July 29, 2020

Office of Regulations and Interpretations
Employee Benefits Security Administration
Department of Labor
Room N-5655
200 Constitution Avenue NW
Washington, DC 20210

Dear Director Canary,

Re: Financial Factors in Selecting Plan Investments: Proposed Regulation (RIN 1210-AB95)

The Canadian Coalition for Good Governance (CCGG) welcomes the opportunity to comment on the notice of proposed rulemaking entitled "Financial Factors in Selecting Plan Investments" ("Proposal"). CCGG encourages the Department of Labor not to move forward with the Proposal.

CCGG's members are Canadian institutional investors that together manage approximately CDN $4.5 trillion in assets on behalf of pension funds, mutual fund unit holders, and other institutional and individual investors. A list of our members is attached to this letter as Appendix A. CCGG promotes good governance practices in Canadian public companies in order to best align the interests of boards and management with those of their shareholders. We also seek to improve Canada's regulatory framework to strengthen the efficiency and effectiveness of the Canadian capital markets. Because a significant portion of our members' assets are invested in U.S. companies, our members also have an interest in the U.S. capital markets and their regulation.

CCGG believes that good governance practices underpin a company's ability to effectively address risks of all kinds and create long-term value for shareholders. CCGG further believes that integrating E&S into corporate governance is a part of the fiduciary duty of investors. In 2018, CCGG released its publication *The Directors' E&S Guidebook* (the "Guidebook") in response to growing shareholder emphasis on environmental and social (E&S) factors. The Guidebook approaches E&S issues from a governance perspective and speaks specifically to the board's oversight of E&S factors that are, or may become, material to a company's long-term value. It also addresses the disclosure of those factors to investors.

CCGG believes that the Proposal misconstrues ESG integration and would lead to confusion and costs for retirement plan fiduciaries. This appears to be, in part, because of a failure to distinguish between ESG integration and economically targeted investing (ETI). ESG integration is the consideration of material ESG factors as part of a prudent investment management process which takes into account both risks and expected financial performance outcomes. ETIs are investments that aim to provide financial returns as well as collateral, non-financial benefits. For example, ETIs often advertise job creation or climate impact as goals of the investment. We, therefore, urge you to allow the existing guidance to remain in effect and not move forward with a final rule.

ESG Integration

The Proposal states that an ERISA fiduciary has fulfilled its obligations if they have "selected investments and/or investment courses of action based solely on pecuniary factors." It goes on to state that, "ESG factors and other similar factors may be economic considerations." There is now a body of research that makes clear that ESG factors are material investment considerations that have the potential to impact analysis of risk and expected financial performance[1]. ESG integration is increasingly being used by institutional investors to inform investment decisions driven by expected financial returns. This is the core rationale underpinning the governance-based E&S oversight and disclosure recommendations to corporate boards in CCGG's Guidebook and why investors see integrating E&S into corporate governance considerations as part of their fiduciary duty.

A policy by the DOL that simply clarifies that fiduciaries must integrate material factors into their investment process and that ESG factors may be material would be appropriate. Such a policy would be consistent with the approach taken in many global stewardship codes including CCGG's Stewardship Principles, the UK Stewardship Code and the ICGN Global Stewardship Principles[2]. We are concerned, however, that the remaining components of the Proposal create confusion and could cause fiduciaries to believe they are not permitted to consider material ESG factors in their investment analysis. This has the potential to create significant challenges for international institutional investors, hired by ERISA plans to manage plan assets, who have integrated ESG factors into their investment processes for all of their investments, including to

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[1] For an example of such research conducted by MSCI, see: Giese, G., L. Lee, D. Melas, Z. Nagy, and L. Nishikawa. 2019. "Foundations of ESG Investing: How ESG Affects Equity, Valuation, Risk, and Performance" *The Journal of Portfolio Management IPR Journals* 45(5): 1-17 [jpm.iprjournals.com]

[2] See for example, CCGG's Stewardship Principles, May 2020 Principle 7 – Focusing on long-term sustainable value: "Institutional investors should make sure they understand the risks and opportunities associated with material sustainability factors, including environmental, social and governance issues, and integrate them into their investment and stewardship activities"; and 2020 UK Stewardship Code, Principle 7 – "Signatories systemically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfill their responsibilities". Also see 2016 International Corporate Governance Network Global Stewardship Principles, Principle 6 "Promoting long-term value creation and integration of environmental, social and governance (ESG) factors".

maximize risk adjusted investment returns. A perceived prohibition by the Department on considering material ESG factors in investment analysis would put institutional investors in the untenable situation of putting fulfilment of their fiduciary duties and stewardship obligations into potential conflict with the Department's rules should it implement the Proposal.

Inconsistent with requirements of other jurisdictions

CCGG believes that the Proposal places ERISA fiduciaries out of step with evolving regulatory requirements and guidance in other jurisdictions which expect pension fiduciaries to state whether ESG factors are incorporated into the plan's investment policies and procedures and, if so, how those factors are incorporated.

In Ontario, the province which is the primary capital markets jurisdiction in Canada, such requirements have been in place since 2016[3]. In a June 2019 expert panel report on sustainable finance delivered to the Canadian government, one of the panel's recommendations was that similar requirements be included in national pension regulation and other provincial regulators be encouraged to introduce similar disclosure requirements in the specific context of climate change[4].

Similarly, as of October 2019, The Pensions Regulator (TPR) in the UK has required trustees of defined contribution pension plans to include in their statements of investment principle (SIP) their "policies in relation to financially material considerations (*including those relating to environmental, social and governance (ESG) considerations*….), over the appropriate time horizon of the investments including how those considerations are taken into account in the selection, retention and realization of investments"[5]. Notably, the TPR guidance expressly acknowledges that ESG considerations may be financially material and where this is the case they must be included in the SIP.

The "all else being equal test"

CCGG is concerned that the Proposal creates new burdens for fiduciaries using the "all else being equal test" that would lead to unnecessary costs for plan participants. It also creates confusion about what activities the DOL is attempting to regulate.

Under the "all else being equal test," which has been in place since 1994, fiduciaries may select an investment that provides collateral benefits only after they have determined that the risk and return profile of that investment option is substantially similar to that of competing options that would meet the financial needs of the fund just as well.

[3] *Pension Benefits Act* (Ontario), O. Reg 909 78(3) at Ss. 78(3).
[4] Final Report of the Expert Panel on Sustainable Finance: Mobilizing Finance for Sustainable Growth, June 2019, Expert Panel on Sustainable Finance (pg. 21) see Recommendation 6.3.
[5] A guide to Investment governance to be read alongside our DC code of practice no. 13, June 2019, The Pensions Regulator (pg. 13). [Emphasis added]

The Proposal raises questions about whether fiduciaries would, in reality, ever have the opportunity to select between multiple investment options. It proposes the retention of the "all things being equal" test but adds new recordkeeping requirements for fiduciaries to document their analysis that multiple options were equal and that it was, therefore, appropriate to make a decision based on collateral benefits.

The "all things being equal test" was originally developed to guide the consideration of ETIs. And while the discussion in the Proposal appears to apply that test to the selection of an ETI investment, the language of the Proposal does not distinguish the application of this test from the broader discussion of ESG integration. It is therefore unclear whether it is meant to only apply to ETI investments or to ESG integrated funds.

Defined contribution plan investment options

The Proposal clarifies that ERISA fiduciaries may select "ESG-themed funds" as an investment option for a participant-directed plan but that an "ESG-themed fund" cannot be selected as the default investment option. This determination appears to be informed by confusion between ESG integration and ETIs. As noted above, CCGG members believe that integrating material E&S factors into corporate governance is a part of their fiduciary duty and reflects prudent investment decision-making.

The Department's stated rationale for prohibiting an "ESG-themed fund" from being selected as the default investment option is that it is not appropriate to select "investment funds whose objectives include non-pecuniary goals." This statement shows a fundamental misunderstanding of the purpose of ESG integration, which is to integrate all material factors into investment decision-making. In addition, it is likely to cause confusion for fiduciaries as they attempt to rationalize the Department's statements earlier in the Proposal that ESG factors are likely to have a material economic impact with its subsequent reference to ESG factors as "non-pecuniary."

Conclusion

The Proposal mischaracterizes ESG integration and fails to distinguish between ESG integration and ETIs. This is likely to lead to confusion for ERISA fiduciaries. If the Proposal is finalized in its current form, we are concerned that fiduciaries will struggle to fulfil their obligations to integrate all financially material risk-return factors while also trying to respond to the language in the Proposal that appears aimed at preventing fiduciaries from taking account of these same factors.

As institutional investors who operate globally, CCGG's members have a duty to act in the best long-term interests of their beneficiaries. Considering this fiduciary role, we believe that ESG factors may be financially material, and integrating ESG factors is core to investment decision-making. If the Proposal goes into effect, it will create unnecessary, industry-wide confusion for global asset managers. As such, we urge you to you to allow the existing guidance to remain in effect and not move forward with a final rule.

We thank you again for the opportunity to provide you with our comments. If you have any questions regarding the above, please feel free to contact our Executive Director, Catherine McCall, at cmccall@ccgg.ca or our Director of Policy Development, Sarah Neville at sneville@ccgg.ca.

Yours truly,

Marcia Moffat
Chair, Canadian Coalition for Good Governance

APPENDIX A

CCGG MEMBERS 2020

- Alberta Investment Management Corporation (AIMCo)
- Alberta Teachers' Retirement Fund (ATRF)
- Archdiocese of Toronto
- Aviva Investors Canada Inc.
- BlackRock Asset Management Canada Limited
- BMO Global Asset Management Inc.
- Burgundy Asset Management Ltd.
- Caisse de dépot et placement du Québec
- Canada Pension Plan Investment Board (CPPIB)
- Canada Post Corporation Registered Pension Plan
- CIBC Asset Management Inc.
- Colleges of Applied Arts and Technology Pension Plan (CAAT)
- Connor, Clark & Lunn Investment Management Ltd.
- Desjardins Global Asset Management
- Fiera Capital Corporation
- Forthlane Partners Inc.
- Fondation Lucie et André Chagnon
- Franklin Templeton Investments Corp.
- Galibier Capital Management Ltd.
- Healthcare of Ontario Pension Plan (HOOPP)
- Hillsdale Investment Management Inc.
- IGM Financial Inc.
- Investment Management Corporation of Ontario (IMCO)
- Industrial Alliance Investment Management Inc.
- Jarislowsky Fraser Limited
- Leith Wheeler Investment Counsel Ltd.
- Letko, Brousseau & Associates Inc.
- Lincluden Investment Management Limited
- Manulife Investment Management Limited
- NAV Canada Pension Plan
- Northwest & Ethical Investments L.P. (NEI Investments)
- Ontario Municipal Employee Retirement System (OMERS)
- Ontario Teachers' Pension Plan (OTPP)
- OPSEU Pension Trust
- PCJ Investment Counsel Ltd.
- Pension Plan of the United Church of Canada Pension Fund
- Public Sector Pension Investment Board (PSP Investments)
- QV Investors Inc.
- RBC Global Asset Management Inc.
- Régimes de retraite de la Société de transport de Montréal (STM)

- Scotia Global Asset Management
- Sionna Investment Managers Inc.
- SLC Management Canada
- State Street Global Advisors, Ltd. (SSgA)
- Summerhill Capital Management Inc.
- TD Asset Management Inc.
- Teachers’ Pension Plan Corporation of Newfoundland and Labrador
- Teachers' Retirement Allowances Fund
- UBC Investment Management Trust Inc.
- University of Toronto Asset Management Corporation (UTAM)
- Vestcor Inc.
- Workers' Compensation Board - Alberta
- York University Pension Fund