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VIA ELECTRONIC FILING

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,

Americans for Financial Reform Education Fund, the Sierra Club, and 10 undersigned organizations write to offer our strong support of the Department's proposed rule, *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights* ("the Proposal"). Under the Employee Retirement Income Security Act of 1974, as amended (ERISA) fiduciaries should be able to prudently choose investments that provide long-term benefits, yield healthy contributions to retirement plans, enhance—rather than undermine—workers' share of earnings, and promote a healthy and livable planet, fair working conditions, and a racially just and democratic society while honoring their fiduciary duty.

In addition to supporting the Proposal, we call for the Department in future rulemakings, guidances and other agency actions to set a minimum standard for fiduciaries' consideration of systemic risks to retirement savings, and to require that participant-directed plans offer a sustainable investing option addressing systemic risks among a prudently constructed lineup of funds offered to participants. As discussed below, ERISA fiduciaries have an obligation to address credible systemic threats to the long-term performance of private retirement plans.

I. Restoring fiduciaries' discretion is critical in light of the impact of climate change and other ESG factors on investment returns

We strongly support restoring fiduciaries' discretion to consider climate change and other environmental, social and governance (ESG) factors in their investments, engagement and voting. The Proposal would remove costly barriers and arbitrary prohibitions on ESG investments and clarify how ERISA fiduciaries can and should consider economically relevant ESG factors in their investment practices.

There is a substantial and growing body of evidence[1] that climate change, racial and economic injustice and other ESG factors affect investment returns and corporate financial performance across many sectors, and will be particularly important to consider for typical retirement savers with long investment horizons and broad ownership of the market. Investors are pouring money into sustainable investments[2] and being rewarded with higher returns, but so far ERISA savers have largely missed out on the substantial economic benefits. This must change. Sustainable investment products and ESG integration are value-added components of modern investing and must be readily available to all ERISA fiduciaries and participants, and encouraged by the Department.

The Proposal rightly states that ESG factors are often economically relevant and in many cases should be considered by a prudent fiduciary

In the Proposal, the Department recognizes the need "to craft rules that better recognize the role that ESG integration can play in evaluation and management of plan investments."[3] The Trump-era rules singled out ESG factors for heightened scrutiny and special documentation requirements, warning that fiduciaries should avoid "too hastily" concluding that ESG factors are economically relevant.[4] The Proposal rightly recognizes that the Trump-era rules "may deter fiduciaries from taking steps that other marketplace investors would take in enhancing investment value and performance, or improving investment portfolio resilience."[5]

We support the Department's overarching conclusion about its Proposal: "The proposal makes clear that climate change and other ESG factors are often material and that in many instances fiduciaries should consider climate change and other ESG factors in the assessment of investment risks and returns."[6]

Likewise, we endorse the Department's rescission of the prohibition on certain ESG-related investment alternatives from being used as a default investment (the Qualified Default Investment Alternative, or QDIA). As the Department states, this only served "to harm participants by depriving them of otherwise financially prudent options as QDIAs."

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[1] A recent review of over 1000 studies published in the last five years found that a higher ESG rating for an individual company was associated with higher corporate financial performance (e.g., return on equity or assets, or stock performance) in 58 percent of the studies, and a higher ESG rating for a portfolio of stocks was associated with better investment returns in 59 percent of the studies. For low carbon ratings in particular, the climate-friendly companies and portfolios performed better 57 percent and 65 percent of the time, respectively;
https://www.stern.nyu.edu/sites/default/files/assets/documents/ESG%20Paper%20Aug%202021.pdf. See also "ESG and Financial Performance: Aggregated Evidence from More Than 2000 Empirical Studies," https://www.tandfonline.com/doi/full/10.1080/20430795.2015.1118917.
[2]See E.g., "A Broken Record: Flows for U.S. Sustainable Funds Again Reach New Heights" https://www.morningstar.com/articles/1019195/a-broken-record-flows-for-us-sustainable-funds-again-reach-new-heights
[3] RIN 1210-AC03, Proposed Rule Preamble
[4] 85 FR 72848, 72859 (Nov. 13, 2020)
[5] RIN 1210-AC03, Proposed Rule Preamble
[6] *Ibid*.

The Proposal's list of potentially relevant ESG factors is incomplete. The final rule should encourage fiduciaries to consider a broader range of additional ESG factors.

The Proposal deviates from the typical "ESG" classification when it introduces a list of factors that "might" be economically relevant to the risk-return analysis and therefore should be considered. This deviation from the typical ESG classification might confuse fiduciaries who are interested in incorporating ESG factors into their investment practices and could bias consideration towards those particular factors that made the list while discouraging consideration of other ESG factors that are economically relevant or may become so.

Notably, the shift from a tranche of "environmental" factors to "climate change" factors could bias against the consideration of important issues like environmental justice; respect for Indigenous rights; responsible stewardship of water and other natural resources; ecological and regional economic impacts of corporate activities in the global forest, food and land sector; and chemicals, plastics, and air toxics pollution, for example. The Proposal mentions environmental regulations in the "Governance" tranche ("avoidance of criminal liability and compliance with labor, employment, environmental, tax, and other applicable laws and regulations")—which can be substantial[7]—but this excludes the economic relevance of environmental issues that may not result in criminal liability or regulatory enforcement. Environmental justice factors are increasingly a market and credit risk;[8] consider the significant Indigenous-led opposition to pipeline projects like the Dakota Access Pipeline and Enbridge's Line 3 that raised the cost of capital for these projects.

The Proposal also omits mention of economically relevant factors related to corporate impact on racial and economic inequality, as well as political activity, which are also increasingly market and credit risks.[9] The final rule should include a broad range of these factors as examples and also make explicitly clear that fiduciaries have full discretion to assess and consider additional ESG factors as needed.

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[7] See E.g.,
https://archive.epa.gov/epapages/newsroom_archive/newsreleases/2520f12f7372fe1d85257694005ab7a7.html; www.cbsnews.com/news/duke-energy-fined-102-million-in-coal-ash-spill/

[8] See E.g.,
https://abcnews.go.com/US/previously-proposed-route-dakota-access-pipeline-rejected/story?id=43274356;
www.bloomberg.com/news/articles/2021-07-01/how-climate-activists-pressure-banks-to-defund-the-oil-industry?sref=CZcaXeEr;
https://thehill.com/policy/energy-environment/510748-court-cancels-shutdown-of-dakota-access-pipeline;
https://mspmag.com/arts-and-culture/how-the-line-3-fight-will-continue/;
www.ran.org/wp-content/uploads/2020/12/RAN-Briefing_Line3_KXL.pdf;
www.bloomberg.com/news/articles/2020-07-28/nordic-fund-divests-45-million-from-jbs-on-amazon-concernswww.morningstar.com/articles/1065414/cop26-deforestation-pledge-will-empower-companies-investors-to-attack-supply-chain-emissions

[9] See E.g,
https://fortune.com/2021/07/21/uber-lyft-drivers-stage-nationwide-strike-right-to-unionize-better-pay/;
www.nbcnews.com/business/business-news/fired-interrogated-disciplined-amazon-warehouse-organizers-allege-year-retaliation-n1262367;
www.nytimes.com/2020/07/28/magazine/pollution-philadelphia-black-americans.html;
https://endpolicesurveillance.com/documents/2021-05-03-Motion-for-Leave-to-File-Brief-as-Amici-Curiae-with-Ex.-A-Amicus-Brief-attached.pdf;

II. The Department should set a minimum standard for consideration of systemic risks to retirement savings.

Although restoring fiduciaries' flexibility to consider ESG factors is an important step, it is not enough to ensure that fiduciaries undertake their ERISA responsibilities with respect to systemic risks to retirement savings. Climate change,[10] racial and economic inequality[11] and threats to democracy[12] are critically important systemic risks that are sometimes ignored in the pursuit of short-term returns. In future rulemakings the Department should set a minimum standard for management of these and any other systemic risks that pose a significant threat to the economy, the financial system and the long-term economic security of plan participants.

One of the key measures of whether a fiduciary is carrying out its ERISA duties of prudence and loyalty to participants and beneficiaries is whether it is properly diversifying its investments.[13] Whenever a plan fiduciary ignores credible long-term systemic risks, it is at odds with this core ERISA requirement. By adhering to minimum standards for considering systemic risks in investments, engagement and voting, fiduciaries can directly bolster long-term retirement income in ways that also confer socioeconomic benefits that further improve retirees' economic well being.

The Department has long made it clear that in enforcing ERISA, it will not judge fiduciaries on the results they achieve but rather by their processes. We support this approach. But the conditions for decision making, and the best practices of fiduciaries in responding to those conditions, have evolved considerably since ERISA's enactment. What might have been a reasonable process in 1974 is no longer today. The global economic meltdown in 2008 provided important lessons about the enormous, unnecessary harm suffered by retirees and workers when asset managers and other financial gatekeepers ignore systemic risks to their retirement savings.

For systemic ESG issues that threaten retirees' financial health over the long term, the Department should engage in a rulemaking to set minimum standards. In addition, the Department can accomplish a great deal by simply providing informal guidance on the process of integrating ESG factors into investment practices. For example, the Department could develop educational materials and convene workshops providing instructions and

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[10] See E.g., https://www.whitehouse.gov/wp-content/uploads/2021/10/Climate-Finance-Report.pdf ("Climate change poses serious and systemic risks to the U.S. economy and financial system."); https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf

[11] See E.g., https://www.pionline.com/sponsored-content/facing-hard-truths-material-risk-rising-inequality; https://www.chicagobooth.edu/review/racial-inequality-business-risk

[12] See E.g., https://www.v-dem.net/media/filer_public/d3/f1/d3f1799a-5d50-4653-8440-1e9547144c0f/wp_111_final.pdf

[13] See §1104(a)(1)(C): "A fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries… by diversifying the investments of the plan so as to minimize the risk of large losses…"

encouragement on development of Sustainable Investment Policies.[14] It could highlight the benefits of investing in and providing options for funds managed by individuals of diverse racial, ethnic and economic background and diverse gender orientation. Finally, it could provide a standardized format for fiduciaries to disclose to the Department, plan participants and beneficiaries how they integrate ESG factors into their investment practices.

III. Participant-directed plans should be required to include at least one ESG option that addresses climate and other ESG systemic risks among a prudently constructed lineup of funds offered to participants.

Recent years have seen an incredible rise in investor demand for ESG products[15] and a recent survey found the majority of investors' want to be Paris-aligned.[16] Yet fewer than 3 percent of defined contribution plans offer a climate-friendly investment option.[17] The vast majority of the 140 million Americans who rely on ERISA plans to save for retirement do not even have the option of investing with companies best oriented toward a climate-safe future.

To correct this, the Department must require that participant-directed plans offer at least one option that addresses climate and other systemic ESG risks as part of a prudently constructed lineup of funds, an essential step in ensuring that fiduciaries satisfy their duty of loyalty to plan participants and beneficiaries. Further, the Department should ensure that plans provide options of funds managed by individuals of diverse racial, ethnic and economic background and diverse gender orientation.

There are a number of market rate ESG funds that have performed as well or better than their non-ESG counterparts over the past decade, and there is no credible reason that a fiduciary would be unable to find such a fund addressing systemic ESG risks to offer to their participants that meets ERISA criteria.[18] Climate science tells us systemic climate risk will continue to grow over the long investment horizons of many retirement savers, at least through 2050. Thus fiduciaries should be required to offer an investment option that credibly addresses climate risk,

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[14] See E.g., www.unpri.org/an-introduction-to-responsible-investment/an-introduction-to-responsible-investment-policy-structure-and-process/4917.article

[15] See E.g., www.investopedia.com/demand-for-esg-investments-soars-emerging-from-covid-19-pandemic-5193532

[16] See E.g., www.barrons.com/articles/future-returns-wealthy-see-a-role-in-investing-to-tackle-climate-change-01632255522

[17] https://www.napa-net.org/news-info/daily-news/could-esg-options-boost-401k-participation

[18] The SEC will likely soon provide more clarity regarding definitions, disclosures, and criteria for different types of sustainable funds, and the Department should incorporate their work into future actions. Recent examinations of major asset managers' ESG funds have revealed that a portion of some of the largest asset managers' funds include investments in companies that have had serious negative impacts related to racial, economic, and environmental injustices. In order to adequately address the systemic risks and economic harms of investments in extractive industries, the Department should follow developments and provide guidance to fiduciaries on best practices for examining these issues. See E.g., www.bloomberg.com/graphics/2021-what-is-esg-investing-msci-ratings-focus-on-corporate-bottom-line/?sref=f7rH2jWS (*"A Bloomberg Intelligence analysis earlier this year showed that BlackRock's ESG Aware holds a portfolio that closely tracks both the S&P 500 and BlackRock's own top-selling S&P 500 fund, with two notable exceptions: The ESG fund has a "sustainable" label thanks to MSCI, and it's more heavily weighted in 12 fossil fuel stocks than the actual S&P 500.")*

an action which is clearly in the financial interests and desires of their participants. Organizations like Fossil Free Funds provide information and investing tools for fiduciaries and participants to search for the most climate-friendly investment options.[19]

An ESG option requirement for participant-directed plans would not significantly raise compliance costs. Asset managers already offer such lineups that include ESG options, and existing ERISA plans could comply simply by adding an option addressing systemic ESG risks to their current lineup, with no need to move money between funds. Until such options are universally available in participant-directed plans, workers and retirees will remain deprived of investment strategies that meet their needs.

We thank the Department for this important proposal and we look forward to further agency actions that will encourage and standardize sustainable investing processes within ERISA plans, to the benefit of workers and retirees.

Respectfully submitted,

Americans for Financial Reform Education Fund, the Sierra Club and Sierra Club Foundation

350.org
Action Center on Race and the Economy
Better Markets
Center for International and Environmental Law
Evergreen Action
Friends of the Earth U.S.
Positive Money U.S.
Private Equity Stakeholder Project
Public Citizen
Rainforest Action Network
Revolving Door Project
Stand.earth
The Communications Workers of America

Cc: Honorable Martin J. Walsh, Secretary of Labor

[19] https://fossilfreefunds.org