth requirements for satisfying the prudence duty under ERISA section 404(a)(1)(B) when deciding on plan investments and investment courses of action.
- The proposal makes five core additions to the regulation:
 1. New regulatory text to codify the Department’s longstanding position articulated in interpretive bulletins (IBs) published in 1994, 2008, and 2015 that ERISA requires plan fiduciaries to select investments and investment courses of action based on financial considerations relevant to the risk-adjusted economic value of a particular investment or investment course of action.
 2. An express regulatory provision stating that compliance with the exclusive purpose (loyalty) duty in ERISA section 404(a)(1)(A) prohibits fiduciaries from subordinating the interests of plan participants and beneficiaries in retirement income and financial benefits under the plan to non-pecuniary goals.
 3. A new provision that requires fiduciaries to consider other available investments to meet their prudence and loyalty duties under ERISA in furthering the purposes of the plan.
 4. The proposal acknowledges that ESG factors can be pecuniary factors, but only if they present economic risks or opportunities that qualified investment professionals would treat as material economic considerations under generally accepted investment theories. New regulatory text sets forth required investment analysis and documentation requirements in the rare circumstances when fiduciaries are choosing among economically “indistinguishable” investments (related to the so-called “tiebreaker rule” in the 1994, 2008, and 2015 IBs). The documentation requirement is intended to provide a safeguard against the incentive for fiduciaries to improperly find economic equivalence and make decisions based on non-pecuniary benefits without a proper analysis and

evaluation. Fiduciaries already commonly document and maintain records about their investment selections. The provision in the proposal would make that general practice required where a fiduciary determines that alternative investment options are economically indistinguishable and where the fiduciary chooses one of the investments on the basis of a non-pecuniary factor.

5. A new provision on selecting designated investment alternatives for 401(k)-type plans. The proposal states the Department's view that the prudence and loyalty standards set forth in ERISA apply to a fiduciary's selection of an investment alternative to be offered to plan participants and beneficiaries in an individual account plan (commonly referred to as a 401(k)-type plan). The proposal describes the requirements for the selection of investment alternatives for such plans that purport to pursue one or more environmental, social, and corporate governance-oriented objectives in their investment mandates or that include such parameters in the fund name.
- Some plans would have to modify their processes for selecting and monitoring investments. The rule may impose costs on plans whose current documentation and recordkeeping are insufficient to meet the new requirement. Plans would need to document selections in some circumstances where a fiduciary concludes the alternative investment options are economically indistinguishable. The Department does not expect this requirement to impose a significant cost as these situations are rare. Overall, the proposed rule would assist fiduciaries in carrying out their responsibilities, while promoting the financial interests of current and future retirees.

Public Comment Period

- The proposal includes a 30-day comment period. The Department invites comments from interested persons on all facets of the proposed rule. Commenters are free to express their views not only on the specific provisions of the proposal as set forth in this document, but on any issues germane to the subject matter of the proposal.
- The proposal includes instructions on submitting comments to www.reg.gov.

Contact Information

For questions about the proposed rulemaking, contact EBSA's Office of Regulations and Interpretations at 202-693-8500.