December 13, 2021

Via Electronic Filing

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210
Attention: Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights

Re: Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights (RIN 1210-AC03)

Ladies and Gentlemen:

The Investment Adviser Association (**IAA**)[1] appreciates the opportunity to comment on the Department's proposed amendments to the "Investment Duties" regulation under Title I of the Employee Retirement Income Security Act of 1974, as amended (**ERISA**).[2] For the reasons discussed below, we support the Proposed Amendments with a few recommendations.

We commend the Department for its efforts to "address uncertainties regarding aspects of the current regulation and its preamble discussion relating to the consideration of ESG issues, including climate-related financial risk, by fiduciaries in making investment and proxy voting decisions,"[3] and appreciate that the Department "makes clear that climate change and other ESG factors are often material" to these decisions.[4] We raised significant concerns about the current rule's ESG and proxy provisions when they were proposed and urged the Department to

[1] The IAA is the leading organization dedicated to advancing the interests of investment advisers. For more than 80 years, the IAA has been advocating for advisers before Congress and U.S. and global regulators, promoting best practices and providing education and resources to empower advisers to effectively serve their clients, the capital markets, and the U.S. economy. The IAA's member firms manage more than $35 trillion in assets for a wide variety of individual and institutional clients, including pension plans, trusts, mutual funds, private funds, endowments, foundations, and corporations. For more information, please visit www.investmentadviser.org.

[2] *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*, 86 FR 57272 (Oct. 14, 2021), available at https://www.govinfo.gov/content/pkg/FR-2021-10-14/pdf/2021-22263.pdf (**Proposed Amendments**).

[3] 86 FR 57276.

[4] *Id.*

withdraw both proposals.[5] We stated that the earlier preamble related to ESG investing reflected "a fundamental misunderstanding about how investment advisers and other investment professionals consider ESG factors as part of the investment process, and how ESG investments are used for the benefit of plan participants and other investors."[6] We emphasized in our comments on these proposals, and continue to believe, that "the selection of investment strategy and individual investments should be left to the judgment of investment advisers that serve as fiduciaries, making decisions in the best interest of their clients. Their decisions must be based on all relevant criteria and circumstances related to both the investor and the potential investments."[7] We believe that the Proposed Amendments would allow fiduciaries to make decisions in the best interest of their clients and we therefore support these changes, with a small number of recommendations that we believe would improve on the proposal. We also support the Department's intent to address uncertainties in this area.

In particular, we strongly support the proposed removal of the concept of "pecuniary factors" from the rule text. The Department underscores in the preamble the confusion caused by the current rule regarding whether climate change and other ESG factors may be pecuniary factors, echoing concerns raised by our members. We believe that removing this concept will make it easier for fiduciaries to consider ESG or other factors when they are material to their risk management and investment decisions.

We are also pleased that the Proposed Amendments would remove certain documentation requirements that in our view are unnecessary, as well as a prohibition in the current rule against adding or retaining a fund, product, or model portfolio as a qualified default investment alternative (**QDIA**) if it considered climate change factors. We agree with the Department's view that "[i]f a fund expressly considers climate change or other ESG factors, is financially prudent, and meets the protective standards set out in the Department's QDIA regulation…there appears to be no reason to foreclose plan fiduciaries from considering the fund as a QDIA."[8]

We also support removing the concept of "economically indistinguishable" that was included in the current rule's "tie-breaker" standard.

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[5] *See* Letter from IAA General Counsel Gail C. Bernstein, *Financial Factors in Selecting Plan Investments* (RIN 1210-AB95) (July 30, 2020), available at https://investmentadviser.org/wp-content/uploads/2021/10/IAA_Comment_Letter_-_ESG_Proposal.pdf (**IAA ESG Letter**) and Letter from IAA General Counsel Gail C. Bernstein, *Fiduciary Duties Regarding Proxy Voting and Shareholder Rights* (RIN 1210-AB91) (Oct. 5, 2020), available at https://investmentadviser.org/wp-content/uploads/2021/10/October_5__2020_-_IAA_Comments_on_DOL_Proxy_Proposal.pdf (**IAA Proxy Letter**).

[6] IAA ESG Letter at 1.

[7] IAA ESG Letter at 1-2.

[8] 86 FR 57279-57280.

Our primary recommendations relate to certain ESG-specific language in the proposed rule text and the disclosure requirement in the proposed "tie-breaker" provision. Specifically, we recommend that:

1) Certain language specific to ESG investing, including specific examples of ESG factors, be removed from the text of the rule. We believe that including such language in the rule text risks creating a rule that may not keep up with the evolving risk management and investment landscape and we recommend a more principles-based, evergreen approach.

2) The proposed disclosure requirement relating to "collateral benefit" characteristics in the "tie-breaker" provision be removed since it treats ESG factors differently from other risk-return factors and is not necessary to achieve the Department's goals.

1) The Rule Text Should Be More Principles-Based and Should Not Include Certain Text on Specific ESG Investing Factors

We recommend changes to proposed Rule 404a-1(b)(2)(ii) and proposed Rule 404a-1(b)(4) to make the rule more principles-based and less likely to become outdated over time.

Rule 404a-1(b)(2)(ii)

Rule 404a-1(b)(2)(ii) discusses considerations of factors by fiduciaries related to a portfolio, including:

(A) The composition of the portfolio with regard to diversification;
(B) The liquidity and current return of the portfolio relative to the anticipated cash flow requirements of the plan; and
(C) The projected return of the portfolio relative to the funding objectives of the plan.

The Department proposes adding to the end of (C) the following language: "which may often require an evaluation of the economic effects of climate change and other environmental, social, or governance factors on the particular investment or investment course of action."

We do not believe that the proposed rule text is necessary because the current provision discusses broad considerations of factors by fiduciaries. We believe that ESG factors are sufficiently addressed in proposed paragraph (b)(4) of Rule 404a-1, with the recommended changes that we discuss below.

Rule 404a-1(b)(4)

The Proposed Amendments would also add a new paragraph (b)(4) to Rule 404a-1 that would read: A prudent fiduciary may consider any factor in the evaluation of an investment or investment course of action that, depending on the facts and circumstances, is material to the risk-return analysis, which might include, for example:

(i) Climate change-related factors, such as a corporation's exposure to the real and potential economic effects of climate change including exposure to the physical and transitional risks of climate change and the positive or negative effect of Government regulations and policies to mitigate climate change;

(ii) Governance factors, such as those involving board composition, executive compensation, and transparency and accountability in corporate decision-making, as well as a corporation's avoidance of criminal liability and compliance with labor, employment, environmental, tax, and other applicable laws and regulations; and

(iii) Workforce practices, including the corporation's progress on workforce diversity, inclusion, and other drivers of employee hiring, promotion, and retention; its investment in training to develop its workforce's skill; equal employment opportunity; and labor relations.

We do not believe that the Department needs to include specific examples of climate change-related factors, governance factors, and workforce practices in the rule text. As the Department explains in the preamble, "Paragraph (b)(4)…would not introduce any new conditions under the prudence safe harbor in paragraph (b); its sole purpose is to provide clarification through examples."[9] We believe that it is sufficient to provide this clarification by including examples in the preamble. We are concerned that including specific examples in the rule text may be read as prescriptive, leading fiduciaries – and potentially regulators – to conclude that fiduciaries must consider the specific examples or explain why they have not. We are also concerned that inclusion of specific examples in the rule text may cause the rule to become outdated as risk management and investment considerations in these areas evolve over time. As an alternative, we recommend that the rule text read: "A prudent fiduciary may consider any factor in the evaluation of an investment or investment course of action that, depending on the facts and circumstances, is material to the risk-return analysis, which might include, for example, environmental, social, or governance factors." We believe that this language, combined with the preamble, provides sufficient clarity without raising the same concerns as the specific examples.

2) The Department Should Not Require the Disclosure of "Collateral-Benefit" Characteristics in the "Tie-Breaker" Standard

Proposed Rule 404a-1(c)(3) provides:

> If, after the analysis in paragraph (c)(2) of this section, a fiduciary prudently concludes that competing investments, or competing investment courses of action, equally serve the financial interests of the plan over the appropriate time horizon, the fiduciary is not prohibited from selecting the investment, or investment course of action, based on

[9] 84 FR 57277.

> collateral benefits other than investment returns. However, if the plan fiduciary makes such a selection in the case of a designated investment alternative for an individual account plan, the plan fiduciary must ensure that the collateral-benefit characteristic of the fund, product, or model portfolio is prominently displayed in disclosure materials provided to participants and beneficiaries. A fiduciary may not, however, accept expected reduced returns or greater risks to secure such additional benefits.

We believe that the requirement to prominently display the collateral-benefit characteristic is not necessary and may cause confusion. Any investment that is selected by the fiduciary must be prudently selected and serve the financial interest of the plan over the appropriate time horizon. In addition, the fiduciary may not accept expected reduced returns or greater risk in connection with the investment. Under these circumstances, we do not believe that the collateral-benefit disclosure is necessary.

A fund that includes ESG integration as a component of its investment strategy may be selected by a fiduciary for reasons other than or in addition to the use of ESG integration. This type of fund also may be selected for different reasons across fiduciaries, which means that the collateral-benefit disclosure may be provided by some plans and not others. The Department does not require prominent disclosure for other considerations used by fiduciaries in the investment selection process and should not depart from that approach. Investment products that have ESG investment strategies discuss those strategies in disclosures that are already available to plan participants and beneficiaries. We do not believe that the proposed collateral-benefit disclosure would provide any additional benefit to plan participants and beneficiaries and may instead cause confusion.

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We appreciate the Department's efforts to ensure that fiduciaries are able to consider all factors they determine are in the best interests of the plan, plan participants, and beneficiaries and also appreciate your consideration of our comments. We would be happy to provide any additional information that may be helpful. Please contact William Nelson, IAA Associate General Counsel, or the undersigned at (202) 293-4222 if we can be of further assistance.

Respectfully Submitted,

/s/ Gail C. Bernstein

Gail C. Bernstein
General Counsel